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Client Information Bulletin

Protecting your business in tough economic times

Economic conditions are deteriorating and a recession is predicted to occur in the major economies of the world.

Owners, managers and directors of businesses are advised to act to protect their business from a downturn and loss of demand for their products and services.

Chartered Accountants can assist businesses by providing financial skills in cash flow management and financial analysis. They can advise on:

- Management of Trade Debtors
- Maintaining positive cash flow
- Effective stock levels
- Timing of payment to creditors
- More effective finance options
- Projected cash flows and budgets
- Cost control.

Businesses are encouraged to act sooner rather than later to protect their cash flow and financial position. Contact BDH & Co to update your budgets and cash flow projections.

Home office expenses

Do you have an office at home? Do you use it for income producing purposes and incur additional running costs? If you answered 'yes' to these questions then you may be entitled to claim a deduction for 'running expenses'.

What you can claim:

- Expenses such as heating and electricity costs
- Telephone expenses
- Depreciation of office equipment. This may include computers, printers, desks, etc.

There are two ways to calculate the deduction:

- Using actual expenses
- Making calculations based on 26 cents per hour.

To claim the hourly rate you need to keep a diary for a four week period that establishes a pattern of use. A new diary must be kept for each financial year and be kept for five years.

Where there is no pattern, records must be kept throughout the year noting the duration and purpose of each home office use.

For telephone expenses there are two options:

- Business related calls can be identified from an itemised telephone account, or
- A four week diary can be used to make a reasonable estimate of the number of business calls.

Claiming 'running expenses' does not usually affect the main residence exemption however if you claim occupancy expenses such as interest, repairs, a proportion of rates and house insurance, it may affect your main residence exemption. If so it would result in the payment of capital gains tax on a portion of the sale of your property should you decide to sell.

Rental property deductions – common mistakes

The Tax Office lists the following as the most common mistakes made by owners of rental properties:

- Incorrectly claiming the cost of structural improvements as repairs instead of claiming a capital works deduction. For example, remodelling a bathroom or installing a pergola is capital in nature
- Overstating interest deductions where the loan is partly for private purposes
- Claiming the full cost of an inspection visit when the visit is combined with private purposes (such as a holiday)
- Claiming a deduction when the rental property is not genuinely available for rent - such as a holiday house
- Not proportioning deductions when the property was only available for rent for part of the year
- Incorrectly claiming the cost of the land in capital works.

Many external items are not deductible but are added to the cost base of the property. This may include soft landscaping, turfing, garden beds and irrigation pipe work. Landscape architect's fees are also ineligible for a deduction.

You may be able to claim a deduction for the cost of construction of the property. This however will depend on the date the construction commenced. You require the original cost of construction for the building, and any structural improvements. You may use a cost estimate if you are unable to obtain the original construction costs from the builder and / or previous owner.

To estimate the costs you will require a quantity surveyor's report. If you refurbish the property yourself, you are required to keep substantive documentation.

If you are unsure that you are correctly claiming your rental property deductions, make an appointment to see your Chartered Accountant.

Summer tax deductions

Now that the weather is warming up we thought it was a good time to remind you that a tax deduction is allowable for expenditure on sunscreen, sunglasses and hats for outdoor workers.

The deduction is allowable for these items where the worker is obliged to work in an environment where they are exposed to the sun. This would generally require that the exposure is for sustained periods and not just short walks between offices.

Some examples of the occupations these relate to include:

- Building and construction workers
- Truck drivers and couriers
- Farmers and forestry workers
- Other outdoor workers such as gardeners and landscapers
- Parking inspectors.

If sunglasses are required for eye protection the cost of prescription sunglasses is also deductible.

Self education costs – BEWARE

Self education expenses are deductible if the course has

sufficient connection to the taxpayer's current employment and:

- It maintains or improves the specific skills or knowledge the taxpayer requires in their current employment, or
- Results in, or is likely to result in, an increase in the taxpayer's income from their current employment.

A deduction for self-education expenses cannot be claimed for a course that does not have a sufficient connection to the taxpayer's current employment even though:

- It might be generally related to it, or
- It enables them to get new employment.

Recent cases have demonstrated how strict the Tax Office's view is of the deductibility of self education expenses.

In one case the self-education expenses were fees paid to a university in regard to studying for a degree in hotel management. The degree required 500 hours of practical experience, which was undertaken by the taxpayer at a Hotel. He continued in various roles at the hotel beyond the requisite hours.

The taxpayer argued that the course of study was relevant to his progression at the hotel but conceded that it was not a condition of his continued employment. Furthermore, pay rises were based on ability and enthusiasm for the job rather than any formal qualification.

The Tribunal found that the taxpayer had not shown that the expense was incidental and relevant to the gaining of assessable income or was a loss or outgoing incurred in gaining assessable income. Rather the expenses were concerned with the getting of work in the future.

As such no deduction was available.

Personal development course fees and life coaching programs are not generally deductible as there is insufficient nexus between the current employment and the program – the expenditure is essentially private in nature. Also if a course is too general or the skills learned are much greater than required for the current position the necessary connection between the self-education expense and employment will not be met.

If you have any questions relating to the deductibility of self education expenses contact your Chartered Accountant.

ATO's compliance program for 2008-09

The Commissioner of Taxation released the ATO's *2008-09 Compliance Program*. There does not seem to be a great deal of change from last year and the ATO continues to have a 'prevention is better than cure' approach.

The additional Government funding of \$700m, improved analytical skills, cooperation with other government agencies as well as revenue authorities overseas, will mean taxpayers will be under more scrutiny, particularly if they fall in the high wealth individual and large business categories.

Some details of the program are set out below.

Individuals

For individuals the ATO will focus on:

- Investors – looking at capital gains, rental income and financial products
- Superannuation – over-claiming deductions for superannuation contributions and excess contributions

- Work related expenses – incorrectly claimed work-related expenses
- Executives and directors – expansion of the review of the remuneration package for senior executives to include those in private and foreign-owned companies.

Micro enterprises

Micro enterprises include small businesses and self managed super funds. The main compliance issues that arise for this group include:

- Employer obligations, including the superannuation guarantee – employers who do not pay the correct superannuation guarantee contributions or do not offer choice of superannuation fund
- The cash economy – focusing regional activities, business-to-consumer transactions and micro enterprises with conspicuous consumption or multiple obligations
- International dealings – ensuring offshore income is correctly reported
- Capital gains on the sale of assets and investments – ensuring capital gains and losses are correctly reported
- Managing tax debt – risk profiling to identify small businesses that may be struggling to manage their tax payment obligations and offer them assistance
- Saving for retirement – ensuring trustees and auditors are achieving a high level of compliance.

Small to medium enterprises (SMEs)

Businesses that have an annual turnover of between \$2m and \$250m are classified as an SME by the ATO. Compliance issues for this group include:

- Increased focus on income tax compliance – the Government has provided additional funding to focus on tax compliance by SMEs particularly within the \$100m and \$250m turnover bracket
- Highly wealthy individuals – the *High Wealth Individuals Taskforce* will be expanded to monitor compliance and follow up with reviews and audits as needed
- Clarification on trust issues – the ATO will seek judicial clarification on a number of trust issues including the effectiveness of clauses in trust deeds that seek to equate trust income with trust taxable income
- Tax planning around business exits – the capital management, international transactions and tax planning around business exits, service trusts and phoenix arrangements will be examined
- Fuel tax credits – monitoring the compliance behaviour of claimants since the fuel tax credit scheme was expanded on 1 July 2008 to allow more businesses to claim a credit.

Non-profit organisations

Organisations that are classified as non-profit are many and varied. The biggest compliance issue facing them is:

- Defining what is a charity – this will focus on arrangements that seek to abuse the concessional status of charities and deductible gift recipients, including arrangements that seek to manipulate access to the GST concessions.

Serious abuse of the tax and superannuation system

There are a small number of people that deliberately abuse the tax and superannuation

system. The ATO will be looking into:

- Tackling cross-border tax crime
- Refund fraud – stolen identities used to commit tax fraud
- Tax implications of criminal activities – organised groups that accumulate wealth from illegal activities and invest it in the financial system through legitimate channels.

Through the ATO's compliance program the hope is that people understand and meet their tax and superannuation obligations at the lowest possible compliance cost to them.

First Home Saver Accounts

The First Home Saver Accounts are open for those aged between 18 and 65. Family members are allowed to contribute as well.

As part of the Saver Accounts the Government will provide a 17 per cent contribution on the first \$5,000 of individual contributions made each year. This means that anyone who contributes \$5,000 to their account will receive an \$850 deposit from the Government.

Combined with a low tax rate of 15 per cent that is equivalent to superannuation, a couple both earning average incomes, putting 10 per cent of their income into individual First Home Saver Accounts, will be able to save more than \$88,000 after five years depending on returns.

This is almost \$13,000 more than they would have saved in a standard savings account, according to the press release.

Since 1 October, the Saver Accounts have been offered by major financial institutions across the country.

For further details on First Home Saver Accounts please contact BDH & Co.

Is your business fraud proof?

Small businesses rely on loyal internal book keeping staff to process daily transactions and accounting functions.

The use of the Internet to make payments to suppliers and creditors is now becoming the normal way of paying accounts.

Does your business have adequate internal controls to prevent:

- Unauthorised payments
- Duplicate payments
- Fraudulent payment to employees
- Loss of stock by employees
- Unauthorised use of business assets.

A review of your business and accounting systems should be conducted.

Chartered Accountants have the necessary experience in accounting systems to provide advice on appropriate internal controls to:

- Safeguard assets
- Prevent and detect fraud
- Expose risks
- Ensure proper financial reporting
- Segregate duties between staff.

Businesses are encouraged to consider a review of their internal controls. Please contact BDH & Co to enable us to identify any weaknesses in your systems.

Business benefits from motivated employees

Not everyone is motivated by money.

Employee motivation can be increased if they are offered **flexibility** in:

- Re-designing their work schedules. For example a father might be allowed to work at night in order to spend time during the day with his young children
- Offering child care or elder care flexibility, where time is made up through flexible work schedules
- Job sharing for employees with family responsibilities
- Flexible Annual Leave for employees who may require extensive return trips to their homeland.

Businesses should consider ways to offer flexibility to their employees. By doing so, you will benefit from higher output and efficiency because employees are more motivated and happier in their lives.

NSW Mini-Budget

The NSW State Government handed down a mini budget on 11 November 2008 containing a number of key changes and announcements on State taxes.

The most significant change is to **defer the abolition of share transfer duty from 1 January 2009 to 1 July 2012**. This is a worrying development which may impact clients who have entered, or propose to enter, transactions based on the old timetable.

A bright note to come out of the mini budget is the Government's proposal to continue with the \$1.9b payroll tax cuts over the next four years.

For more information regarding the Mini-Budget [click here](#)

Client Profile:

Mark Chain, Smartline Personal Mortgage Adviser.

Tightening of Lender's Credit Policies.

Lenders credit policies are tightening significantly as a result of the "credit crunch" and gloomy forecasts for the local and international economies.

It is becoming increasingly difficult to finance or re-finance clients with any blemishes on their credit record. "Blemishes" particularly being mortgage and personal credit payments being made late or in arrears, and defaults listed on credit file, whether they have been paid or not.

High Loan to Valuation (LVR) products are beginning to disappear This is particularly applicable to Lo-Doc, but it is even affecting fully documented applications. ANZ has been one of the first players to move, withdrawing Lo-Doc products where the LVR is >60%, and full doc lending where LVR is over 90%. The policy on re-financing and consolidating debt, and line of credit or "cash out" is also becoming much more restrictive. Up until recently most of the major lenders have been happy to re-finance and consolidate finance without to high LVRs to borrows with good credit history with very little trouble. There have been several lenders prepared to finance borrowers who were considered less than "prime". These borrowers may have paid a premium on their interest rate with these second tier lenders as their loans were "rated-for-risk" but at least these alternatives were available. The number of lenders now playing in these spaces is shrinking rapidly.

The reason for this communication is to let you know that given these changes if you do have clients who may be affected by any of the above changes, or are considering re-financing debts to put them into a position to ride out what may be tough times ahead, I would advise them to consider doing this sooner rather than later. This is particularly applicable to any clients who may fit into the Low Doc category, and clients who may be at risk of not being able to meet their present commitments if the economic situation deteriorates further.

BDH & Co news

Welcome to our new Practice Manager, Linda Mikaelian who comes to us with 8 years of experience within the industry. Linda is in charge of all facets of our administration

In January we look forward to welcoming our new Client Manager Stuart Reid to our team. He brings 20 years of extensive accounting and taxation knowledge having started his career at Ernst & Young.

Welcome also to our new accountants Ivy Chen and Michelle Townsend.

Christmas parties and FBT

Staff Christmas parties are likely to feel the heat of the tough economic times so it's never been more important for employers to consider the tax-inclusive cost of their corporate entertainment.

It is important to remember the fringe benefits tax (FBT) implications of your annual Christmas party. By planning ahead you can avoid unforeseen tax obligations

To work out the FBT you will need to think about where the function is held, who attends, what is provided, how much it costs and the income tax status of the employer.

An increase in the minor benefits threshold means that 'infrequent' corporate entertainment benefits valued individually at less than \$300 per head can be exempt from FBT in many situations.

Importantly for employers who allow their staff to bring family members to end of year functions, the Australian Taxation Office (ATO) has confirmed that each benefit received by each family member is assessed separately against the \$300 cap. Food and drink consumed at the party is a separate benefit to the take-home gift of a hamper or box of chocolates. However the catch is that the overall benefit value received by the employee and their family should still be 'moderate' in order for the FBT exemption to apply.

It is also important to note that the gift, providing it is not entertainment in itself (such as tickets to a concert), will be a deductible expense to the employer whilst the food and drink is not tax deductible if it is exempt from FBT.

Christmas break

Our office will be closed from midday on Friday 19 December 2008 and will re-open on Monday 5 January 2009.

DISCLAIMER: The contents of this publication are general in nature and we accept no responsibility for persons acting on information contained herein.