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December 2021

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# If Santa was an Australian tax resident

A lighter look at the complexity of Australian taxation laws and the year that has been.

Dear Mr Claus,

Thank you for the opportunity to provide strategic business, tax and compliance advice for your operation. We're pleased you have initiated this advice as the Australian Taxation Office (ATO) has instigated a number or reviews that may impact on your operations and your team, and its relationship to contractors. Some of these issues have been exacerbated by the pandemic.

We have identified a number of areas of concern as a starting point for further discussions. These include:

### Western Australia border closures and 'elf' contractors

We understand that the hard  
*Continued over...*

## Merry Christmas

If someone asked you what your ideal day is, what would you answer?

This year was a year where many of us have taken stock of what is important, refined our goals, and focussed on closing the gap between our ideal and our reality.

We'll look forward to working with you again in 2022 and helping you to close that gap!

On behalf of all the team we wish you a safe and happy Christmas.

Office closure - 12pm, 24 December 2021 to 10 January 2022.

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**Note:** The material and contents provided in this publication are informative in nature only. It is not intended to be advice and you should not act specifically on the basis of this information alone. If expert assistance is required, professional advice should be obtained.

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border closure in Western Australia has created a series of logistical challenges for your delivery schedule. The very specific timing and nature of the gift delivery mean that, while existing vaccinated team members can enter Western Australia on a G2G pass, it is not possible to fulfil the 14 day quarantine requirements. To manage the Christmas Eve requirements, you have instigated a relationship with a local contractor.

We have several concerns about this relationship. Leaving aside our capacity to verify the existence of the elf in question, the elf appears to be an individual and not operating as a logistics specialist – no ABN is on record. Based on the information you have provided to us it appears that the elf is likely to be considered an employee of yours regardless of what your performance contract specifies. As such, you will be liable for superannuation guarantee and tax will need to be withheld from any payment to them. We refer you to the ATO's [contractor checklist](#).

The nature of the payment to the elf is also of concern. "Goodwill to all men" is an intangible asset and as such, we may need to bring in a specialist valuer. This asset has been a globally scare commodity over the last few years and while supply has improved dramatically since January 2021 and spikes in December each year, the normalised value is likely to be significant.

### **Business structure viability**

The fact that you run a global enterprise that generates no income or profit but 'gifts' millions of toys each year produced by your offshore factory, has significant brand value, is represented extensively in merchandise, your spokespeople are employed by shopping centres all around the world, but you have never lodged a tax return or paid tax in Australia, is likely to trigger an ATO investigation. There is also a risk that the Serious Financial Crime Taskforce might become involved.

As discussed, we do not believe that the "it's magic" argument will suffice in the event of an investigation. The argument has been tested previously with the ATO to no avail.

Your enterprise's lack of structure also means that you are missing out on significant benefits. For example, tax deductions might be available for expenses you incur. A number of significant changes were made in recent years enabling businesses to immediately deduct the cost of assets used to produce income.

### **Expenses incurred**

Your flying reindeers are likely to be considered beasts of burden and as such can be depreciated as plant. However, a deduction is only available to the extent that the reindeer are used to produce income that is taxable in Australia.

At present, you do not make any claim for expenses incurred during your Christmas Eve deliveries. While we understand food – cookies, reindeer food, glasses of milk and the occasional tippie of scotch – is provided free by the world's children, there are likely to be other expenses that you incur. The cost of your uniform, dry-cleaning (removing chimney soot), and postage, to name a few.

### **Research & Development**

We understand that the 'flying sleigh' was developed in your workshop and the technology has developed markedly over the years. In addition, your purpose built 'naughty or nice' technology system is unique (we note our concerns about potential privacy breaches and a lack of an opt in/opt out system; I know you have been watching the detrimental brand impact on several social media outlets). If incorporated, there is a potential to access the R&D tax incentive that provides entities with a turnover of less than \$20m a refundable tax credit of your corporate tax rate plus 18.5%. The value of the tax offset is lower for companies with a turnover of \$20m or more.

*Continued page 6...*



# The top Christmas tax questions

Every year, we are asked about the tax impact of various Christmas or holiday related gestures. Here are our top issues:

## Staff gifts

The key to Christmas presents for your team is to keep the gift spontaneous, ad hoc, and from a tax perspective, below \$300 per person. \$300 is the minor benefit threshold for Fringe Benefits Tax (FBT) so anything at or above this level will mean that your Christmas generosity will result in a gift to the Tax Office as well. To qualify as a minor benefit, the gifts also have to be ad hoc (no ongoing gym membership payments or giving the same person regular gift vouchers amounting to \$300 or more).

A question we often get is what is the tax impact if you give your team say a hamper and a gift card? The good news is that the tax rules treat each item (the hamper and the gift card) separately. FBT won't necessarily apply as long as the value of each item is less than \$300. However, the minor benefits exemption is a bit more complex than this. For example, you need to look at the total value of similar benefits provided to the employee across the FBT year etc.

If you are planning to provide your team with a cash bonus rather than a gift voucher or other item of property, then this will be taxed in much the same way as salary and wages. A cash

bonus at Christmas is not a gift; it's still income for the employee regardless of the intent. A PAYG withholding obligation will be triggered and the ATO's view is that the bonus will also be treated as ordinary time earnings which means that it will be subject to the superannuation guarantee provisions unless it relates solely to overtime that was worked by the employee.

## The staff Christmas Party

If you really want to avoid tax on your work Christmas party then host it in your office on a work day (COVID rules allowing!). This way, Fringe Benefits Tax is unlikely to apply regardless of how much you spend per person. Also, taxi travel that starts or finishes at an employee's place of work is also exempt from FBT. So, if you have a few team members that need to be loaded into a taxi after overindulging in Christmas cheer, the ride home is exempt from FBT.

If your work Christmas party is out of the office, keep the cost of your celebrations below \$300 per person. This way, you won't generally pay FBT because anything below \$300 per person is a minor benefit and exempt.

If the party is not held on your business premises, then the taxi travel is taken to be a separate benefit from the party itself and any Christmas gifts you have provided. In theory, this means that if the cost of each item per person is below \$300 then the gift, party and taxi travel can all be FBT free. However, the total cost of all benefits provided to the employees needs to be considered in determining whether the benefits are minor.

The trade-off to this is that if the costs associated with hosting the party are not subject to FBT then it would be difficult to claim a tax deduction or GST credits for the expenses.

If your business hosts slightly more extravagant parties and goes above the \$300 per person minor benefit limit, you will generally pay FBT but you can also claim a tax deduction and GST credits for the cost of the event.

### Client gifts

Few of us have that much time in the diary for pre-Christmas entertainment so why not give a gift instead? In addition to a few extra hours saved and a lot less calories to work-off (most of us are still struggling post lock down), there is also a tax benefit. As long as the gift you give to the client is given for relationship building with the expectation that the client will keep giving you work (that is, there is a link between the gift and revenue generation), then the gift is generally tax deductible as long as it doesn't involve entertainment.

Entertaining your clients at Christmas is not tax deductible. If you take them out to a nice restaurant, to a show, or any other form of entertainment, then you can't claim it as a deductible business expense and you can't claim the GST credits either. It's goodwill to all men but not much more.

### Charitable gift giving

The safest way to ensure that you or your business can claim a deduction for the full amount of the donation is to give cash to an organisation that is classified as a deductible gift

recipient (DGR). And, the charities love it as they don't have to spend any of their precious resources to receive it.

There are a few rules that make the difference between whether you will or won't receive a tax deduction.


- The charity must be a DGR. You can find the list of DGRs on the [Australian Business Register](#).
- If you buy any form of merchandise for the 'donation' – biscuits, teddies, balls or you buy something at an auction – then it's generally not deductible (the rules become more complex in this area). Your donation needs to be a gift, not an exchange for something material. Buying a goat or funding a child's education in the third world is generally ok because you are generally donating an amount equivalent to the cause rather than directly funding that thing.
- The tax deduction for charitable giving over \$2 goes to the person or entity whose name is on the receipt.

If your business is making a donation on behalf of someone else, such as a client or that friend 'who has everything', it will depend on how the donation is structured. The tax rules generally ensure that the deduction is available to the individual or entity who actually makes the gift or contribution. Having receipts issued in someone else's name can make this more complex.

## Quote of the month

“You can't change conditions. Just the way you deal with them.”

Jessica Watson, sailor



# The 'Backpacker Tax' and the High Court

## The High Court has ruled that the 'backpacker tax' is discriminatory. We look at the impact.

Since 2017, the 'backpacker tax' has taxed the first dollar of income a backpacker earns in Australia - regardless of their residency status - at the working holiday maker tax rate of 15% up to:

- \$37,000 in an income year for 2019-20 and earlier income years
- \$45,000 for 2020-21 and later income years.

When the tax was introduced in 2017, a backpacker would pay a maximum of \$5,500 in tax on the first \$37,000 of income. However, an Australian national performing the same work would have a maximum tax liability of \$3,572.

In this case, Catherine Addy, a UK national working in Australia since 2015, contested her 2017 amended income tax assessment which imposed the backpacker tax on the grounds that it contravened the Double Tax Agreement (DTA) with the United Kingdom. Article 25(1) of the DTA seeks to ensure that nationals of the UK are not subject to "other or more burdensome" taxation than is imposed on Australian nationals "in the same circumstances, in particular with respect to residence". Ms Addy was a tax resident of Australia.

The ATO did not accept Ms Addy's argument and she launched action in the Federal Court. The Federal Court initially upheld the Tax Commissioner's position. However, Ms Addy

appealed the decision and the High Court overturned the Federal Court's decision. The question for the Court was whether a more burdensome tax was imposed on Ms Addy owing to her nationality. The short answer was "yes".

The High Court decision found that the backpacker tax is inconsistent with the non-discrimination clause in the UK DTA. That is, the flat working holiday maker tax rate is not valid in some situations. Non-discrimination clauses that are similar to the one in the UK DTA can also be found in the DTAs with Chile, Finland, Japan, Norway, Turkey, Germany and Israel.

## So, what does this mean?

Some individuals who have been taxed under the backpacker tax rules may be able to obtain a tax refund from the ATO. However, there are a couple of key points to bear in mind:

- The decision only impacts those classified as an Australian tax resident. Many individuals who are living or working in Australia on a working holiday visa will be classified as non-residents, in which case this decision will be less relevant.
- The decision is only likely to be relevant to individuals who are a citizen/national of a country that has a DTA with Australia containing a non-discrimination clause similar to the clause found in the UK DTA.

# 2022: The year ahead

2021 was to be the year we returned to a post-COVID normal however the pandemic has fundamentally changed the way many of us operate in our personal and work lives. Here is some of what we can expect in 2022:

## Federal Election

The Federal election will be held between March and May 2022. Annoying text messages, robo messages and advertising are on their way!

## Federal Budget in March

The timing of the election will bring the Federal Budget forward to March 2022. It's an election year; expect many of the productivity based tax concessions to be extended.

## Lock-in digital gains

[McKinsey & Company](#) reports that consumer digital adoption rates accelerated dramatically during the pandemic.

- Many sectors will lock in the digital gains they made. Some, however, will see a decline in digital sales as consumers are no longer forced to shop online – groceries for example.
- To lock in the gains of digitalisation, consumers expect trust, end-to-end digital service (from start to after sales service), and an improved online experience.
- Forced online adoption has changed the consumption habits of an older and wealthier portion of the market. The average age of online users in the McKinsey Global Sentiment Survey increased by around 3 years and spend around 4% more.
- Coming off a lower base, developing nations have experienced a much higher growth in digital adoption than developed nations; evening out global access.

## Going green

Business and consumers will be expected to be mindful of their carbon footprint. A wasteful process is likely to diminish consumer appeal.

## If Santa was a tax resident

*Continued from page 2.*

The technology developed in your workshop, if patented and commercialised, could revolutionise logistics and put a whole new meaning to same day delivery. We are certain that Australia Post in particular, would be very interested in entering into discussions with you.

## Global taxation

There have been significant shifts over recent years to ensure that multinational enterprises pay tax in the country where they generate their income. The increase of digitalisation has only exacerbated the issue. While not earning an income, your enterprise operates globally with a workshop located in the North Pole and delivers to clients across the globe.

Representation in a particular country may also be enough to make your operation subject to local tax laws. You appear to have local agents - several thousand Santa representatives - with authority to operate on your behalf in shopping centres across Australia. These agents commit the operation with the promise of toys to millions of children. A local agent acting with authority may expose you to local tax laws. This is an issue that may extend well beyond Australia and requires urgent assessment.

As discussed, there are currently no provisions within Australian tax law to allow the Commissioner the discretion to ignore your tax liabilities as a goodwill gesture. Please contact us urgently regarding these issues.

Thank you.