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NEWSLETTER

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'EBAY ENTREPRENEURS' IN ATO SIGHTS

The Tax Office has successfully obtained records from eBay and The Trading Post that will enable them to data match income declared by taxpayers to their income generated online.

Targeting those with earnings of \$20,000 or more in any of the last three financial years, the ATO crackdown is looking for online operators who are effectively running a business but not declaring the income. The Tax Office also expects to catch existing businesses that are generating additional income through the trading sites but not declaring or understating the income.

The Tax Office will match data from the trading sites to Tax File Numbers, ABNs, addresses and dates of birth. The data matching program identifies a list of taxpayers 'of interest' to the Tax Office who are then contacted for review or audit.

For many, sites like eBay offer a distribution channel for home or start up businesses without the expense of a shop front or developing a retail network where margins can be squeezed and profits reduced. It's a way of 'dipping your toe' in the retail market to gauge a product lines appeal without many of the overhead costs associated with traditional business. The Tax Office focus means that they suspect there are a host of eBay business entrepreneurs who are not declaring income earned.

So, at what point do you have to declare income you have earned to the Tax Office? The Tax Office will be looking to see if your activity online could be deemed to be a business. There is no one test for what qualifies you as a business versus a hobby but factors such as the regularity of your transactions, whether or not you are promoting yourself as business (developing a brand name etc), if you

engage in marketing activities, whether you intend to develop a business and make a profit (or have the capacity to generate a profit over time), the size, scale and permanency of your activities, and whether you operate in a business-like manner, all go toward determining whether what you are doing is a business or merely a hobby. If your activities are just a hobby then the income is not assessable, and the expenses are not deductible. If you are a business then you need to declare the income earned but you also get to claim deductions for the cost of the business activities.

If you think you might be affected by the ATO's data matching program, contact us today. The ATO is offering reduced penalties to taxpayers who voluntarily disclose income earned from the online trading sites.

DON'T LET SHARE STRUCTURE TRIP YOU UP

Many companies have different classes of shares but when it comes time to sell, this share structure might be an impediment.

There are a number of reasons why differential share structures are used - the ability to provide different rights to equity holders and allowing dividends to be paid to one class of shareholder in preference to another are common reasons. Much of this comes down to the way the company is managed and the arrangements between shareholders. Having different share classes can provide an additional level of flexibility in the ownership of a company.

There is however one occasion where different share classes can work against you; when the company sells capital assets, triggers a capital gain and wants to reduce that capital gain by accessing the small business CGT concessions. The most common example of this is the sale of the business or shares in the company. The concessions are attractive because they can defer capital gains tax or reduce it to zero.

To access a number of the small business CGT concessions you need to be a significant individual, as defined by the legislation. This is a person who holds at least a 20% participation interest in the company. Such an interest

requires them to have rights to dividends, return of capital, and voting rights. So, what is the problem with different share classes?

Let's assume we have a company with three shareholders. Each shareholder has one ordinary share. Also on issue is one A class share, one B class share, and one C class share. These shares have the same rights attaching to them. The different shareholders each hold a different class of share in addition to the ordinary share they own. This structure was put in place to allow dividends to be paid to the shareholders at different times. The directors have the right to declare dividends to any class of share. Over the years the company has declared dividends but only to the ordinary shares. They have never used the different share classes for dividend purposes. Now, the company sells its business and wants to manage the capital gain by using the small business CGT concessions. The preferred concession they want to access is the small business retirement concession. This concession requires there to be a significant individual. Unfortunately, none of the shareholders qualify. Because the company could pay a dividend to any of the classes of shares and no one shareholder holds at least a 20% interest in all classes of shares on issue, a significant individual does not exist. The fact that the company has never paid dividends to one share class in preference to another does not matter. The mere ability to do this fails the significant individual test.

This test is applied at the time of the CGT event. So, even where there are different share classes on issue it may be possible to overcome this problem. Don't simply rush out and issue shares though, as this could trigger other CGT problems. This is something that needs to be considered and planned well in advance of a CGT event.

Failing to have a significant individual does not mean you lose access to all of the small business CGT concessions. It does however limit the concessions that are available to you.

WHO IS ON THIS YEARS TAX HIT LIST?

The ATO are fairly up front. Every year they tell you what they are targeting and why. That's why when the Tax Commissioner released his compliance program for 2010/2011, we took a keen interest in what he had to say.

The way the tax office catch tax evasion is more sophisticated and far reaching than ever. Last year, they utilised over 500 million transaction records from third parties. That is, bank details, international transactions, investments, welfare data, super fund information, luxury car and boat purchases, employee share scheme details, property data, are all used to make sure that the income you declare on your tax return is an honest assessment.

Individuals

- Details of employee share schemes
- Executive salaries and access to executive perks

- Lifestyles that don't match income declared
- Claims for home office expenses
- Claims for business travel (particularly mistaken claims for travel between the office and home).

Investors

- Claims for rental and share investment expenses not entitled to or can't be substantiated
- Breach of superannuation caps

Business

- International transactions - Project Wikenby is credited with reducing the flow of cash to international tax havens - Vanuatu, Switzerland, Lichtenstein - by 20 to 30%!
- Transfer pricing issues
- High level of GST credits

EXTENSION OF SMALL BUSINESS ASSISTANCE PACKAGE

The Tax Office will extend the Small Business Assistance Package, which was originally intended to expire on 30 June 2010, until 30 June 2011.

The extension of the Small Business Assistance Package will mean that eligible businesses with a turnover of \$2 million or less will continue to have access to:

- a 12 month general interest charge free payment arrangement with the Tax Office; and
- a deferral of activity statement payment due dates.

PAID PARENTAL LEAVE BILLS BECOME LAW

Legislation for the Paid Parental Leave scheme has been passed by Parliament.

From 1 January 2011, the scheme will provide eligible working parents with 18 weeks of Parental Leave Pay at the National Minimum Wage, currently \$570 a week before tax.

Parents and employers can find out more about the scheme, its eligibility requirements and how it will operate at www.familyassist.gov.au.

Disclaimer: Many of the comments in this publication are general in nature and anyone intending to apply the information to practical circumstances should seek professional advice from us so we are able to independently verify your interpretation and the information's applicability to your particular circumstances.