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March 2006

Salary Packaging Opportunities

A common misconception is that salary packaging is only worthwhile in the not-for-profit sector. However, employers in the commercial and government sectors should be aware that they can pass on significant savings to their employees through salary packaging, with very little effort. These days employees expect to be offered salary packaging, and given the importance of staff retention in today's competitive employment market, having a salary packaging policy can be crucial.

Provided below is an outline of basic salary packaging strategies that all employers can consider, with some tips on keeping administration to a minimum.

Superannuation

Employees who wish to invest in extra superannuation will find that salary packaging additional contributions is extremely tax effective.

The salary to be sacrificed, or given up, for additional superannuation is simply the amount of the contribution, since no fringe benefits tax (FBT) applies.

The immediate saving for the employee will be the difference

between the employee's marginal tax rate, say 48.5%, and the contributions tax of 15% deducted from salary packaged superannuation contributions.

The employee also benefits very significantly over time from the earnings on the higher amount after tax invested in the fund.

Laptops, electronic diaries and PDAs

These items are specifically exempt from FBT and are useful to salary package, as the effective cost to the employee is halved. This applies for personal digital assistants (PDAs) from 1 April 2006. Packaging laptop computers is particularly attractive for employees who need them for school children.

Packaging of these items is simple to administer. The simplest process is where the employee purchases the item and then seeks reimbursement from the employer. The reimbursement can be paid with the employee's salary in the normal pay cycle.

That is, the employee's gross salary is reduced by the amount of the reimbursement and the reimbursement amount is added to the employee's net pay as a tax-free amount. The total is paid to the employee, normally by way of direct debit into the employee's bank account. The reimbursement and corresponding reduction in salary can occur in one pay cycle, or can be spread over a period.

Where employees purchase PDAs prior to 1 April 2006, the cost can be reimbursed after this time as part of a salary packaging arrangement and still qualify for FBT exemption.

Cars — novated and associate leases

Cars can provide terrific tax savings for employees in many cases. The FBT legislation assumes an element of business travel and therefore operates on a concessional basis. Consequently tax savings can typically arise, particularly where the kilometres travelled exceeds 15,000. Naturally, the tax outcome should be reviewed in each case in light of the employee's particular circumstances.

Novated leases involve leasing a car through an external financier. Associate leases involve the employer leasing a car from the employee's associate (usually spouse). Associate leases are therefore very useful where the employee or spouse currently owns an existing car, as this car can be used in the associate lease arrangement.

Associate leases have an additional benefit over novated leases where the associate is on a lower marginal tax rate than the employee, as they have an income-splitting type effect. Specifically, the employee's assessable income is reduced in favour of the spouse who receives the lease payments.

From the employer's perspective, the arrangement is simple. The employer pays lease payments to the financier or associate and any FBT that arises. The employee sacrifices salary equivalent to these costs. All the running costs and other associated obligations remain with the employee under the novated lease scenario and with the associate under the associate lease scenario. As a result, the administration for the employer is minimal.

Policy manual

As the first step in implementing or updating a system to incorporate the above benefit offerings, we recommend the introduction of a salary packaging policy manual. This document should describe the practical aspects of the system and double as a guide for employees wishing to participate. It should include:

- outline of the key concepts;
- menu of benefits, including full details;

- example calculations of potential savings;
- the impact of reportable benefits;
- related policy considerations, e.g. basis for compulsory superannuation, arrangements for when employees take unpaid leave, basis for accrued leave calculations;
- instructions for employees wishing to participate; and
- standard documentation for implementation.

Sale subject to Anti-avoidance

In a recent case, the Federal Court held that the sale of shares from one family discretionary trust (Trust No. 1) to another family discretionary trust (Trust No. 2) was subject to the anti-avoidance provisions.

The taxpayer was a family trust that originally purchased shares between July and October 1997. The purchase of the shares was financed by a bank loan. The terms and conditions of the loan stated that the shares could not be sold without the bank's approval. Failure to gain approval from the bank would result in a default of the loan.

In June 1998, Trust No. 1 sold the shares to Trust No. 2 at their market value. The share sale agreement was not executed and the bank's approval was not sought. The sale agreement provided that the transfer would take place even if the funds were not provided by Trust No. 2. Trust No. 1, however, would be entitled to interest on the balance of the unpaid funds.

The sale gave rise to a capital loss of \$800,000.

The Administrative Appeals Tribunal (AAT) held that the sale was subject to anti-avoidance provisions. The transaction was entered into so Trust No. 1 could realise a capital loss. The AAT held that in the circumstances it was unreasonable to expect that the applicant would have incurred the capital loss had the transaction or scheme not been carried out. The capital loss was therefore denied to Trust No. 1. The Federal Court agreed with the AAT decision.

➤ **CAUTION:** Transactions which create a deduction or capital loss between related entities may be subject to Tax Office review.

GST and Residential Renovations

The Tax Office recently released two GST 'advices' on whether certain additions to houses constitute 'substantial renovations' making the premises 'new residential premises' for the purposes of the GST law.

In these advices, the Tax Office explains its view that the addition of a second storey to a single storey house or the addition of four rooms to a six-room house does not constitute 'substantial renovations'.

Accordingly, the sale of the premises will not be taxable supplies of new residential premises. Instead, they will be input taxed supplies.

As a result, taxpayers will be able to apply the principles expressed in the Tax Office's ruling to determine the correct GST treatment of supplies of residential premises.

Important: This is not advice. Clients should not act solely on the basis of the material contained in this Bulletin. Items herein are general comments only and do not constitute or convey advice per se. Also changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. The Bulletin is issued as a helpful guide to clients and for their private information. Therefore it should be regarded as confidential and not be made available to any person without our prior approval.