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IS A RENTAL ASSET ALWAYS EXCLUDED FROM BEING AN ACTIVE ASSET?

One of the basic conditions required to be able to access the generous small business CGT concessions is that the asset passes the Active Asset Test.

It is generally understood that for the asset to pass the test, it must be used in your business for at least 7.5 years, or for at least half of the asset's ownership period.

One of the notable assets that is excluded from qualifying as an active asset, is an asset that is mainly used to derive rent. This exclusion does not extend to an asset where its main use for deriving rent was only temporary, or where the asset was being used in a business being run by a related party.

This "exclusion from the exclusion" allows for the common scenario of having a business and its premises owned by different entities, but under common ownership, to have access to the small business CGT concessions for all the assets used in the business.

So where does this leave a business where the main income is rental income, but that rental income is not coming from a related party's business?

The devil (or anti-devil in this case) may just lie in the detail.

Consideration has to be given to the specific circumstances, as the generalisation that it is rental income being received does not necessarily hold true for small business CGT concession purposes.

One of the keys to income being considered "rental income" is the right of the tenant to exclusive possession of the property. It is this element that generally excludes a standard leased residential or commercial property from being an active asset. But how may this apply to other "rental arrangements"?

The Commissioner has set a few examples in TD 2006/78 where, in his view, the otherwise rental arrangement would not actually be deriving rental income.

These scenarios cover the lease of commercial storage units, the operation of a boarding house and the leasing of a complex of holiday apartments. When reviewing the legal rights of the tenants, the Commissioner is of the view that the tenants do not have exclusive possession of the relevant property, and as a result a landlord/tenant relationship does not exist and the income is not rental income. Therefore, the asset is not an excluded asset under the Active Asset Test.

This does not necessarily mean the sale of the asset would pass the Active Asset Test, as consideration still needs to be given as to whether a business is actually being conducted.

So the questions that exist for your "rental asset" are: What are the contractual terms of the rental arrangement? What rights do the tenants have? If they do not have exclusive possession that may be the first step in the asset passing the Active Asset Test.

If you have any questions on the Active Asset Test, please contact Andrew Lowry or Leonard Tebbutt on 08 9444 9711.

DO SUB-DIVISION ACTIVITIES AMOUNT TO "ENTERPRISE" FOR GST?

Determining whether GST is payable on the sale of sub-divided property is difficult where the primary issue is whether the activities amount to a taxable supply 'made in the course or furtherance of an enterprise' under section 9-5, A New Tax System (Goods and Services Tax) Act 1999 (GST Act). Each case needs to be considered on the facts and objective evidence available.

In a recent Administrative Appeals Tribunal (AAT) case, Mr Paul Lance (the Taxpayer) contested the ATO's decision that GST was payable on the sale of his heritage listed property (Sutton Farms), **Lance V Commissioner of Taxation [2024] AATA 11 (Lance)**. The primary issue for the AAT to determine was whether the sale of a heritage listed property was made 'in the course or furtherance of an enterprise' carried on by the taxpayer, as all other elements of making a taxable supply were satisfied.

The Taxpayer's main argument was that Sutton Farms was intended to be used as a family home and the subdivision had no commercial purpose. As a result, the taxpayer sought to argue that the sale of Sutton Farms did not occur in the course of an enterprise and therefore should not be subject to GST. However, the Taxpayer was unsuccessful due to the lack of evidence supporting his contention and the fact that the AAT found inconsistencies with the Taxpayer's statements. These inconsistencies were in the form of:

- local newspaper articles referencing his plans to commercialise and develop the site to add facilities, (e.g. develop a restaurant or bar, and tourist accommodation);

- statements made by the Taxpayer to the ATO during the objection stage of the dispute indicating that he intended to subdivide the property to sell some of these lots to repay loans owed to the Taxpayer's brother-in-law; and

- Representations from the Taxpayer's accountant that GST credits on the original development costs were claimed because the intended subdivision and sale of the several lots within the property amounted to an enterprise,

Consequently, the AAT held that the series of activities conducted by the Taxpayer amounted to an enterprise in the form of a business for GST purposes. This decision was notwithstanding that Sutton Farms had not actually been sub-divided and the fact that it was ultimately sold as a single lot.

Additionally, the AAT held that the property could not qualify as "input taxed residential premises" on the basis that none of the buildings were capable of being occupied (i.e. the buildings were uninhabitable). The AAT also found that **regardless** of whether or not the Taxpayer was in the business of being a property developer, the series of activities amounted to an enterprise in the form of a business for GST purposes (within section 9-20(1) of the GST Act). Therefore, the sale was a taxable supply and was subject to GST.

This AAT decision is an important reminder that the term "enterprise" is much broader than the income tax concept of "carrying on a business". The Lance case is also a timely reminder that a taxpayer's activities prior to the sale of land and any objective evidence will be scrutinised when considering whether or not the taxpayer is carrying on an enterprise.

Furthermore, this decision has potential flow-on implications for income tax purposes especially for those looking to argue that the sale of a property should be taxed on capital account. Careful consideration of the facts and evidence needs to be made before determining whether a property owner is conducting an enterprise and has made a taxable supply on which GST is payable when they sell their sub-divided property.

If you would like to discuss this matter further, please contact Andrew Lowry or Leonard Tebbutt on 08 9444 9711.

ATO Toughens Its Tax Debt Stance – GIC & SIC Becoming Non-Deductible

It is notably obvious that owing debt to the ATO is not as simple as it used to be. With the amount of collectable debt increasing each year and $50.2 billion outstanding as of 30 June 2023, taxpayers and their advisors will soon find out (if they haven't noticed already), that the ATO is much tougher than it has been in the past with its' terms and conditions and its' collection and enforcement of outstanding tax debt.

It has now added another measure to its' arsenal on debt collection. On 13 December 2023, as part of the 2023–24 Mid-Year Economic and Fiscal Outlook (MYEFO), the Government announced that it will amend the tax law to deny deductions for ATO interest charges. Although this measure is not yet law, once enacted, it will mean that after 1 July 2025, taxpayers will no longer be able to claim a tax deduction for ATO interest charges.

The general interest charge (GIC) is incurred when a tax debt has not been paid on time, while the shortfall interest charge (SIC) is imposed when a taxpayer incorrectly self-assessed how much they owed the government. Both charges are currently tax deductible.

The current deductibility of interest charges allows for a reduction in the effective interest rate based on the taxpayer's marginal tax rate. Even though this measure has not been passed as law, with a start date of 1 July 2025, taxpayers with outstanding debts or who currently negotiating repayment plans need to consider the potential impact of these changes including:

- Voluntarily amending returns or a making a voluntary disclosure;
- Payment plans surpassing 1 July 2025 being denied a deduction on interest charges incurred after this date;
- Making late tax payments, including through payment arrangements; and
- Consider submitting a compelling submission for a Commissioner's discretion for a remission of GIC and SIC in circumstances such as where:
  - ➢ Delays occurred when the ATO is undertaking lengthy reviews and audits;
  - ➢ Payments are made early or a payment arrangement is entered into;
  - ➢ The taxpayer is relying on the ATO's advice or general administrative practice;
  - ➢ Circumstances that existed which were beyond the taxpayer's control (such as where there is a natural disaster or serious illness); or
  - ➢ A delay in payment but where the taxpayer took reasonable action to reduce the delay.

Finally, where a tax debt is in dispute, we recommend dealing with that via discussion, negotiation or more formal processes like Objections or Appeals sooner rather than later so the matter is resolved and the tax debt determined to mitigate the impact of these new measures. The Government's intent is clear and aims to address the significant and growing outstanding tax debt situation by removing the interest charge deduction in order to discourage taxpayers with large outstanding debts to use the ATO as a loan facility. It would be prudent to be mindful of these measures in dealings with the ATO on tax debt.

If you would like to discuss these matters further, please contact Andrew Lowry or Leonard Tebbutt on 08 9444 9711.