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NGR
ACCOUNTING
NGR Accounting Pty Limited
Phone 02 9011 6669
Email info@nrgaccounting.com.au

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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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When is a gift not a gift?

The Tax Commissioner has successfully argued that more than \$1.6m deposited in a couple's bank account was assessable income, not a gift or a loan from friends.

The case of *Rusanova and Commissioner of Taxation* is enough for a telemovie. The plot features an Australian resident Russian couple 'gifted' over \$1.6m in unexplained bank deposits, over \$67,000 in interest, the Russian father-in-law seafood exporter, a series of Australian companies, and the generous friend loaning money in \$20,000 tranches.

The crux of the case before the Federal Court is whether you can prove to the Australian Tax Office (ATO) that unexplained deposits should be treated as gifts or loans and what happens when the Tax Commissioner thinks otherwise? If the Commissioner suspects the deposits are income, he can issue a default tax assessment and decide what tax should be paid. The burden of proof is then on the taxpayer to prove the Tax Commissioner wrong.

The unexplained deposits

Between 2012 and 2016, an Australian resident husband and wife had an estimated \$1,636,000 deposited into their bank accounts. The ATO became curious when neither spouse had lodged tax returns in the mistaken belief that they had not earned any income.

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The money deposited, they said, was a gift from the wife's father and therefore not assessable income. Curiously, there were no records produced to support the deposits and not a single text or email notifying that money had been remitted, or acknowledging its receipt.

In addition, a friend of the couple deposited money into the husband's account including a series of \$20,000 transactions over about a week. These, the friend said, were interest-free loans with no agreed terms but an expectation that they would be repaid. The friend could not remember how he was requested to make the loans and there were no loan documents, emails, or texts disclosed to support the loans. Around the same time as the loans were being advanced, there was evidence of the husband 'repaying' amounts in excess of what had been lent. In addition, documents show the husband transferred a Porsche Cayenne to his friend in Russia, said to be repayment of the loan.

Compounding the issue were the four directorships of Australian companies held by the husband, none of which had lodged tax returns. One of the companies was a seafood wholesaler, distributing the product of his father-in-law's American registered Russian export company. The dedicated son-in-law stated that he was merely trying to develop his father-in-law's business during 2010 and 2016, without remuneration.

Contesting the Tax Commissioner

In 2017, a covert tax audit utilised entries in the couple's bank accounts to assess their income tax liability and the ATO issued a default assessment based on the unexplained deposits and expenses. The couple objected to the assessment and this objection was partly allowed. A second assessment was then issued to which the couple again objected before the Administrative Appeals Tribunal (AAT) on the grounds that the assessment was excessive.

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Can the Tax Commissioner really decide how much tax you should pay?

The Tax Commissioner has the power to issue a 'default assessment' for the amount he believes is owing from overdue tax returns or activity statements. The assessment is the amount the ATO believes is owing, not what has been declared.

The problem with a default assessment is not just the Tax Commissioner deciding how much tax you should pay, it is the potential addition of an administrative penalty of 75% of the tax-related liability for each default assessment issued. This penalty may be increased to 95% of the tax-related liability in certain circumstances for taxpayers who have a pattern of non-compliance.

But, here is the problem for the couple. While genuine gifts of money are not taxable, the burden is on the taxpayer to prove that the gift is truly a gift, if the ATO asks. The AAT held that, "absent any reliable evidence..., there is no proper basis to make any findings as to whether the deposits constitute part of the applicants' taxable income or not."

The Tax Commissioner can rely on a "deficiency of proof".

The couple's stance that the deposits were either gifts from the father or loans from a friend were rejected by the AAT. This is despite an affidavit and evidence from the wife's father stating that the amounts transferred to them were gifts. The couple did not demonstrate what their income actually was to prove the Tax Commissioner's assessment was unreasonable, and they could not substantiate that the gifts were indeed gifts from a very generous father.

The Federal Court dismissed the couple's appeal with costs, leaving the Tax Commissioner's default tax assessment and penalties in place.

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Avoiding the gift tax trap

A gift of money or assets from an individual is generally not taxed if the gift is given voluntarily, nothing is expected in return, and the gift giver does not materially benefit.

However, there are some circumstances where tax might apply.

Gifts from a foreign trust

If you are a tax resident of Australia and the beneficiary of a foreign trust, it's possible that at least some of the amounts paid to you (or applied for your benefit) will need to be declared in your tax return. This applies even if you were not the direct beneficiary of the foreign trust, for example, a family member received money from a foreign trust and then gifted it to you. This applies to cash, loans, land, shares, etc.

Inheritances

Money or property you inherit from a deceased estate is often not taxed. However, there are circumstances where capital gain tax (CGT) might apply when you dispose of an asset you inherited. For example, if you inherit your parents' house, CGT generally does not apply if:

- The property was their main residence; and
- Your parents are Australian residents for tax purposes; and
- You sell the property within 2 years.

However, CGT is likely to apply if for example:

- You sell your parents former main residence more than 2 years after you inherit it; or
- The property you inherit was not your parents' main residence; or
- Your parents were not Australian tax residents at the time of their death.

Managing the tax consequences of an inheritance can become complex quickly. Please contact us for assistance when planning your estate to maximise the outcome for your beneficiaries, or managing the tax implications of an inheritance. These issues are often not taken into account if you are drafting or updating a will.

Gifting an asset does not avoid tax

Donating or gifting an asset does not avoid CGT. If you receive nothing or less than the market value of the asset, the market value substitution rule might come into play. The market value substitution rule can treat you as having received the market value of the asset you donated or gifted when calculating any CGT liability.

For example, if Mum & Dad buy a block of land then eventually gift the block of land to their daughter, the ATO will look at the value of the land at the point they gifted it. If the market value of the land is higher than the amount that Mum & Dad paid for it, then this would normally trigger a CGT liability. It does not matter that Mum & Dad did not receive any money for the land. Mum & Dad might have a CGT bill for land they gifted with nothing in return.

Donations of cryptocurrency might also trigger CGT. If you donate cryptocurrency to a charity, you are likely to be assessed on the market value of the crypto at the point you donated it. You can only claim a tax deduction for the donation if the charity is a deductible gift recipient and the charity is set up to accept cryptocurrency.

Quote of the month

“Only the guy who isn't rowing has time to rock the boat”.

Jean-Paul Sartre, Philosopher

Divorce, you, and your business



Breaking up is hard to do. Beyond the emotional and financial turmoil divorce creates, there are a number of issues that need to be resolved.

What happens when there is a family company?

For couples that have assets tied up in a company, the tax consequences of any settlements paid from the company will need to be assessed. Settlements paid out by a corporate entity can sometimes be treated as taxable dividends and taxed at the relevant spouse's marginal tax rate.

If you are receiving assets from a corporate entity as part of a property settlement, it's essential that you understand the tax implications prior to settlement or a sizeable portion of the settlement could go to the ATO.

For business owners, outside of the tax and financial issues, it's important to not lose focus on what's important to keep the business running efficiently.

What happens to your superannuation in a divorce?

A spouse's interest in superannuation is a marital asset and can be split as part of the breakdown agreement. It's important to be aware however that superannuation cannot be paid directly to a spouse unless the spouse is eligible to receive superannuation (they have met a condition of release) but it can be rolled over into the spouse's fund until they are eligible to receive it. Laws exist to prevent taxes such as CGT being triggered when superannuation assets are transferred. This is

particularly important where your superannuation fund holds property.

A Court order or Superannuation Agreement is required to give effect to the agreed split in the SMSF assets or to execute a rollover eligible for the CGT rollover concession.

If you have an SMSF and both spouses are members, it's important to get advice to make sure that all of the appropriate administrative issues are taken care of. Where a divorce is not amicable, it's important to keep in mind that the SMSF trustee is required under law to act in the best interests of the fund and its beneficiaries. Anything less and the fund members may seek compensation for loss or damage.

Can you protect both parties from divorce?

In a divorce, assets are split based on a multitude of factors such as earning capacity, maintenance of children, and the assets held pre-marriage. Many couples don't go through their marriage with an equal view of how assets and income should be attributed until something goes wrong. If there is a disparity between the income levels of each spouse, there are a lot of benefits to the household in general of evening out how income flows through to the family. If your partner earns less than you, there is a very real financial benefit to topping up their super as superannuation has preferential tax rates. The same goes for taxable income. If you can even out income coming into the household, it spreads the tax burden. Good planning can make a difference.



The changes to how tax practitioners work with clients

The Government has amended the legislation guiding registered tax practitioners to include compulsory reporting of material uncorrected errors to the Tax Commissioner.

The Government has legislated a series of changes to the *Tax Agents Services Act 2009* that place additional requirements on registered tax practitioners and how they interact with clients.

The reforms are in response to the recommendations of a Senate enquiry into the actions of accounting group PwC and the consulting industry in Australia generally. The enquiry was sparked when a now former PwC Partner shared confidential information from Treasury consultations and through his engagement with the Board of Taxation. Despite having signed multiple confidentiality agreements, the Partner intentionally shared this confidential information with PwC partners and others in Australia and overseas, seeking to assist existing and potential new clients avoid some proposed anti-avoidance tax laws. The Senate enquiry estimates that the scandal put at risk \$180 million in tax revenue per annum and generated new income of at least \$2.5 million for the first tranche of PwC's services assisting clients to "sidestep the new laws".

Among other issues, the scandal revealed a series of flaws and deficiencies within the regulation of tax practitioner services, the investigative powers of the Tax Practitioners Board (TPB), and the ability of Government departments to share information.

While many of the resulting legislative reforms impact consulting services to Government, we are now obligated to advise clients of: how to check the currency of our registration as tax practitioners;

how to access the complaints process for registered practitioners; and, our obligation to report material uncorrected errors and omissions to the Tax Commissioner.

Tax practitioner registration

The TPB registers and regulates tax practitioners in Australia. Only licensed practitioners can provide tax or BAS services to you. You can check the public register here: <https://www.tpb.gov.au/public-register>

NGR Accounting's registration number is 24753409.

Managing complaints

We are committed to providing quality services to you. If we fall short of your expectations and you would like to make a complaint, in the first instance, please contact Belinda Bendon, Practice Manager, 02 9011 6669 or belinda@ngraccounting.com.au.

If your matter is not resolved to your satisfaction, you have the right to make a complaint to the TPB: <https://www.tpb.gov.au/complaints>.

Correcting errors and omissions

We are prohibited from making a statement to the Tax Commissioner or other government agency that we know, or ought to know, is false, incorrect or misleading, or incorrect or misleading by omission.

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If we become aware that a statement made to the Tax Commissioner is materially incorrect, we are obligated to either:

- Correct it, if we made the misstatement; or
- If the misstatement was made by you, advise you that it needs to be corrected.

If the misstatement is not corrected, we are obligated to report this to the Tax Commissioner.

Concerned?

If you have any concerns about the changes, please contact Nathan Rigney on 02 9011 6669

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The rise in business bankruptcy

ASIC's annual insolvency data shows corporate business failure is up 39% compared to last financial year. The industries with the highest representation were construction, accommodation and food services at the top of the list.

Restructuring appointments grew by over 200% in 2023-24. Small business restructuring allows eligible companies – those whose liabilities do not exceed \$1 million plus other criteria – to retain control of its business while it develops a plan to restructure its affairs. This is done with the assistance of a restructuring practitioner with a view to entering into a restructuring plan with creditors.

Of the 573 companies that entered restructuring after 1 January 2021 and had completed their restructuring plan by 30 June 2024, 89.4% remain registered, 5.4% have gone into liquidation, and 5.2% were deregistered as at 30 June 2024.

In the latest statement from the Reserve Bank of Australia, Michelle Bullock stated that, "...there's also some signs that the business sector is under a bit of pressure, that the business outlook isn't as rosy as it was." Productivity is also lagging.

Strategically, managers need to be on top of their numbers to identify and manage problems before they get out of hand. If you do not know what the key drivers of your business are - the things that make the difference between doing well and going under - then it's time to find out.

A business becomes insolvent when it can't pay its debts when they fall due.

The top three reasons why companies fail are:

1. Poor strategic management
2. Inadequate cashflow or high cash use
3. Trading losses

It's easy to miss the warning signs and rely on optimism that things will get better if you can just get past a slump. The common problem areas are:

1. Significant below budget performance.
2. Substantial increases in fixed costs without an increase in revenues - Fixed costs are costs that you incur irrespective of your business activity level. When fixed costs go up, they have a direct impact on your profitability. If your fixed costs are increasing, such as leasing more space, hiring more people, buying more plant and equipment, but there is no measurable increase in your turnover and gross profit, it might tip you over.
3. Falling gross profit margins - Your gross profit margin is the margin between your sales, minus cost of goods sold. Every dollar you lose in gross profit is a dollar off your bottom line.
4. Funding your business primarily from debt rather than equity finance.
5. Falling sales - If sales are falling, it is going to have a ripple through effect on your business, reducing profit contribution and inhibiting growth.
6. Delaying payment to creditors - Your sales are good but you don't seem to have enough cash in the business to pay your creditors on time.
7. Spending in excess of cashflow - Trying to pay today's expenses with tomorrow's income.
8. Poor financial reporting systems - Driving your business with a blindfold over your eyes!
9. Growing too quickly - You're making more sales than your business can sustain.
10. Substantial bad debts or 'dead' stock - Customers who won't pay their accounts and stock that you can't sell.