



Avoid common mistakes in your business return, and include appropriate income

We know you want to get your tax right, so it may help you this tax time to know how to avoid making what the ATO has found are the most common tax mistakes.

To do this make sure you have:

- declared all income, including cash and online sales, dividends, interest, capital gains or one-off transactions such as selling equipment
- accurately recorded the value of goods taken for private use and directors' fees or other money drawn out of your business
- correctly apportioned expenses that are used both privately and in your business, including adjusting your rent expenses if you store personal assets at your business premises

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About this newsletter

Welcome to Manser Tierney & Johnston's client information newsletter, your monthly tax and super update keeping you up to date on current issues, news and changes you need to know. Should you require further information on any of the topics covered, please do not hesitate to contact us.

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⇒ *Avoid common mistakes ... cont*

- only claimed expenses you're entitled to claim (for example capital improvements can't be written off as a repair)
- correctly claimed any business losses.

It's important to have good records that are up to date. It can help to have a dedicated business bank account to help keep business transactions separate from your other finances.

WHAT TO INCLUDE IN YOUR BUSINESS'S ASSESSABLE INCOME

When calculating your business's assessable income, include:

- all gross income (before tax) from your everyday business activities, including sales made over the internet, income from sales (cash and electronic) and foreign income. Gross income doesn't include goods and services tax (GST).
- all other business income that is not part of your everyday business activities, including changes in the value of trading stock, capital gains, isolated transactions intended to make a profit, and cash prizes for your business.

CASH INCOME

If your business receives cash payments for goods or services, the ATO will expect you to declare them as assessable income. Included here are:

- all your cash earnings
- income your business earned through coupons, vouchers or gift cards
- income your business deposited into a mortgage or private credit card
- bank interest, dividends, franking credits, etc.

Note that the ATO's data matching analysis and forensic capabilities have developed into a very sophisticated toolkit, making cash payments more visible to it than ever before. For example, it can identify people who may be running a part of their normal business activities "off the books" and avoiding tax obligations.

COMMISSIONS, INVESTMENT EARNINGS, GRATUITIES, COMPENSATION PAYMENTS

If you receive commissions, investment earnings (such as dividends), gratuities or compensation payments as part of your business activities, include these amounts as assessable income. These payments include:

- commission income
- royalties, such as payments when other entities use your patent
- incentive payments, such as a cash payment to lease business premises
- interest on business investments, and interest on overpayment or early payment of tax
- dividends and franking credits (from company tax already paid) on business investments
- rental income from property owned by your business
- lease payments and hire charges (if you are in the business of hiring out assets)
- tips and gratuities, including cash or electronic payments
- compensation, such as workers compensation, payments for trading stock losses, business interruptions or contract cancellations
- recovered bad debts for which you have received a tax deduction.

INCOME NOT PART OF EVERYDAY BUSINESS ACTIVITIES

Your business may receive income that is not part of your everyday business activities. These amounts must also be included in your business's assessable income at the end of the income year.

These sources of income can include:

- disposal of non-trading stock assets
- taking some trading stock for your own use
- sale of goods or services in return for something other than money

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- increase in trading stock value
- isolated transactions intended to make a profit
- business prizes or awards
- payments from insurance claims.

GOVERNMENT PAYMENTS

A number of federal, state and territory government grants and payments have been made available to businesses in response to recent natural disasters and COVID-19. Only those grants and payments that are “assessable income” will need to be included.

These payments include:

- fuel tax credits or product stewardship (oil) benefit
- wine equalisation tax producer rebate
- JobKeeper payments (COVID-19)
- Supporting Apprentices and Trainees wage subsidy (COVID-19)
- excise refund scheme for alcohol manufacturers
- grants, such as an amount you receive under the Australian Apprenticeships Incentives Program
- subsidies for carrying on a business.

Note well that you should not include the following grants and payments:

- cash flow boost payments (COVID-19 - this is “non-assessable, non-exempt” income)
- government grants and payments that are tax-free.

CAPITAL GAINS AND LOSSES

Capital gains or losses can occur when you dispose of a business capital asset by way of sale, gift, transfer, destruction, surrender, or other means. Business capital assets are all assets your business owns.

However, you can only generally make a capital gain or loss on particular assets, such as your business premises, land, goodwill, or rights or licences. You can't generally make a capital gain or loss on your trading stock. CGT generally doesn't apply to depreciating assets, such as tools or motor vehicles that you use in your business.

In certain circumstances, the following discounts apply to CGT:

- Individuals or trusts qualify for a 50% discount if they hold an asset for at least 12 months before disposing of it. This means you include only 50% of the capital gain in your assessable income.
- Companies aren't entitled to a CGT discount.
- Partnerships don't pay tax on capital gains. Instead, the individual partners determine their share of the capital gain, when working out their net capital gain, and include it in their personal assessable income.
- If you're a small business that owns active assets, you may also be eligible for the small business CGT concessions (ask this office about these). ■

This information has been prepared without taking into account your objectives, financial situation or needs. Because of this, you should, before acting on this information, consider its appropriateness, having regard to your objectives, financial situation or needs.

Getting deductions for clothing and laundry expenses right

The ATO allows certain taxpayers to claim a deduction for the cost of buying and cleaning occupation-specific clothing, items of protective wear and for certain unique, and usually distinctive, uniforms.

To claim a deduction it is generally expected that you will be able to provide evidence that you purchased the clothing concerned, and will have diary records or other evidence of your cleaning costs.

If you receive an allowance from your employer for clothing, uniforms, laundry or dry-cleaning, it will be necessary to show the amount of this allowance on your tax return.

OCCUPATION-SPECIFIC CLOTHING

You can claim for clothing that is specific to your occupation and is not everyday in nature. Generally this sort of clothing also allows the public to easily recognise your occupation — such as the checked pants a chef wears.

But the ATO will resist allowing claims made for the cost of purchasing or cleaning clothes you bought to wear for work but that are not specific to your occupation — for example, the black trousers and white shirt generally preferred by waiters or bartenders, or an office worker's suit and tie.

PROTECTIVE CLOTHING

You can claim for clothing and footwear that you wear to protect yourself from the risk of illness or injury that may arise from your income-earning activities, or from the environment in which you are required to carry out these activities.

To be considered “protective”, the items must provide a sufficient degree of protection against that risk. Therefore protective clothing includes:

- fire-resistant and sun-protection clothing
- high-visibility vests
- non-slip nurse's shoes
- rubber boots for concreters

- steel-capped boots, gloves, overalls, and heavy-duty shirts and trousers
- overalls, smocks and aprons you wear to avoid damage or soiling to your ordinary clothes during your income-earning activities.

Ordinary clothes (such as jeans, drill shirts, work shorts, trousers, socks, closed shoes) are not regarded as protective clothing if they lack protective qualities designed for the risks of your work.

The ATO generally disallows claims for the cost of purchasing or cleaning ordinary clothes that you wear for work that may also serve to protect the wearer. For example, you can't claim for normal, closed shoes, even though by wearing them you will protect your toes and feet.

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⇒ Getting deductions for clothing and laundry expenses right cont

WORK UNIFORMS

Generally, you can make a claim for a uniform (either compulsory or non-compulsory) that is unique and distinctive to the organisation you work for.

Clothing is unique if it has been designed and made specifically for an employer. Clothing is considered distinctive if it has the employer's logo permanently attached and items are not available to the public.

Claims are generally disallowed that are for the cost of purchasing or cleaning a plain uniform (that is, neither unique nor distinctive).

Compulsory work uniform

Compulsory work wear is a set of clothing that identifies you as an employee of an organisation with a strictly enforced policy that makes it compulsory for you to wear the uniform while you're at work.

You may also be able to claim a deduction for shoes, socks and stockings where they are an essential part of a distinctive compulsory uniform and where their characteristics (colour, style and type) are specified in your employer's uniform policy.

You may be able to claim for a single item of distinctive clothing, such as a company shirt or jumper, if it's compulsory for you to wear it at work.

Non-compulsory work uniform

You can't claim expenses incurred for non-compulsory work uniforms unless your employer has registered the design with AusIndustry. Shoes, socks and stockings can never form part of a non-compulsory work uniform, and neither can a single item such as a jumper.

CLEANING OF WORK CLOTHING

You can claim the costs of washing, drying and ironing eligible work clothes, or having them dry-cleaned. It will be expected however for you to have written evidence, such as diary entries and receipts, for your laundry expenses if both:

- the amount of your claim is greater than \$150, and
- your total claim for work-related expenses exceeds \$300 (excluding car, meal allowance, award transport payments allowance and travel allowance expenses).

If the amount seeking to be claimed is less than the above, and you don't need to provide written evidence for your laundry expenses, you may use a reasonable basis to work out your claim. For washing, drying and ironing you do yourself, the ATO considers that a reasonable basis for working out your laundry claim is:

- \$1 per load (this includes washing, drying and ironing) if the load is made up only of work-related clothing, and
- 50 cents per load if other laundry items are included.

If you choose a different basis to work out your claim, you may be asked to explain that basis to the ATO.

DRY-CLEANING EXPENSES

You can claim the cost of dry-cleaning work-related clothing. If your *total* claim for work-related expenses exceeds \$300 (not including car, meal allowance, award transport payments allowance and travel allowance expenses), you must have written evidence to substantiate your claim.

The deductibility of clothing and uniform expenses can be tricky – contact this office if you require assistance. ■

Steps to take when winding up your SMSF

There will most likely come a time when your SMSF will need to be wound up, with a change in members, the fund's finances, perhaps separation or other family causes among the many reasons why winding up the fund becomes necessary.

The many reasons people may find it necessary to wind up an SMSF could include:

- there are no members left – they may have passed away or rolled benefits into other funds
- there are no assets left – the SMSF may have paid members all of their benefits
- divorce – a marriage breakdown may force husband and wife members to split the fund's assets and may affect the ability of members to effectively undertake their trustee obligations
- insufficient funds – there is not enough money in the fund to keep covering running costs
- old age – trustees' circumstances may have changed in a way that has affected their capacity to effectively manage an SMSF, which can be complex and constantly requires a significant investment of time and expertise
- death – where there is only one member, their legal personal representative will be required to pay out all benefits as per the trust deed or death benefit nomination. Where there is more than one member, other members may not wish to continue the fund.

Once the decision to wind up an SMSF has been made, it is always a good idea to sit down and read your trust deed, as it may contain vital information about winding up your fund. And remember, once a fund is wound up, it cannot be reactivated.

THE NECESSARY STEPS

You need to let the ATO know within 28 days of the fund being wound up. This is best done in writing, to ensure a record is made, but you must include:

- the name of your SMSF
- its Australian business number (ABN)
- your name and contact details, and
- the date you wound up your SMSF.

You will also need to deal with member benefits, and will have to make sure that:

- you deal with members' benefits according to the superannuation law and the trust deed
- you obtain market value balances of all related accounts

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⇒ Steps to take when winding up your SMSF ... cont

- you ensure all SMSF assets have been sold and member contributions dealt with in accordance with the trust deed and superannuation laws
- you ensure all proper steps are taken to transfer ownership and title of any assets
- you decide whether any corporate trustees in your fund wish to deregister with the Australian Securities and Investments Commission (ASIC), and
- your fund has no assets left once it has been wound up.

But remember, if you have wound up your fund but you, as a member, have not met a condition of release – retirement, transition to retirement, or reaching an eligible age – you cannot access your superannuation. Your superannuation needs to be rolled over into another regulated superannuation fund. Remember, there are serious legal penalties for accessing your superannuation benefits before you are legally allowed.

Advice may be required on the potential capital gains tax (CGT) implications for your SMSF on the disposal of assets to enable the payment of benefits or the rollover of benefits to another fund.

When winding up your fund, you will need to have an audit completed by an approved SMSF auditor before you can lodge your final SMSF annual return. Also any outstanding tax liabilities will need to be paid at this time and lodge any outstanding returns from previous years.

It is important to wind up your fund correctly. If you fail to carry out these reporting responsibilities, you may be the focus of compliance activities and you may be subject to penalties.

After meeting all of your tax responsibilities, the ATO will send you a confirmation letter stating that it has cancelled your SMSF's ABN and closed your SMSF's record on its systems.

TAX IMPLICATIONS

The most common tax issues are outlined below.

Unrealised capital gains

If an asset(s) of the fund has been held over a long period, a capital gain (or loss) event would be triggered upon disposal where the SMSF is in accumulation phase.

If the fund is wound up and a net capital gain arises, the fund will have significant taxation liabilities which, in effect, will reduce the members' overall superannuation balance.

Significant realised/unrealised capital losses

Alternatively, the reverse is that the fund may realise a capital loss during the wind-up process. While these capital losses can be added to the capital losses carried forward from previous years and offset against any current year capital gains, any residual capital losses that are not utilised during the wind-up process will be wasted. Because they cannot be transferred to another person (member or beneficiary) or entity (another superannuation fund), the benefit from any remaining unused capital losses will be lost once the fund is wound up.

Carried forward income tax losses

Some SMSFs can have carried forward income tax losses (because they could not claim any tax deductions that exceeded their income) that could be used to offset any future taxation liability of the fund. Unfortunately, as with capital losses, the benefit of using up its carried forward income tax loss will be lost upon wind up. ■

When the taxman sends a bill, not a refund

While most people look forward to receiving a tax refund once their return is processed by the ATO, it is also not unheard of to receive a tax bill on occasion.

Most people who earn income as employees have tax payments made on their behalf throughout the year through pay-as-you-go (PAYG) withholding to help them meet their annual tax obligations. But this withholding of amounts can sometimes miss the mark.

You may receive a tax bill if you have not had a sufficient amount withheld from your income throughout the year to meet your tax obligations. This may occur in the following circumstances:

- you move to a higher tax bracket – for example, through promotion, multiple or extra sources of income
- you have incorrectly made multiple claims for the tax-free threshold
- your income increases leading to a higher repayment threshold for your study or training support loan
- you have a study or training support loan that is not reported to an employer on a tax file number declaration
- you need to pay the Medicare levy or Medicare levy surcharge, or the amount of private health insurance rebate you receive changes
- a change in income affects your single or family income threshold for relevant tax offsets or rebates
- you are the recipient of Australian government allowances and payments.

Note that tax is not withheld from every single source of income. For example, the following income sources do not generally have tax amounts withheld:

- a capital gains event occurs where you receive additional income through the sale of a capital asset such as real estate or shares
- you receive income from a business, partnership or trust
- you receive income from property investments (including the sharing economy), dividends on shares, interest or returns on any other investment
- you earn income as a sole trader.

If tax is not withheld when you receive payments from income earned as a sole trader or from investments, you can voluntarily enter into PAYG instalments. This is a way of prepaying tax and reduces the chances of having to pay a large amount at the end of the income year.

It is also possible to make tax prepayments any time and as often as you like to make it easier for you to manage your tax. The ATO will hold the prepaid amounts you make towards your expected bill unless a refund is requested. ■

