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TAX matters

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EMPLOYEE SHARE SCHEMES – THE ATO IS COMING!

There is currently a significant amount of ATO audit activity in relation to shares and options acquired by taxpayers under employee share schemes.

It appears that there is a team of ATO officers based in Queensland who are

currently reviewing annual reports and writing to taxpayers seeking information regarding how the shares and rights (including options) they have acquired have been treated for income tax purposes.

One issue commonly raised by the ATO concerns the time of acquisition of rights under the employee share scheme.

Common errors that we have seen that have been made by taxpayers are the failure to make a valid section 139E election (to be taxed on the discount up front) within the required timeframe and the incorrect cost base being used when calculating the capital gain on ultimate disposal of the shares.

Where errors have been made, making relevant voluntary disclosures can help to significantly reduce liability through the reduction of penalties. Such reductions may be more readily available if disclosure is made prior to notification of an audit.

Norton & Smailes has handled numerous audits and enquiries from the ATO in recent months. Please contact Chris Smailes, Daniel Fry, Richard Norton or Rachael Munro with any queries.

Please Contact Chris Smailes, Daniel Fry or Rachael Munro

EMPLOYEE SHARE SCHEMES – THE PROPOSED NEW LAW

Draft legislation to implement the proposed changes to the Employee Share Schemes rules announced in the 2009/10 Federal Budget has now been introduced. As foreshadowed in the Budget, the legislation, if passed, will significantly change the way that recipients of shares and rights under employee share schemes will be taxed.

Generally the new measures will apply to shares and rights acquired on or after 1 July 2009. The new measures will also apply to shares and rights acquired prior to that date, subject to the application of transitional measures.

A significant change to the current treatment is that generally, the discount to market value of shares or rights received by a taxpayer under an employee share scheme will be taxed in the year of acquisition – there is no automatic deferral.

The ability to defer tax or be taxed up front in relation to shares and rights acquired under an employee share scheme will no longer be at the election of the taxpayer. The ability to defer tax will depend on

the particular terms of the scheme itself.

However, a deferral of tax will occur if certain conditions are met. One such condition is that there is a “real risk of forfeiture” of the shares or rights.

The new measures will have a significant impact on the manner in which equity-based remuneration is offered to employees.

There is potential for significant adverse tax treatment for employees who are assessed upfront. Accordingly, existing and proposed share and option plans entered into post 1 July 2009 should be reviewed to take into account the impact of the proposed new measures.

Please Contact Chris Smailes, Daniel Fry or Rachael Munro

High Net Worth Individuals Questionnaire

Financial planners and accountants with high-net-worth clients need to be aware of the ATO’s focus on high net worth individuals and their increasing use of questionnaires for information gathering purposes.

Care should be taken when responses are being made. Often the client will require assistance regarding such matters as the ambit of the information sought and dealing with the questions on control of trusts.

Norton & Smailes has handled numerous questionnaires and enquires from the ATO in recent months in regard to these questionnaires and can assist in responding to them.

ONE DAY MY CHILD THIS WILL ALL BE YOURS

A son has successfully claimed a 1/3rd interest in farming land owned by his father under the proprietary estoppel principle – *Consolaro V Consolaro [2009] WASC 240*.

The son satisfied the Supreme Court that he had acted on the promise of the parents to be placed on the title, in exchange for the son working over a number of years on the property for low or no wages.

These arrangements are common amongst members of farming families. If clients are proposing these arrangements (and sometimes you need to ask if they are), then advice is required on the potential claims. The claims could include common law (contract), equitable (proprietary estoppel) and statutory (Inheritance Act) claims, if the promise is not fulfilled. Advice is also required on the transaction taxes that may result if the promise is fulfilled.

If the matter deteriorates into a dispute, then the evidence of 35 years of family history can be laid bare in a lengthy and very public Supreme Court judgement, as it was in the *Consolaro* case. In other words, the large factual matrix is likely to result in expensive litigation.

Proper succession planning is more than likely to result in a resolution between the parties, without deteriorating into a dispute. Proper planning could also result in the availability of exemptions to transaction taxes, such as the small business CGT concessions, the transfer duty farming exemption and the GST going concern or farming exemption.

Contact: Craig McKie

TO SELL OR NOT TO SELL? THAT IS NOT THE QUESTION - GST DIVISION 129.

The ATO recently released GSTR 2009/4 entitled “New residential premises and adjustments for change in creditable purpose”.

One could say this ruling was meant to provide relief for property developers by allowing them to claim a portion of input tax credits on construction costs while renting out new residential premises so long as the properties were being held for sale.

However, the recent AAT Case, *GXCX* and Commissioner of Taxation [2009] AATA 569 (“*GXCX*”), highlights that developers need to be cautious and that advisors need to be asking the right questions.

The Facts

In *GXCX*, the taxpayer built and/or developed approximately 91 apartments in 2000 and 2001. The apartments were marketed for sale before and during construction. In December 2001, when the development was completed, 22 apartments remained unsold and were rented. A further 10 apartments were then sold in 2008 and 2009. The taxpayer claimed input tax credits on the full construction costs.

The Issue

The Tribunal had to decide whether the developer was required to make an adjustment under Division 129 of the GST Act when they made the decision to rent out the 22 unsold apartments.

The Tribunal’s decision

The Tribunal held that the developer was required to make an increasing adjustment because section 129-55 requires an analysis

of the actual application by the developer of the premises in the period following the change in intention.

“there were no overt acts demonstrating the fact that the apartments were available for sale and the evidence of the directors, demonstrates that the intention was not to sell in the short term. The intention to sell was predicated upon the market reaching a level where the capital growth could be realised”.

Hence, in the Tribunal’s view, the application of the premises during the period in question was entirely for the non-creditable purpose of leasing.

It held that the mere intention to sell the properties at some time in the future, without more, did not amount to an application of the premises for a creditable purpose.

The Tribunal’s decision in GXCX highlights the need for developers to be cautious when claiming input tax credits on construction costs on the establishment of residential premises which are ultimately rented.

Developers should be aware of factors the ATO, in GSTR 2009/4, considers relevant to establishing the requisite intention, for Division 129 purposes, namely:

- (a) having business plans;
- (b) finance documents supporting the planned sale;
- (c) past activities of the entity that demonstrate it carries on an enterprise of selling new residential premises; and
- (d) marketing of the property for sale.

However no one factor is determinative and the circumstances should be judged on a case by case basis.

The calculation of the amount of input tax credits that can be claimed should be performed in accordance with the reasonable methodologies set out in GSTR 2009/4. **Stay tuned for another Tax Matters on this issue in the near future.**

Contact Chris Smailes, Rachael Munro or Reagan Gruenthal with any queries.

Norton & Smailes

We advise on:

- the small business CGT concession;
- income tax, GST and FBT
- employee share schemes
- wills, estate planning and business succession planning
- superannuation and superannuation deeds
- transfer duty, land tax, payroll tax and other State taxes
- trusts and trust deeds
- objections and appeals
- tax and commercial litigation
- commercial law