

CONTENTS:

- 1 • Loans from Private Companies Division 7A rules.
- 4 • Proposed changes to existing Division 7A rules.
- 5 • Is your business car available for private use?
- 6 • Do you import goods and services?
 - 4 ways to avoid simple mistakes with GST reporting.
- 7 • Do you hold vacant land? Your expenses may no longer be deductible.
- 8 • New tax reporting requirements for couriers and cleaners.
- 9 • Key tax dates.



Borrowing from your business? Find out how you might be triggering the Division 7A rules & the ATO's proposed changes to these rules

Are you a shareholder or associate of a private company?

Does your company have a distributable surplus at the end of the income year?

Do you borrow or use business assets for your personal use and enjoyment?

If you answered yes to any of these questions, then the legislative provisions of Division 7A of the *Income Tax Assessment Act 1936* could potentially affect you.

What is Division 7A?

Division 7A is essentially designed to prevent shareholders and their associates from using private company profits without paying tax at their marginal tax rates.

With the highest individual marginal rate sitting at 45% (47% with the Medicare levy), opportunistic tax planners might attempt to structure their tax affairs to access the lower company tax rate of either 30% or 27.5%. However, the anti-avoidance provisions of Division 7A operate to prevent this kind of activity.

Division 7A rules determine what kinds of benefits to shareholders and their associates are treated like unfranked dividends and therefore subject to personal income tax without any credit for company tax paid.

Does Division 7A apply to me?

You may potentially be affected by Division 7A if your group structure includes a:

- private company
- non-resident private company

- closely-held corporate limited partnership
- trust
- interposed entity
- shareholder or associates of a shareholder.

Note! The term 'associate' in this case extends to a shareholder's spouse, child, relative or trustee of a trust under which the shareholder benefits.

What transactions does Division 7A apply to?

Division 7A can apply to a broad range of transactions, including:

- loans
- payments
- debt forgiveness
- payments or loans where a trust has an unpaid present entitlement (UPE)
- payments and loans through interposed entities
- private use of company assets
- transfer of company assets
- gifts
- guarantees.

Note! An unpaid present entitlement (UPE) is a payment or distribution that you are entitled to but have not been paid.

When does Division 7A not apply?

Division 7A does *not* apply to:

- payments to a shareholder or associate in his or her capacity as an employee. In such situations, fringe benefits tax (FBT) may apply rather than Division 7A.
- amounts that are assessable to the shareholder or their associate under other parts of the income tax law, such as normal dividends or director's fees.
- a payment or benefit that is potentially subject to Division 7A if it is repaid or converted into a Division 7A complying loan by the company's lodgement day for the income year in which the payment or benefit occurs.

What is a complying loan?

A loan is a complying loan if the loan has satisfied the minimum interest charge and maximum term requirement and is made or put under a written agreement before the private company's lodgement day (currently 7 or 25 years depending on the terms).

Note!

- Complying loans will have tax implications for the company and shareholder (eg the taxation of interest will need to be considered).

When is Division 7A triggered?

Division 7A can be triggered if:

- a private company provides a payment or benefit to a shareholder or associate; or
- a trust has allocated income to a private company but has not actually paid it, and the trust has provided a payment or benefit to the company's shareholder or their associate.

Note!

- A payment or other benefit provided by a private company to a shareholder or their associate can be treated as a dividend for income tax purposes under Division 7A even if the participants treat it as some other form of transaction such as a loan, advance, gift or writing off a debt.
- Division 7A can also apply when a private company provides a payment or benefit to a shareholder or associate through another entity.

What is considered a payment by a private company?

A payment may include:

- the provision of an asset for use by a shareholder or their associate (other than a transfer of property)
- when a company asset is available for use by a shareholder or their associate to the exclusion of the company, but not where there is a general entitlement to use the company's assets
- a right to use assets under a licence or lease, but which does not involve a transfer of property. It does not matter when the right to use the asset is granted.

Note! An asset may also be available for use by a shareholder or their associate without a formal agreement or where there is no actual use.

When is a payment treated as a dividend?

A private company may be taken to pay a dividend to an entity at the end of the company's income year if it pays an amount to the entity during the year:

- when the entity is a shareholder or an associate of a shareholder of the company; or

- a reasonable person would conclude that the payment was made because the entity was a shareholder or an associate of a shareholder at some time.

Note!

- However, the total of all dividends a private company is taken to pay under Division 7A is limited to its distributable surplus for that income year.
- Division 7A applies even if the participants treat the payment or benefit as some other form of transaction such as a loan, advance, gift or writing off a debt.

What is considered a loan by a private company?

A loan may include:

- an advance of money
- a provision of credit or any other form of financial accommodation
- a payment for a shareholder or their associate, on their account, on their behalf, or at their request if they have an obligation to repay the amount
- a transaction (whatever its terms or form) that is the same as a loan of money.

When is a loan treated as a dividend?

A private company may be taken to pay a dividend to an entity at the end of the company's income year, if it loans an amount to an entity during the year:

- when the entity is a shareholder or an associate of a shareholder of the company; or
- a reasonable person would conclude that the payment was made because the entity was a shareholder or an associate of a shareholder at some time.

Transactions that will create deemed dividends

Certain transactions between a private company and shareholder or associate are deemed to create an unfranked dividend assessable to the shareholder or associate.

Note!

- The shareholder or associate need not be a shareholder or associate at the time the transaction occurred, as long as a reasonable person would conclude that the transaction occurred because the person was a shareholder or associate **at some time**.

Payments treated as deemed dividends

These include:

- an amount paid or credited to the shareholder or associate
- an amount paid or credited on behalf of, or for the benefit of, the shareholder or associate
- a transfer of property to the shareholder or associate.

Case study 1

Matt owns shares in a private company, ABC Pty Ltd. On 30 June 2017, ABC Pty Ltd makes a payment of \$5,000 to Matt's mother, Norma.

Norma is not an employee of ABC Pty Ltd and she is not an associate of an employee of the company. However, she is an associate of Matt.

The payment will be taken to be an unfranked dividend paid to Norma and she must include the \$5,000 as assessable income on her 2016-17 tax return.

Loans treated as deemed dividends

These include:

- loans made to a shareholder or an associate of a shareholder
- loans that are not fully repaid before the private company's lodgement day for the year when the loan is made. A private company's lodgement day is the earlier of the due date for lodgement, or the actual date of lodgement of the private company's income tax return for the income year
- loans that are not excluded specifically by other sections of Division 7A.

Case study 2

Charlotte is a shareholder in a private company, XYZ Pty Ltd. Charlotte's credit card bills, totalling \$10,000, are paid with company cheques throughout the income year and debited to her loan account. Interest is not payable on the balance of the loan account.

If Charlotte repays the \$10,000 to XYZ Pty Ltd prior to the earlier of lodgement of the company's income tax return or its due date for lodgement, no amount should be treated as a deemed dividend under Division 7A. If she does not repay all of the \$10,000, an unfranked dividend may arise.

There may be other tax implications for Charlotte and the company.

Consequences of triggering Division 7A

Generally, if Division 7A has been triggered, the shareholder would be deemed to have received a dividend equal to the amount of the payment, loan or benefit received.

[What if I borrow an asset from my company for personal use?](#)

Case study 3

Bruce is a shareholder of a private company that owns a luxury yacht. Bruce does not have a formal agreement with the company in relation to the yacht, however, he borrows the yacht and takes it out every second weekend. Bruce keeps the yacht at the company's business premises but takes the key home. Bruce stores his personal items on the yacht.

Bruce's fortnightly use of the yacht is effectively treated like a payment under Division 7A. The availability of the yacht for Bruce's use is also subject to Division 7A because the yacht is not readily available for use by the company.

The company would need to arrange with Bruce to get the key and for the removal of his personal items before using the yacht. The asset is available for Bruce's use to the exclusion of the company.

Case study 4

Nicole is a shareholder of a private company that owns a city apartment. The apartment is generally available for rent. However, Nicole asks the company not to rent the apartment out for a week so that she and her family can borrow it over a long weekend. Nicole's use of the apartment may be a payment for the purposes of Division 7A.

[What if my company provides a loan to a shareholder?](#)

Case study 5

Conway Pty Ltd loans \$20,000 to Angie, a shareholder of Conway Pty Ltd. The money is loaned to Angie on the basis that she pays it back when she can. The \$20,000 is a loan from Conway Pty Ltd to Angie because it is an advance of money. Consequently, Division 7A may apply.

Case study 6

Wayne Pty Ltd provides \$10,000 to Bob, a shareholder of Wayne Pty Ltd, by way of a promissory note. The note places no obligation on Bob to repay the amount. The \$10,000 is a loan from Wayne Pty Ltd to Bob because it is a form of financial accommodation. Consequently, Division 7A may apply.

[What if my company provides a car for use by a shareholder?](#)

Case study 7

Carla is a shareholder of a private company that owns five cars for company use. Shareholders and their associates have general permission to use the cars on weekends if they are not being used for company business. Carla regularly takes one of the cars home.

Carla's use of the car that she takes home will be subject to Division 7A. This will include driving the car (actual use) and the availability of the car for her use to the exclusion of the company, such as when it is parked at home, or at a restaurant that Carla is visiting.

Although Carla may have general permission to use all five of the cars, she does not use all of them for the purposes of Division 7A. The four cars that Carla leaves at the company premises are available for the company to loan to another shareholder, employee, customer, or other party. That is, these cars are not available to Carla to the exclusion of the company.

Note! Providing cars or other residual benefits (eg a holiday house) to shareholders may be caught by FBT instead of Division 7A. Please contact your Blaze Acumen tax adviser for further information on FBT implications.

Government's proposed changes to the existing Division 7A Rules

In October, the Government released for public consultation a paper proposing changes to Division 7A.

The proposed changes to the legislation are intended to apply from **1 July 2019** and may impact you if you are a company owner, a shareholder of a private company or an associate of a shareholder.

[What do the changes mean?](#)

The proposed changes are intended to make it easier for businesses to comply with Division 7A. A summary of the proposed amendments is set out below:

- A self-correction mechanism to assist taxpayers to promptly rectify breaches of Division 7A.
- Clarification that unpaid present entitlements (UPEs) come within the scope of Division 7A.
- Simplified loan rules as follows:
 1. As mentioned above, complying loans are not treated as dividends under Division 7A. Under the current law, there are 2 types of

- complying loans (7 years for an unsecured loan or 25 years for a secured loan). Under the proposed changes, there will be one single 10-year model.
2. Annual benchmark interest rate to be the variable interest rate most recently published by the Reserve Bank of Australia prior to the start of each income year.
 3. No requirement for a formal written agreement, however written or electronic evidence showing that a loan was entered into and its terms must exist by the lodgement date of company's tax return.
 4. Minimum yearly repayment amount must consist of both principal and interest based on the benchmark interest rate.
 5. Interest to be calculated for the full income year, regardless of when the repayment is made during the year (apart from Year 1). If the loan is repaid early, interest will not be charged for the remainder of the agreed loan term.
- For existing loans, there are transitional rules that will be introduced as follows:
 1. Complying 7-year loans in existence as at 30 June 2019 must comply with new proposed loan model above and new benchmark interest rate but will retain existing outstanding term.
 2. Complying 25-year loans in existence as at 30 June 2019 will be exempt from the majority of changes until 30 June 2021. However, interest rate payable during this period must equal or exceed the new benchmark interest rate. On 30 June 2021, the outstanding value of loan will give rise to a deemed dividend unless a complying loan agreement is put in place prior to the lodgement day of the 2021 company tax return.
 3. Pre-1997 loans pre-date the current Division 7A rules. However, under the proposed new rules, such loans will be subject to Division 7A. There will be a two-year transitional period to repay the loan before 30 June 2021. After that date, the loan will need to be placed on a complying loan agreement by the lodgement day of the 2021 company tax return with the first repayment being due in the 2022 financial year. Otherwise, it will be treated as a dividend in the 2021 financial year.
 - As mentioned above, the amount of a deemed dividend under Division 7A is currently limited by the distributable surplus of the private company providing the benefit. Under the proposed amendments, the concept of distributable surplus will be removed so that the amount that can be deemed a dividend will be based on the entire value of the benefit that was extracted from the company.

- It is also proposed that the limited period of review for the ATO to revise assessments where Division 7A has been triggered will be replaced with a review period of 14 years. This is 14 years after the end of the income year in which the loan, payment or debt forgiveness gave rise or would have given rise to a deemed dividend. This will apply from 1 July 2019.

What next?

Division 7A is always on the ATO's radar. Contact your Blaze Acumen tax adviser if you have been involved in transactions that you think may trigger Division 7A and if you would like to discuss further.



Is your business car available for private use?

A car fringe benefit occurs when your business owns or leases a car and makes it available for your employees' private travel. In this case, directors might also be employees.

Note! Generally, travel to and from work is private use of a vehicle.

For fringe benefits tax (FBT) purposes, a car is any of the following:

- a sedan or station wagon
- any other goods-carrying vehicle with a carrying capacity of less than one tonne – eg a panel van or utility (including four-wheel drive vehicles)
- any other passenger-carrying vehicle designed to carry fewer than nine passengers.

If the vehicle provided does not meet the definition of a car, and your employee has private use of the vehicle, the right to use the vehicle may be a residual fringe benefit.

Providing car fringe benefits

Some examples of providing a car fringe benefit include:

- employees using the car for private travel, such as travel between work and home;
- garaging the car at or near your employees' home, which makes it available for private use – even if it is not used privately.

Note!

- If a car is garaged at or near your employee's home, even if only for security reasons, it is taken to be available for their private use regardless of whether or not they have permission to use the car privately.
- Similarly, where the place of employment and residence are the same, the car is taken to be available for the private use of the employee.

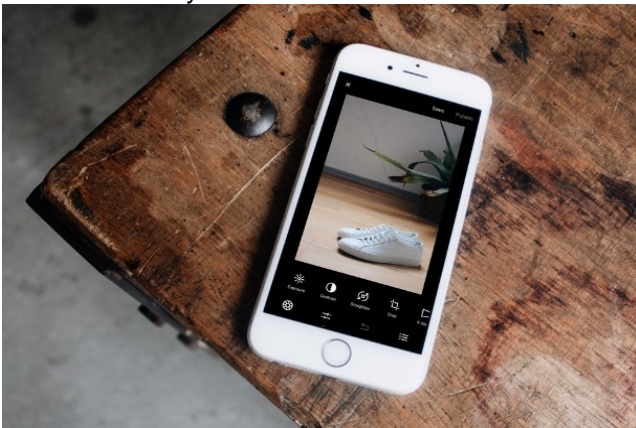
Working out the taxable value of a car fringe benefit

To calculate a car fringe benefit, as an employer, you must work out the taxable value of the benefit using either:

- the statutory formula method (based on the car's cost price)
- the operating cost method (based on the costs of operating the car).

You can choose whichever method yields the lowest taxable value, regardless of which method you used in a previous year.

Note! If you have not kept the required documentation for the operating cost method (eg log books), you must use the statutory formula method.



Do you import goods and services?

The deferred GST scheme may be of interest to you if you import goods and services. The deferred GST (DGST) scheme allows you to defer payment of GST on all taxable importations into Australia. This is subject to eligibility requirements.

Note!

- You need approval to participate in the DGST scheme, which you can get by applying to the ATO.

Am I eligible to participate in the deferred GST scheme?

To be eligible to participate in the deferred GST scheme, you must:

- have an ABN
- be registered for GST (you can register for GST and apply for an ABN on the one form if you don't already have an ABN)
- lodge your activity statements online
- lodge your activity statements monthly (if you are lodging quarterly, you can elect to lodge monthly)
- make your activity statement payments electronically.

When am I not eligible?

You may not be eligible if:

- you are not up to date with your tax returns or payments – this includes members of GST groups, branches and joint ventures (see GST group members and representatives)
- you or anyone relevant to the application has, in the past three years, been convicted or penalised by a court for specific offences.

4 ways to avoid simple mistakes with GST reporting

Businesses can make simple mistakes reporting their GST. To avoid errors, keep an eye out for the following common errors and ensure you report correctly.

1. Transposition and calculation errors

Transposition errors can occur when an amount is manually input. These errors can be easily eliminated by double checking all figures and calculations before submitting your BAS.

2. No tax invoices

You need to keep tax invoices to claim GST credits you have claimed on business related purchases.

3. Transaction classification

Make sure you check what's GST applicable. Transactions involving food may be GST applicable.

4. Accounting systems

Check your systems as one coding error can classify several transactions incorrectly.

If you find you've made a mistake on a previous return, you can:

- correct the error on a later activity statement – if you meet certain requirements;
- lodge an amendment; or
- contact your Blaze Acumen tax adviser or the ATO for advice.



Do you hold vacant land? Your expenses may no longer be deductible

Are you a property owner sitting on vacant land? The Government has recently released draft legislation to deny deductions for certain expenses associated with holding vacant land.

The current law

The current law allows you to claim the costs of holding vacant land if it is held for the purpose of gaining or producing assessable income or carrying on a business for the purpose of gaining such income.

The proposed law

From 1 July 2019, the proposed law will limit deductions for expenses associated with holding vacant land.

The proposed rules do not apply to expenses associated with holding vacant land that is used by the owner or a related entity to carry on a business. For example, the measure will not apply to a business of primary production or to a property developer that is carrying on a business and is holding land for the purpose of that business.

The proposed rules also do not apply to corporate tax entities, managed investment trusts, public unit trusts and unit trusts.

Why the changes?

This proposed measure was announced in the 2018-19 Federal Budget, and addresses concerns that deductions are being improperly claimed for holding vacant land where the land is not genuinely held for the purpose of earning assessable income.

What is vacant land?

Land is vacant if there is no building or other structure on the land that is substantial and permanent in nature and in use or ready for use.

In this context, land does not have to refer to the whole of the land on a property title but could refer to part of the land on a property title. For example, if a property title includes two areas of land, one containing a factory and the other undeveloped, the part of the property title containing the factory has ceased to be vacant land, while the undeveloped area remains vacant land.

What does 'substantive' in nature mean?

To be substantive, a building or structure needs to be:

- substantial in size; and
- have an independent purpose or function (not ancillary in nature to other structures or proposed structures on the land such as is the case for retaining walls or fences).

Case study

Deborah owns a block of land. She intends to eventually build a rental property on the land. However, while the block of land is fenced and has a large retaining wall, it currently does not contain any substantial or permanent building or other structure.

As the property does not have a substantial permanent building or structure on it, it is vacant land and Deborah cannot deduct any holding costs she may incur in relation to the land.

What if land does not have a substantive permanent building or structure?

There are many genuine commercial reasons land may not have a substantive permanent building or structure (eg holding yards for goods that are awaiting transport or customs clearance, parking

areas for trucks/buses for a logistics company) as not all business operations require structures and buildings.

If the owner of land used for these purposes is a private trust or individual who does not have the requisite connection to the business being carried on (especially where there is a genuine commercial lease to an unrelated third party), all deductions will be denied even though the "vacant land" is an essential part of the business activities.

Tip! Speak to your Blaze Acumen tax adviser to find out more about how these proposed changes may affect you or your business.



New tax reporting requirements for couriers and cleaners

If you own a business that provides cleaning or courier services (even if it's only part of the services provided), you now need to lodge a taxable payments annual report (TPAR) each year to tell the ATO about your payments to contractors.

What is a TPAR?

The TPAR tells the ATO about payments that are made to contractors for providing services.

Contractors can include subcontractors, consultants and independent contractors.

The details you need to report about each contractor are generally found on the invoice you should have received from them. This includes:

- their Australian business number (ABN), where known
- their name and address
- gross amount you paid to them for the financial year (including any GST).

The ATO will use this information to make sure the contractors you pay are reporting all their income and meeting their tax obligations.

TPAR now extended to couriers and cleaners

New laws were recently passed in Parliament to extend the taxable payments reporting system to include businesses providing:

- cleaning services – to report payments to contractors for cleaning services
- courier services – to report payments to contractors for courier services.

What are courier services?

Courier services include:

- activities where items or goods are collected from, and/or delivered to, any place in Australia using a variety of methods including by car, truck, station wagon, van, ute, motorcycle, motorised scooter, drones, bicycle or other non-powered means of transport, or on foot;
- door-to-door services that are often used for specialty deliveries or for small parcels or packages. Goods commonly transported using courier services include parcels, packages, letters and food.

Note! If you sell goods and you provide the option of a delivery service, you are supplying a courier service unless the customer doesn't have the option to obtain the goods from you any other way.

Courier services don't include:

- delivery of goods your business provides where delivery is the only method your clients or customers have of receiving the goods
- passenger transport services – for example, buses and taxis
- freight transport – the transportation of bulk or large quantities of items, goods or commodities via rail, sea, air, or road (usually heavy vehicle trucks or larger vehicles) from one location to another.

What are cleaning services?

Cleaning services include (but are not limited to) any of the following activities undertaken on a building, residence, structure, place, surface, transport/vehicle, industrial machinery or equipment and for events:

- interior cleaning
- exterior cleaning (except sandblasting)
- carpet cleaning
- chimney cleaning
- gutter cleaning

- road sweeping and street cleaning
- swimming pool cleaning
- park and park facilities cleaning.

Note! If your business provides mixed services, not just courier or cleaning services, you may need to lodge a TPAR if the payments you receive for either courier or cleaning services make up 10% or more of your total GST turnover.

When do you need to lodge a TPAR?

If your business needs to lodge a TPAR, you will need to lodge it by 28 August 2019 for payments made to contractors between 1 July 2018 and 30 June 2019.



Key tax dates

Date	Obligation
21 Nov 2018	Oct monthly BAS due
26 Nov 2018	Sept quarter BAS due (tax agent concessional due date)
28 Nov 2018	Sep quarter SG charge statement due
1 Dec 2018	Tax payment due for large/medium companies
21 Dec 2018	Nov monthly BAS due
15 Jan 2019	Lodgement due date for taxable large/medium taxpayer in the immediate prior year
21 Jan 2019	Dec monthly BAS due
28 Jan 2019	Dec quarter SG due
4 Feb 2019	Feb fuel tax credit rates change
21 Feb 2019	Jan monthly BAS due
28 Feb 2019	<ul style="list-style-type: none"> • Dec quarterly BAS due • Dec quarter SGC statement due • Dec quarter PAYG instalment due

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