Newsletter - December 2017

Merry Christmas!

Christmas is a time that reminds us that there is more to life than work. Embrace the season and all the pleasures it delivers.

We wish you and your family a peaceful, safe and happy Christmas.

We look forward to exploring the New Year with you and seizing the opportunities it offers.

Our office will be closed from 23rd December 2017 and will reopen on 2nd January 2018.

Why 'property flipping' is the next ATO target

The tax law does not allow you to 'flip' a property tax-free even if you are living in it. Most people think that they can move in to a property, renovate it, and then sell it without paying tax. The main residence exemption - the exemption that protects your family home from tax - does not apply if your primary purpose is to 'flip' the property for a profit. The fact that you are living in the property does not mean it's exempt from tax.

Some people reading this are probably thinking, but who is going to know? How can the Australian Taxation Office (ATO) really know what my intention is when I buy a property to live in? Generally, the ATO is looking for a pattern of behaviour or a declaration of intention. For example:

- You are not employed and earn your income moving in, renovating then selling
- You have a pattern of renovating and selling properties
- Your loan documents on your mortgage suggest the property is for flipping and not for the long term
- You go on national television stating that you are looking to move in, renovate and flip the property (hello *The Block* contestants).

The ATO's guide on property is clear: *"If you're carrying out a profit-making activity of property renovations also known as 'property flipping', you report in your income tax return your net profit or loss from the renovation (proceeds from the sale of the property less the purchase and other costs associated with buying, holding, renovating and selling it)."*

People often make the assumption that any gain made from property flipping will be exempt from tax as long as the property is their main residence for the entire ownership period. However, this is only the case where the property is held on capital account. A property would generally be held on capital account if it is bought with the genuine intention of using it as a private residence or rental property for the foreseeable future and there is evidence to back this up.

The ATO indicates that someone who is renovating a property with the intention of selling the property again at a profit could be taxed on revenue account in which case the main residence exemption does not apply.

The guide identifies three main scenarios and the general tax implications:

- Personal property investor – this is someone who purchases a property with the primary intention of using it as a long-term rental property or private residence. If this person undertakes renovations and then sells the property earlier than originally planned, then they should still generally be able to argue that the sale is dealt with on capital account, which means that the main residence exemption and/or Capital Gains Tax (CGT) discount could apply.
- Isolated profit making undertaking – this is someone who buys a property with the primary intention of carrying out renovations and then selling the property when the work is completed. Someone in this category is likely to be taxed on revenue account with no access to the main residence exemption or CGT discount.
- Business of renovating properties – this is someone who undertakes property-flipping activities on a regular or repetitive basis and where the activities are organised in a business-like manner. As with the category above, there is generally no access to the main residence exemption or CGT discount.

Just because you live in the property for all or part of the ownership period does not automatically mean that the profits from sale are exempt from tax. The main residence exemption can only reduce capital gains; it cannot reduce amounts that are taxed on revenue account.

What is the main residence exemption?

Generally, you do not pay CGT on the sale of your private home.

A full exemption should be available if the following conditions are met:

- You are an individual who is selling a dwelling or an ownership interest in a dwelling;
- The dwelling has been your home for the entire ownership period;
- The dwelling has not been used to produce assessable income (i.e., rented out); and
- The dwelling is situated on land that is 2 hectares or less.

In some situations it is possible to apply a full exemption even if you have not lived in the property for the entire ownership period or where the property has been rented out for a period of time. However, the rules can be complex and need to be analysed in detail to confirm the position.

If a full exemption is not available, it may still be possible to apply a partial exemption. The general 50% CGT discount can also be applied if you have owned the dwelling for more than 12 months (subject to your residency status).

Earlier this year the Government announced that non-residents and temporary residents would no longer able to access the main residence exemption (existing properties held prior to 9 May 2017 will be able to access the exemption until 30 June 2019). However, these proposed changes are not yet law and we are still waiting on the final version of the new rules to be released.

Whether a dwelling is your main residence is a question of fact. The following factors are often taken into account to help determine the issue:

- The length of time you have lived in the dwelling;
- The place of residence of your family;
- Whether you have moved your personal belongings into the dwelling;

- The address you have your mail delivered;
- Your address on the Electoral Roll;
- The connection of services such as telephone, gas and electricity; and
- Your intention in occupying the dwelling.

Other tax and renovation issues

The main residence exemption is not the only issue that comes up with property flipping. Tax deductions for rental properties and renovating for profit inside an SMSF are common topics:

Can I claim a tax deduction for renovations on my investment property?

It is not generally possible to claim an upfront deduction for amounts spent on improving a property unless you are carrying on a business of buying, renovating and selling properties. If the property is held for long-term investment purposes then it is generally possible to claim a deduction for these costs over a period of time while the property is used to generate rental income.

Can I renovate a rental property owned by my SMSF?

An SMSF can renovate a property it owns as long as the money used to pay for the renovation is from money already within the fund. If the members pay for the renovation themselves (instead of using money in the fund), the renovation costs can create a contribution issue and the value could even be the improved value of the asset. The usual restrictions around a SMSF acquiring assets from a related party should also be considered, so the SMSF should pay for all the required materials for the renovations directly (or under an agency agreement) rather than reimbursing a related party for the expense.

Foreign property owners slapped with fee for vacant property

Australia has followed the international trend of penalising foreign owners of Australian residential property who keep their property vacant for extended periods of time.

Last month Parliament approved legislation that imposes an annual vacancy fee on foreign owners of residential real estate if the property is not occupied or genuinely available on the rental market for at least 183 days in a particular 12 month period.

Foreign owners can avoid the fee by living in the property (or have a family member live in the property), leasing the property, or making it available for rent, for a total of 183 days in a 12 month period. A property is genuinely available for rent if it is made available on the rental market; advertised publicly; and, available at a market rent.

Interestingly, the law requires the property to be let for a minimum of 30 days – so short term rentals arranged through platforms such as AirBNB are not an option unless the rental period is 30 days or more.

If owners fail to comply with the new law the Government has the capacity to recover any outstanding fee as a debt and/or by the creation of a charge over Australian land owned by the foreign person.

The vacancy fee is equal to the initial foreign investment application fee (currently $5,500 for properties acquired for $1m or less). The vacancy fee can also apply even if the initial application fee was waived.

A vacancy year generally starts at settlement when the property was acquired or in some cases when the occupancy certificate is issued for newly built dwellings. The new vacancy fee system only applies if the notice or application to acquire the property was submitted with the Foreign Investment Review Board on or after 7.30pm on 9 May 2017.

Importantly, a foreign person who falls within the scope of the rules will need to lodge a vacancy fee return with the ATO within 30 days of the end of the relevant 12 month period. If this obligation is not met then the owner is deemed to be liable to the vacancy fee, even if the 183 day occupation requirement was actually satisfied. The main exception to this is where the owner has disposed of their interest in the property before the end of a particular vacancy year.

The Uber Driver GST Surprise

As most people are now aware, Uber drivers need to register for GST by the time they complete their first drive. What many are unaware of however is that the GST registration applies to any other businesses that they run as a sole trader. Take the example of someone who has a micro business that turns over less than $75,000. Under GST law, the business owner is not required to be registered for GST and there should be no GST on the things they sell to customers. However, if this same micro business person starts driving for Uber, the GST registration applies not only to their Uber activities but to their micro business as well.

ACCC gets tough on credit card surcharge

The ACCC has issued a warning to businesses charging excessive credit card fees. One large merchant has already been issued with four infringement notices and has paid $43,200 in penalties.

The new rules, which came into effect from 1 September 2017, prevent merchants from charging more than the true cost of the transaction. As a guide, where a charge is imposed, the ACCC says that consumers should expect to pay around 0.5% to 1% for payment by debit card, 1% to 1.5% by MasterCard and Visa credit cards and 2% to 3% for American Express. Consumers are being encouraged to contact the ACCC if a business is charging more than what the ACCC expects.

TEAKLE ACCOUNTING PTY LTD

6 Hampden Road, Mount Barker SA 5251
Ph 8391 1200
www.teakleaccounting.com.au