KnowledgEquity – Australia Taxation - FAQs

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Module 1 - FAQs

In Question 1.15, is instalment amount method the same as GDP-Adjusted notional tax method?

(See 'Question 1.15', pages 53 and 447)

Yes, the instalment amount method (where the ATO provides the amount that the taxpayer must pay) is otherwise known as the GDP-adjusted notional tax method. The other method of calculating PAYG instalments is the instalment rate method (where the ATO provides a rate, which the taxpayer applies to their instalment income for a period).

Module 2 - FAQs

In Question 2.5, why is the $2,000 voucher for luxury resort accommodation statutory income while the $1,500 trip to Sydney to watch a play is not?

(See 'Question 2.5', pages 99, 450)

The luxury resort accommodation, by itself, does not necessarily meet the definition of entertainment in this scenario, as there is no direct link to 'recreation' as required by s.32-10 (ITAA97). However, the Sydney trip is, by its nature, much more clearly a form of entertainment (to see a stage play, which is recreation). This is why the $2,000 is considered statutory income under s.21A (ITAA36), while the $1,500 trip to Sydney is not assessable as the benefit is reduced to zero under s.21A(4) (ITAA36). Note that this difference in treatment has nothing to do with one being a voucher and one being payment, or with one being for the individual and one being with a spouse. It comes down to the definition of entertainment, which does not include all accommodation (i.e. a hotel stay at a luxury resort is not necessarily entertainment). However, note that accommodation that is related to the provision of food, drink or recreational activities would be considered entertainment.

For the provider of the benefit (i.e. the client), this would likely be deductible – it would be seen as part of the cost of rewarding someone for undertaking work for the business – this is, of course, assuming that the provider of the benefit was a business or someone undertaking an income producing activity, and was paying Joe for services relating to their business (or other income producing activity). On the other hand, if it is assumed that the client had work undertaken for private purposes (e.g. on their main residence), then no deduction would be available for them.

Can you clarify why the seller can claim the credit for any foreign resident capital gains withholding (FRCGW) payment, when it is the buyer that has had to pay the 15%?

(See 'Foreign Resident Capital Gains Withholding', page 171)

This is a withholding tax, so the tax is taken from the buyer, but in effect, it's to pay for tax payable by the seller. This has similarity to when an employer withholds some of the employee's salary, so as to pay the ATO the employee's estimated tax liability — in such a situation, one body (the employer) is forwarding the estimated tax liability of another (the employee) — the employee can then get a tax credit for this — just like with FRCGW, the seller can get a tax credit for the FRCGW paid by the buyer.

In Question 2.8 and Question 2.16, why is there a difference in the deductibility of the cost of a gift?

(See 'Question 2.8' and 'Question 2.16', pages 111, 135, 451 – 452, 455 – 456)

The difference between the two questions is the recipient of the gift. In Question 2.8, the cost of a gift given to an employee who was about to be married is deductible as it is developing good employer/employee relationships. There is a clear connection with gaining or producing assessable income as required by s. 8-1 (keeping employees happy will benefit the business – potentially improving staff productivity and retention). However, in Question 2.16, the gift is not deductible under s. 8-1 as it was to a charity with no connection to the business and so it cannot be argued that it is a cost incurred in gaining or producing assessable income.

In Question 2.15, why is the FEE-HELP loan repayment denied as a deduction?

(See 'Question 2.15', pages 134, 454 – 455)

As stated on page 122, these payments are specifically denied because such payments do not constitute "expenses of self-education". Please note that this applies to those who pay their HECS up front as well as those that incur a HECS-HELP debt (both at the incurring stage and paying off the loan stage).

Is trading stock only deductible when it is on hand, or you have the legal power to dispose or sell the stock?

(See 'Definition of Trading stock and whether on hand', pages 162)

Trading stock is only deductible when it becomes 'on hand'. One exception to this is if the taxpayer earns money from the sale of the stock before it becomes 'on hand' — in which case, the trading stock is deductible when the taxpayer earns money from it.

In Question 2.27, how is the actual purchase of the trading stock treated for income tax purposes?

(See 'Question 2.27', pages 167, 460 – 461)

When it comes to trading stock calculations for income tax purposes, there are 3 broad steps:
1. Sales are treated as income;
2. Purchases are deductible; and
3. The difference in opening and closing stock must be accounted for.

Note that it is only for the third step that the taxpayer can choose how to value trading stock (the closing stock). For the second step, deducting purchases, the taxpayer can only deduct the cost, they cannot elect to use a different valuation method.

When can I start claiming a capital works deduction?

(See 'Capital Works', pages 156 – 158)

Note that the deduction rate (2.5% or 4%) is based on the date the construction commenced, but the deduction itself can only be claimed from the date construction was completed.

Module 3 - FAQs

In Question 3.10, why is there no capital gain or loss?

(See 'Question 3.10', pages 206, 464)

Please note that the cost base here after indexation is $56,900. As the capital proceeds are less than this amount there is no capital gain. Note that $56,900 is the cost base, not the reduced cost base. The reduced cost base here is $50,200 (as it cannot be indexed). As the capital proceeds are greater than this, there is no capital loss either.

If capital proceeds less cost base produces a positive number, there is a capital gain. If capital proceeds less cost base produces a negative number, it does not automatically mean there is a capital loss.

If reduced cost base less capital proceeds produces a positive number, there is a capital loss. If reduced cost base less capital proceeds produces a negative number, it does not automatically mean there is a capital gain.

Why does the section entitled 'Specific CGT Exemptions' list a depreciating asset as exempt?

(See 'Table 3.6', page 207)

A depreciating asset that is fully used for a taxable purpose will be generally exempt from CGT (s. 118-24) – instead, the sale of a depreciating asset will trigger a balancing adjustment event (see page 141). This will be the case whether the depreciating asset is active or not. Note that if the depreciating asset is not fully used for a taxable purpose, then the portion that is not used for a taxable purpose will potentially, upon disposal, be subject to CGT Event K7.

In Question 3.11, what are the tax implications for Shaun Simnett and Jane West in claiming different main residences?

(See 'Question 3.11', pages 209, 464)

As Shaun's interest in the townhouse did not exceed 50%, he will not have any CGT liability on the townhouse for the relevant period. Jane, however, will have to pay CGT on her 50% share. This means for instance that if the total capital gain made during that period on the townhouse was $100,000, her capital gain would be $50,000.

As far as the beach house is concerned, Shaun will have to pay full CGT on his share. So, if for instance there was a capital gain of $200,000 on the beach house, Shaun's capital gain would be 30% of this, being $60,000. As Jane's interest in the beach house exceeded 50%, it is deemed to be her main residence for only half the period. As a result, her portion of the capital gain under the above assumptions would be $140,000 (70% of $200,000), and half of this would be exempt, though the other $70,000 would be her capital gain.

In Example 3.23, there seems to be two different methods for allocating capital losses, so how do we know which one to apply?

(See 'Example 3.23', page 219 – 220)

This example has two sentences that can sometimes be seen as contradictory in terms of the application of capital losses.

Firstly, the example states, "the taxpayer can choose the order to apply capital losses against capital gains". This applies to where there is more than one capital gain -- a given capital loss can be offset against the capital gains in the order in which the taxpayer chooses.

Secondly, the example also states, "current year capital losses have to be applied first and capital losses from prior years are applied in the order they were made". This applies to where there are multiple capital losses, in such an instance the order cannot be chosen regarding current v previous capital losses -- more previous ones are to be offset first.

Module 4 - FAQs

In the suggested answer to Question 4.2 (a)(ii), where does the franking credit of $600 come from?

(See 'Question 4.2', pages 234 – 235, 468)

The question states that Joshua has earned a fully franked dividend of $1,400 for the income year. For non- base rate entities, the company paying the dividend is taxed at 30%, which in turn equates to a franking credit of $600 (i.e. $1,400 x 30% / (1 – 30%)). Please refer to Module 5 for more detail in relation to franked dividends.

If a super balance is over $1.9 million, can contributions made under the CGT cap amount still be made?

(See 'Capital gains tax cap amount', page 264)

Yes. Although non-concessional contributions are generally disallowed where there is a $1.9 million super balance, this prohibition doesn't apply to contributions made under the CGT cap amount. This is an example of a concession that is excluded from the $1.9 million cap.

In a transition to retirement income stream (TRIS), why are lump sum withdrawals prohibited?

(See 'Benefits paid through a transition to retirement income stream', page 266 – 267)

Some clarification to the relevant study guide paragraph is required here, although note that the following information is not examinable. If a fund member has already met a condition of release with a nil cashing restriction, they can access their super benefits in other ways and don't need a TRIS. In these circumstances, the trustee can start paying the member a normal account-based pension or pay the member a benefit as a lump sum without having to go through the process and cost of setting up a TRIS.

Module 5 – FAQs

In Example 5.8, why do we include Ross' income when calculating Jarli's assessable income for the assessable income test?

(See 'Example 5.8', pages 309)

The assessable income test is one of the tests that can be fulfilled to allow the taxpayer to offset their business losses against their non-business income. When the taxpayer is a sole trader, only their income will be taken into account with this test. However, where there is a partnership, the assessable income test takes the income of all the partners (except for non-individuals) into account -- please see page 307 under the "Assessable income test". This is why both Jarli and Ross have their incomes included.

In Example 5.13, how much of the partnership salary is assessable to Christine and why would she need to repay the $10,000 if the partnership is wound up?

(See 'Example 5.13', pages 314)

Where a partnership agreement allows the payment of a 'salary' to a particular partner, this effectively adjusts the allocation of partnership profits (and net partnership income) between the partners. As noted in paragraph 17 of Taxation Ruling TR 2005/7:

The effect of an agreement to pay a 'partnership salary' is that the partner receives a fixed part of the profits of the partnership before the remaining part falls to be divided among the partners in the appropriate proportions.

In Example 5.13, the $20,000 'salary' paid to Christine during the year is an advance on Christine's final allocation of partnership profits for that year. As the partnership net income was only $10,000, this means that $10,000 of this salary, from a tax point of view, is regarded as taking her share of the profit, while the other $10,000 is regarded as further drawings out of the firm which is not profit. This is why she would have to repay this if there were no future profits to cover that extra $10,000.

In Example 5.22, why are Pujan and Isha benefiting from a franking credit offset instead of a deduction?

(See 'Example 5.22', page 340)

Please note that the example is assuming that the requirements for beneficiaries being entitled to franking credits are fulfilled. Specifically, it is assuming that this is a family trust and it has made the relevant elections.

In Example 5.25, why is the depreciation of the existing machinery based on a cost of $492,000 (Schedule A) and what is the relevance of the $209,200 figure for the machine?

(See 'Example 5.25', pages 348 – 350)

This example states, in item (h), that the machinery is to be depreciated using the prime cost method. The prime cost method utilises the item's original cost rather than its written down value. The original machinery's cost is $500,000 (item (d)), though some of the machinery that had an original cost of $8,000 was disposed of on the first day of the tax year (see item (a)), meaning that the cost of the machine to be depreciated is $492,000.

The $209,200 figure is the written down value and would only be relevant if the machine were being depreciated using the diminishing value method. However, the company needs to keep track of this figure as it will be relevant for calculating any balancing adjustment on future disposals of the machinery.

In Example 5.25, how is the disposal of the machine dealt with in the calculation of taxable income?

(See 'Example 5.24, pages 348 – 350)

The calculation of taxable income starts with Net profit before tax for accounting purposes of $244,100. This figure includes the accounting gain on disposal of the machine of $1,000. However, in order to calculate the taxable income, we need to strip out this accounting gain and replace it with the balancing adjustment on disposal of the machine (which is effectively the tax gain/loss on the disposal). The balancing adjustment rules were discussed in Module 4 and require a comparison between termination value (sales proceeds) and adjustable value. In this example, the selling price was $4,630 and the adjustable value was $4,800 (refer part (a)). As termination value is less than adjustable value, the taxpayer can claim a balancing adjustment deduction equal to the difference of $170 (i.e. $4,800 - $4,630) on sale of the machine.

Consequently, in the calculation of taxable income we see the accounting profit on disposal of $1,000 deducted (stripped out), and then the balancing adjustment of $170 (effectively the tax loss on disposal) deducted.

Please note that Schedule B: Sale of plant should be displayed as follows –

Termination value (sales proceeds)	*$4630*
Less Adjusted value (tax depreciated value 30 June 2021)	*$4800*

Balancing adjustment on disposal of machine (s.40-285) *($170)**

**As the termination value is lower than the adjusted value, the difference is a deductible balancing adjustment amount.*

Module 6 – FAQs

When does Division 100 apply to vouchers, and what are the GST differences when it does apply as compared to when it does not apply?

(See 'Vouchers', page 379 – 380)

In general, a voucher that allows the holder to acquire a certain dollar amount of goods or services is subject to Division 100. For instance, a voucher for a major clothing chain that allows the holder to $100 of goods in that store is subject to Division 100. As a result, there is no taxable supply (and so no GST payable) when the clothing store voucher is acquired. However, there is a taxable supply (and so GST payable) when the voucher is later used to acquire clothing from that store. In contrast, if someone acquired a voucher for a specific good or service, such as a voucher that entitled them to a certain amount of petrol, then that would not be covered by Division 100. As a result, there would be a taxable supply when the voucher was sold, not when it was later used.

When are credit card charges input taxed and when do they include GST?

(See 'Financial Supplies', page 386)

There has been some confusion in relation to the following statements on page 384: financial supplies, including credit charges on credit cards, normally supplied by banks are input taxed. However, credit card charges and merchant fees paid to credit card companies are not financial supplies and will include GST.

The distinction between the two is based on different supplies. Charges paid by an entity (individual or other type of entity) on their own credit cards are input taxed. However, if a business pays a credit card company a fee so that the business can accept payments from customers using that type of credit card (merchant fees), these payments will include GST.

On page 392, why is the $100 input tax credit allocated to period 1 if the tax invoice is received in period 2?

(See 'Non-cash (Accruals) Basis Attribution Rules', page 394)

The input tax credit is available at the earlier of the tax period in which the invoice is received or the period when first payment is made. But there is an additional requirement (as set out on page 371) which applies to all taxpayers and requires a tax invoice to be held by the time the BAS is lodged in order to get an input tax credit. In other words, if the first payment is made in period 1, but an invoice is not issued until period 2, the only way to get an input tax credit in period 1 is to ensure that the tax invoice is received before the BAS for period 1 is lodged (which will be part-way through period 2).

In Question 6.19, why is David's golf club subscription deductible when, as per s. 32-5 of ITAA97, entertainment expenses are not deductible?

(See 'Question 6.19', pages 432, 485 – 486)

Although entertainment expenses are generally not deductible, one of the exceptions to this is entertainment expenses that constitute a fringe benefit (see pages 120 - 121 of the study guide) -- in which case they are deductible.