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Client Newsletter – Tax & Super
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ATO IS CHASING "LAND BANKING" BY FOREIGN INVESTORS

About this newsletter
Welcome to the **GDF Partners** client information newsletter, your monthly tax and super update keeping you on top of the issues, news and changes you need to know. Should you require further information on any of the topics covered, please contact us via the details below.

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If you are a foreign resident and you have acquired vacant land in Australia with Foreign Investment Review Board approval, and you have not met a condition of that approval (namely, building a dwelling or dwellings on that land within the required time), then be careful.

continued overleaf ⇨

The ATO is now taking legal action under the *Foreign Acquisitions and Takeovers Act 1975* to have fines imposed on investors who do not meet a condition of their approval.

The ATO is taking action against "land banking" by foreign residents (presumably in line with government policy to increase housing supply in Australia).

Some of the fines imposed have been big. Very big.

In a recent Federal Court case, a foreign investor acquired vacant land for some $300,000 close to 10 years ago. The land now has a market value of over $550,000. The investor was fined $508,000 for failing to complete construction of a residential dwelling on the land within 4 years of its purchase, as required by the conditions of their foreign investment approval.

In addition, freezing orders were made over the land (and other land owned by the investor in Australia) to help secure payment of the fine.

The ATO said it identified the breach through intelligence from data matching and its land banking audit program.

The ATO also said it is auditing all foreign investment approvals requiring development of residential land. The audit seeks to identify and address land banking, where a foreign investor may hold land for future gain rather than putting it to productive use through development.

The ATO is very serious about the matter.

For example, in the 2024-25 income year alone, the ATO forced remediation of 217 breaches of the foreign investment rules, including the disposal of 111 residential properties.

Therefore, if you are a foreign resident (or know one) who has acquired vacant land in Australia and who has not complied with any requirement to build on the land within the required time, be careful: the ATO is determined to find you and have fines imposed.

Don't forget that if you are a foreign resident and you own land in Australia and you sell it, you will be liable for CGT on any gain you make on the sale.

You also won't be entitled to the CGT concessions that an Australian resident is entitled to in calculating that gain, in particular the CGT discount (and indexation after 1 July 2027). On top of that, you will be taxed on the gain at higher tax rates.

So if you are in this situation (or know anyone else who is), talk to us about what can be done, ideally before any problem emerges.

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SELLING REAL PROPERTY?

DECLARE ANY GAIN IN THE RIGHT INCOME YEAR!

A recent Federal Court case showed the importance of the rule that a capital gain is assessable in the income year in which the contract for its sale is entered into, even if settlement occurs in a later income year (perhaps several years later).

This is typical of contracts for the sale of land, where the contract is entered into (or exchanged) at one point in time (eg in June of one income year) but settlement does not occur until another time (eg in the next income year or later).

In that case, the taxpayer made a capital gain of some $5m from the sale of a city unit. He had entered into the contract in the 2019 income year, but the contract was not due to settle until the 2023 income year.

In the interim he received the deposit of $500,000 in the 2020 year, and he (wrongly) declared part of the capital gain attributed to this deposit in that 2020 year. In the 2023 year, he received the balance of the sale price and (wrongly) declared the rest of the capital gain in that 2023 year.

When the ATO found out about it soon after, it amended his tax assessments to make sure all the capital gain was included in the correct 2019 income year. In this case, a special provision in the tax law enabled the ATO to go 4 years back to 2019 to amend the return for a capital gain arising from the sale of land under a contract.

The ATO also amended the 2023 year to remove the capital gain he had wrongly declared there. In this case, the basic rule that allows the ATO to go 2 years back to amend a tax return enabled this amendment.

However, the ATO could not amend the 2020 tax return to remove the capital gain that had been declared in the 2020 income year. There was no provision in the tax law to allow the amendment of that return in this case.

As a result, the taxpayer was subject to double taxation in respect of that $500,000. The Court said there was nothing it could do about it, as the tax law applied "according to its terms", and these terms prevented an amendment being made to the 2020 income year.

So, the moral of this story is that capital gains (and losses) must be accounted for in the income year in which the contract is made, even if the settlement of that contract does not take place until a later year (including many years later). This is often the case where land is sold to a property developer who does not pay the full price until each block is developed and then sold.

However, the ATO provides an important concession for taxpayers who are liable to pay tax on a capital gain in one income year but do not receive the sale proceeds to help pay that liability until a later year.

Under this concession, the ATO will allow the taxpayer to go back and amend their tax return to include the capital gain when the sale proceeds are actually received, without charging interest for late payment. But this is subject to strict conditions, including that the return be amended as soon as the sale proceeds are received.

If you are selling land or any other property and you find yourself in this situation, talk to us. We can also advise on legitimate planning to take advantage of this rule.

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RECEIVING LOANS OR OTHER BENEFITS FROM YOUR COMPANY? BEWARE!

Earlier this year, the High Court handed down an important decision about the operation of Division 7A (Div 7A). This is the rule in the tax law that, broadly, treats company loans made to shareholders (or their associates) as a deemed dividend in the hands of the shareholder.

In that decision, the High Court held that the ATO practice of treating an unpaid present entitlement (UPE) of a company beneficiary of a trust as a Div 7A loan back to the trust was *wrong!* The decision overturned some 20 years of ATO practice.*

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More precisely, the High Court held that UPEs from a trust to a corporate beneficiary do not automatically become a Div 7A loan made to the trust.

Otherwise, the decision has no bearing on the operation of Div 7A in general, namely where a shareholder (or an "associate") receives a loan directly from a company, or obtains some other form of "financial accommodation" from the company because they are a shareholder (or an "associate").

In other words, Div 7A continues to prevent small business owners, shareholders and directors from taking company profits tax-free in the form of loans or informal cash drawings.

Div 7A is ordinarily triggered whenever company funds are used for personal purposes without being paid out through normal channels like salary or a franked dividend.

Apart from making a direct loan to a shareholder or associate, other ways Div 7A can be triggered include:

- moving company cash directly to a personal account.
- company-owned assets (such as a holiday home, vehicle or yacht) being used privately.
- directing the business to pay personal costs like school fees or private home renovations.

If these amounts are still sitting on the balance sheet as an unpaid "shareholder loan" or "drawings account" by the company's tax return lodgment date, Div 7A treats the entire amount as an assessable dividend, without any franking credits to reduce the tax payable on it.

For private business owners, keeping personal expenses separate from company funds is very important.

However, the tax law provides a "safe harbour" rule known as a "complying loan agreement".

To be accepted by the ATO, the agreement must be in writing and must meet strict commercial terms:

- the loan term cannot exceed 7 years if unsecured, or 25 years if the loan is secured by a registered mortgage.
- the loan must charge interest at or above the benchmark rate, which is based on a Reserve Bank of Australia housing loan rate.
- the borrower must make a minimum yearly repayment of principal and interest by 30 June of each later income year.

The ATO remains heavily focused on Div 7A in private groups, using data matching to cross-check company balance sheets, bank data and personal returns to catch non-compliant arrangements. It is also not afraid to go to court in this area.

So, if you are concerned about Div 7A in any way, talk to us.

*Be assured, if you were a party to this type of arrangement, we are looking at it closely and waiting to see how, exactly, the government may respond to it.

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SUPER DEATH BENEFIT

ATO rules adult child is not a dependant despite disability

Adult children are not usually dependants for tax purposes. A recent private ruling shows that even a serious disability may not be enough for an adult child to satisfy dependancy. In the private ruling the adult child had severe medical conditions from childhood and needed 24-hour support for life. They saw their parent every week or two and the two took trips together. Even so, the ATO found the child was not the parent's dependant, so the taxable component of the parent's super death benefit was taxed.

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Understand why dependant status matters

A super lump sum death benefit paid to a tax dependant is tax free. A non-dependant pays up to 15% on the taxed element of the taxable component and up to 30% on any untaxed element. The 2% Medicare levy also applies.

A spouse, former spouse or child under 18 is automatically a dependant. An adult child has to show financial dependence or an "interdependency relationship" with the parent.

What were the circumstances

The child lived in private accommodation with support workers on hand 24 hours a day. They needed help with everything from showering and dressing to medication, meals and money.

The parent's own medical conditions limited the care they could give. After a seizure from a fall, the parent was diagnosed with further life-threatening conditions. Before the parent died, the child visited them in palliative care with two support workers.

The parent and child were close. The parent gave emotional support when the child's health suffered and gifted the child money in a term deposit. The ATO also had booking confirmations for trips they organised together.

The parent's SMSF paid the death benefit to the estate, to be held for the child.

Why did the ATO say the child was not an interdependant

An interdependency relationship needs four things: a close personal relationship, living together, financial support, and domestic support and personal care. If either person has a disability that stops them meeting any of the last three, the law can set those aside. A close personal relationship is always required.

The ATO accepted the term deposit as financial support. But it saw a typical parent and child relationship, with no evidence of a mutual commitment to a shared life.

The ATO noted that children are not generally expected to be in an interdependency relationship with their parents. The child's lifelong care needs did not change that view.

Reminder

A private ruling only binds the ATO for the person who asked for it, but it shows how the ATO approaches these cases. A disability on its own won't make an adult child a dependant for tax purposes. The relationship has to go well beyond the usual parent and child bond, and there has to be evidence to prove it. If you have an adult child with a disability, talk to us about how your super would be taxed if it is paid to them as a death benefit.

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PART IVA

WHERE TAX PLANNING CROSSES THE LINE

You're entitled to arrange your affairs to pay less tax. Choosing a business structure or timing an asset sale is ordinary planning. But Part IVA of the *Income Tax Assessment Act 1936*, Australia's general anti-avoidance rule, lets the ATO cancel a tax benefit where the dominant purpose is to get that tax benefit. That can happen even when every step follows the law.

Part IVA applies when three elements are present.

There is a scheme

"Scheme" is defined very widely. It covers any agreement, arrangement, understanding, transaction or course of conduct. The ATO can point to a whole restructure or one step inside it. Even not doing something can be part of a scheme.

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There is a tax benefit

The ATO compares what you did with what would reasonably have happened without the scheme. If that alternative would have cost more tax, you got a tax benefit, such as:

- a deduction you wouldn't otherwise have claimed
- income left out of your assessable income
- a capital loss you wouldn't otherwise have made
- withholding tax you didn't pay

Choices the tax law expressly gives you, such as certain elections and rollovers, are generally outside Part IVA, unless you set things up just so you could make the choice.

The dominant purpose was to get a tax benefit

The test is objective. What you think or say your purpose was doesn't decide it. If a reasonable person looking at the facts would conclude the dominant purpose was the tax benefit, the test is met.

The law lists eight factors to weigh, including how the arrangement was carried out, its form compared with its substance, its timing and the change in your financial position. Warning signs include:

- steps with no commercial reason
- money that goes round in a circle
- related-party dealings on terms strangers wouldn't accept
- a tax result that doesn't match the real economic outcome

Know the cost

The ATO can cancel the tax benefit and reassess you as though the scheme never happened. Penalties are 50% of the tax shortfall, or 25% if your position was reasonably arguable, plus interest charges.

Write down the commercial reasons

Your best protection is a genuine commercial reason recorded at the time. Board minutes, emails and file notes carry far more weight than an explanation put together once an audit starts. If asset protection is the reason, be ready to show the actual risk and why a simpler route wouldn't have worked.

Reminder

Before you restructure, move assets between family entities or change how business income is shared, talk to us. We can check the plan against Part IVA and help you keep the right records from day one.

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WHAT HAPPENS TO YOUR AGE PENSION IF YOU RETIRE OVERSEAS

If you retire overseas, you may still be able to receive the Age Pension, but some things change. The Pension Supplement and Energy Supplement stop the day you leave, and your Pensioner Concession Card is cancelled. After 26 weeks, your pension can be cut if you lived in Australia as a resident for less than 35 years between age 16 and Age Pension age.

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Claim before you go

You must normally apply for the Age Pension before you leave. On the day you claim, you must be an Australian resident and physically in Australia. You also need at least 10 years as an Australian resident in total, with at least 5 of those years in a row.

If you have already moved overseas, you generally can't claim unless you live in a country that has a social security agreement with Australia.

There is also a trap for people who live overseas and come back to Australia to claim. If you return to live in Australia, start the Age Pension and then move back overseas permanently within 2 years, your pension may be cancelled.

The rules are not as harsh if you are only travelling and intend to return. In that case, you keep the full Pension Supplement for up to 12 weeks and the Energy Supplement for 6 weeks while overseas. Your Pensioner Concession Card is cancelled after 6 weeks but will be reissued when you return, if you're still eligible.

Count your working life residence

After 26 weeks overseas, your base pension rate depends on your Australian Working Life Residence. That is the time you lived in Australia as a resident between age 16 and Age Pension age. It does not matter if you actually worked during those years.

With 35 years or more, your base pension rate generally stays the same, subject to the usual income and assets means test.

With less than 35 years, your pension is reduced in proportion. Someone with 20 years receives 20/35ths of their rate, or roughly 57%.

Say someone migrated to Australia at 40 and retires overseas at 67. Their working life residence is 27 years. Their base rate stays the same for the first 26 weeks overseas. After that they receive 27/35ths of it, or about 77%.

The rules can also vary depending on the country you move to.

Check for a social security agreement

Australia has agreements with a number of countries. If you are moving to one of them, the agreement may let you claim the Age Pension from overseas, count time spent in that country towards the 10-year residence rule, or claim a pension from the other country as well. The rate paid under an agreement is still usually proportional to your Australian Working Life Residence.

Tell Services Australia before you leave. You can do this through the Travelling outside of Australia service in your Centrelink online account.

Plan the whole move

The Age Pension is only one part of retiring overseas. Leaving Australia can change your tax residency, which affects how your income, investments and any property you keep here are taxed. Your super may be treated differently in your new country, and you may lose access to Medicare once you stop living here. You'll also want to think about health insurance, exchange rates, how a foreign pension could affect your Age Pension, and what happens to your estate plans under another country's laws.

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