WHITEHEAD DINGLEY & BETAR

# NEWSLETTER – CHRISTMAS 2007

As Christmas is fast approaching again I thought it topical to include the following information.

## Christmas fringe benefits

In general, entertainment provided by way of food, drink or recreation by an employer (or associate of the employer or a third party under an arrangement) to an employee (or an associate of the employee eg. relative, de facto spouse, partner) will be subject to FBT, deductible for income tax purposes and any input tax credits will be claimable for GST purposes. However there are many tips and traps within the tax legislation which may result in a different outcome for tax purposes, especially in relating to Christmas.

### Entertainment on employer's premises

Except for tax exempt organisations, if an employer provides food and drink to employees on the employer's premises on an ordinary working day the expenditure is exempt from FBT under the 'in-house property rules' and is deductible for income tax purposes.

If the food and drink is provided on the employer's premises at a social function, no FBT is payable and there is no income tax deduction.

However, if the food and drink is provided to associates of employees (eg. family members) on the employer's premises then that expenditure is not exempt from FBT. Notwithstanding this, if the food and drink provided to family members on the employer's premises is a 'minor benefit' (see below) and the value of the employee's and any family member's benefit is under $300 each then the expenditure will be exempt from FBT.

If the employee brings a client instead of a family member to the Christmas party, then in relation to the client's costs there is no FBT, but there is no income tax deduction either.

TIP: A Christmas party held on the premises on a working day with only employees and clients attending and where only finger food or a light meal is provided with no alcohol, then the entire cost is tax deductible. There is no FBT and a GST input tax credit can be claimed.

### Entertainment not on employer's premises

Generally, any function provided for employees not on the employer's premises is subject to FBT, except in limited circumstances. Christmas parties are exempt from FBT as minor benefits if the value of the benefit to the employee is under $300. This applies also to any family member attending (see 'Minor benefits' below).

TRAP: If employers use the 50/50 split method for meal entertainment, all meal entertainment must be split accordingly, including meal entertainment under the $300 minor benefit threshold which might otherwise be exempt.

*Example: An employer provides a Christmas party at a local restaurant for all employees. The catering cost per person is $210 for food and drink. Employees may bring their spouses to the function. If an employee attends the function with his spouse, the cost is below $300 per head, therefore there is no FBT liability as the cost qualifies as a minor benefit. The employer would not be entitled to claim a deduction for the cost of providing those benefits. If the cost per head is $300 or more for each employee or each associate of an employee, the total cost (not just the excess) is subject to FBT but a tax deduction is allowable for both the cost of the benefit and any FBT paid.*

TIP: A Christmas party held on the business premises on a working day is usually the most cost effective.

### Christmas party and a gift

For non-tax exempt employers, it may also be tax effective to provide both a Christmas party (at a cost of less than $300 GST-inclusive) and a gift, such as a Christmas hamper.

The Tax Office now accepts, that a separate gift value of less than $300 made at a Christmas function will be a minor benefit, provided that such a gift is made infrequently and the total value of the minor benefit and associated benefits made in the year and other years are not considered to be substantial. The gift and the party must be considered separately (see 'Minor benefits' below).

*Example: Big Company holds an annual Christmas party for its employees and their partners at a cost of $200 per head. At the party, each employee is provided with a hamper valued at $250. The employees do not receive identical or similar benefits during that or other FBT years. In that case the minor benefit exemption would apply. As the provision of the hampers is not an entertainment expense, an income tax deduction is allowed and a GST input tax credit may be claimed.*

### Multiple social events

It is sometimes more tax effective to provide a couple of events during the year than one large Christmas party. For example, an employer sets a budget at the beginning of the year of $550 per employee and per associate of the employee for all social events. The employer gives consideration as to whether to expend the total on one gala event at Christmas, or split the amount and also have an end of financial year event in July.

Minor benefits The general rule for employers is that 'minor' benefits are exempt from FBT if, in relation to identical or similar benefits, they are provided infrequently and irregularly, and the value is less than $300 from 1 April 2007 (less than $100 prior to 1 April 2007). It is important there is no pattern or regularity, and that the number supplied is small; eg. gifts of less than $300 to employees at Christmas and on birthdays are exempt.

NEWSLETTER

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Basically, to be an exempt minor benefit the employer needs to ensure that any associated identical or similar benefits are provided on an infrequent and irregular basis. The more often and regular that benefits are provided, the less likely the benefit will be a minor benefit.

Therefore an employer is effectively able to provide a Christmas party for employees and their associates for $299 per head and not pay FBT.

TRAP: The under $300 minor benefit threshold is the GST-inclusive amount. To the extent that a minor benefit is tax deductible, an input tax credit would be claimable. If the minor benefit involves the provision of entertainment, the expenditure will be non-deductible for income tax deduction purposes. In addition, input tax credits cannot be claimed for GST.

WARNING! Care should be taken when examining expenses in the ledger to determine minor benefits. Expenses need to be grossed-up to reflect the GST-inclusive amount.

TIP: This general rule does not apply to minor benefits provided by tax-exempt bodies such as certain public hospitals as defined in s.57A (FBTAA), public benevolent institutions (PBIs) or concessionally taxed (or rebatable) employers. For these employers the less than $300 minor benefit exemption applies in only two very limited circumstances.

*Example 1: An employee and his family are given a Christmas hamper to the value of $200. This is the only gift given during the year. The gift is a minor benefit and as the hamper is not considered to be 'entertainment' (TD94/55), the cost is tax deductible and exempt from FBT.*

*Example 2: Each employee is given a bottle of Scotch or a perfume valued at $80 and a bottle of champagne as a Christmas present. These are the only benefits received. The Scotch is not entertainment and is a minor benefit. The cost is therefore deductible to the employer and there is no FBT. The cost of the perfume and champagne are also deductible and not subject to FBT because it is a minor benefit.*

*Example 3: An employer puts on a Christmas function at an exclusive function centre, with employees and their partners attending. Food and drink are supplied at per head cost of $220. The venue engages a band at an effective cost of $30 per head, and also organises a fireworks display in the grounds of the centre. This display amounts to $60 per head, giving a total cost per head of $310. Because the entertainment has been organised by the venue, it cannot be argued that there is a separate benefit for each of the meals, band and fireworks display and therefore the minor benefit exemption will not apply.*

*Example 4: An employer gives each employee a Christmas hamper of festive goods valued at $200. Included in the hamper is a gift voucher for $200 for a major retailer. The fact that the voucher is included in the hamper suggests that the employee is the recipient of one gift and the value of $400 would preclude the minor benefit exemption applying.*

Multiple gifts may be eligible for the minor benefit exemption, but it is essential that the gifts are clearly of a separate and different nature. It is necessary to take into account the various criteria set out in s.58P(1)(f) of the *Fringe Benefits Tax Assessment Act* (for full details see the *2007 and 2008 Tax Summary* at 13.100).

WARNING! The minor benefit exemption is not available to employers using the 50/50 split method for meal entertainment expenses.

### Taxi fares

It is common for employers to pay for taxis to take employees, or clients, to and from the place of entertainment. For FBT purposes there may be different consequences for payment of the taxi fare depending on the recipient of the benefit.

•In respect of clients, the taxi fare is considered to be part of the entertainment expense and no income tax deduction is allowable. Input tax credits are not available.

For employees, if the fare is for travel from home to the place of entertainment (not being their place of employment), and return home again, the benefit is considered to be for the facilitation of entertainment and is not a separate benefit from the entertainment itself. The result is that the employer would then have to rely on the total entertainment package being under $300 for the minor benefit rule to apply.

However, if the Christmas function is held on the employer's premises and the employer pays for taxi fares from home to those premises and from there to home after the function, the benefit is exempt from FBT. The exemption applies provided that the trip is a single trip beginning or ending at the employee's place of work. The effect is that the taxi fare is exempt from FBT even if the function itself is subject to FBT.

The taxi exemption could apply if the employee went from the workplace to home, or any other place. However, the exemption would not apply if the trip was broken and continued at some other time. For example, the employee gets a taxi from the workplace and goes to a nightclub: that trip is income tax deductible and exempt from FBT. If the employee later gets a taxi home, that leg of the trip would be deductible to the employer but FBT would be payable.

While the taxi fare to and from work will be exempt from FBT, the cost will impinge on the minor benefits threshold. This is because one of the conditions of the minor benefits exemption is that the employer has to take into account the value of benefits provided in connection with the minor benefit. Because the taxi fare is connected with the provision of the function, it effectively means that unless the entire package (function and taxi) is less than $300, the function costs would not be treated as a minor benefit.

### Gifts to clients

For gifts of alcohol or food hampers to clients, an income tax deduction is allowable provided they are taken away for private consumption (ie. not given in circumstances where there is immediate consumption such as would occur at a restaurant). Gifts of other items such as perfume etc. would also be deductible and input tax credit allowable. The Tax Office view on what constitutes 'entertainment' is contained in TR 97/17.

### Gifts to employees

As a general rule, any gifts provided to an employee or an associate of the employee (eg. family members) by the employer are subject to FBT because those benefits constitute a 'property fringe benefit'. However there are exceptions that can be used to eliminate any FBT liability and effectively provide a tax-free benefit to employees.

Separate to the minor benefits exemption discussed above, there are many benefits which are specifically exempt from FBT. The exemptions could be used to provide employees with Christmas presents. To be exempt the benefit must be provided to an employee (not an associate of the employee). These exempt benefits include a myriad of electronic gagetry, which if anyone is interested we can supply details.:

In each case the employer can claim an income tax deduction and input tax credits.

### Taxable value of meal entertainment

For FBT purposes, there are various options to determine the taxable value of meal entertainment. If the employer chooses not to adopt any of the options, the employer pays FBT based on the actual cost of the entertainment provided to employees or their associates.

*Example: Actual cost basis: An employee takes a customer to a business lunch and the employer reimburses the employee for the total cost. The tax consequences are as follows:*

Cost of the employee's lunch is deductible and subject to FBT.

Cost of the customer's meal is not deductible to the employer and is not subject to FBT.

Only the proportion of GST charged on the deductible employee portion is available to be claimed *as an input tax credit.*

TIP: The Tax Office allows the cost of the meal to be allocated on a per head basis to determine what part of the meal is subject to FBT (employee's portion) and which part of the meal is not subject to FBT. This simplifies matters, as taxpayers do not have to submit details of consumption by particular individuals.

WARNING! Taxpayers should ensure that they are not over claiming input tax credits by including the non-deductible portion of meal entertainment as part of their input tax credit entitlement for GST purposes.

### Examples of different types of benefits that may arise from the provision of entertainment are –

Cost of theatre tickets purchased by employee and reimbursed by employer. This would be an expense payment fringe benefit and not meal entertainment.

Provision of food and drink by the employer to the employee. This would generally be considered provision of a property fringe benefit and not meal entertainment unless the circumstances in which it is provided confer an element of entertainment. (eg. if the employer reimbursed an employee's weekly food and drink consumption). If the employer reimbursed an employee for food or drink provided in a social situation (eg. restaurant meals, family social events such as a wedding, engagements, birthdays etc), then this would be considered meal entertainment and not a property fringe benefit. Likewise, if the employer reimbursed an employee for elaborate dinner parties then this could arguably qualify as meal entertainment. To be considered meal entertainment, the food and drink must be consumed soon after it is provided. Getting your employer to purchase your weekly alcohol requirements will unfortunately not qualify as the provision of meal entertainment. Reimbursement of alcohol provided as part of any social arrangements (ie. parties, social events such as birthdays etc.) may however qualify.

### Christmas entertainment guide

The following guide provides a quick reference to FBT and income tax teatment of each circumstance.

- If under $300 and irregularly provided, no fringe benefits tax is payable. (minor benefit threshold was less than $100 prior to 1/4/07). If meal entertainment then the cost would be non-deductible for income tax and no GST input tax credit claimable.
- If a meal while travelling includes additional entertainment eg. floor show, allocate costs on non-travelling basis (ie. item 3a).

- If travelling for dominant purpose of attending entertainment function then allocate costs as if non-travelling.
- For "Non-Employee's", if the travelling person is not on Company business eg. spouse of consultant, then allocate costs as if non-travelling.
- Meal entertainment is not a reportable fringe benefit.
- GST input tax credits are claimable if expenditure is deductible for income tax purposes.

## Tax offsets for over 55s

If you've made it this far, then you may be entitled to the Senior Australian Tax Offset, (SATO) which I detail below, along with a few explanations.

SATO Table

| | Single | Married | Married (apart) |
|---|---|---|---|
| Max tax offset | $2,230 | $1,602 | $2,040 |
| Shade out start | $24,867 | $20,680 | $23,600 |
| Cuts out at | $42,707 | 33,496 | $39,920 |

Question 1: Can a person be entitled to both the mature aged worker tax offset (MAWTO) and the low income tax offset (LITO) at the same time?

Yes, it is possible for a person to be entitled to both MAWTO and LITO. However, both of these tax offsets have different eligibility criteria.

MAWTO is available to residents aged 55 and over at the end of that financial year with a net working income of $63,000 or less. The maximum MAWTO available to an individual is $500, when net working income is between $10,000 and $53,000. Net working income is basically income from working (excluding termination payments and passive income) less deductions relating to earning the income.

LITO is available to residents whose taxable income is less than $40,000.Themaximum tax offset available is $600 for taxpayers with taxable income of $25,000 or less in the 2006-07 financial year.

A person who is entitled to the maximum amount available under LITO and MAWTO can earn up to $13,333 in the 2006-07 financial year and $14,333 in the 2007-08 financial year without paying any income tax. The 2007-08 year amount is calculated based on the maximum LITO amount of $750 as announced in the last Budget.

Question 2: Can a person be entitled to both Senior Australian Tax Offset (SATO) and the Pensioner Tax Offset at the same time?

No, SATO and the Pensioner Tax Offset are mutually exclusive. Each of these offsets has different eligibility criteria, and their own set of income thresholds. The following table is a comparison between both of these offsets for the 2006-07 financial year:

Evidently, for a person entitled to both of these offsets, it is more beneficial to choose SATO over the Pensioner Tax Offset as it provides a greater offset and at correspondingly higher income levels before the offset is affected. The only people who are likely to

benefit from the Pensioner Tax Offset will be those who are below the age for the Age Pension but in receipt of a government pension.

Note: Unlike the Pensioner Tax Offset, SATO only requires a person to be eligible for a government pension, and not necessarily in actual receipt of a pension.

Question 3: In the circumstances where a person is entitled to SATO and LITO, which of these offsets takes precedence and how will this affect the transfer of unused SATO to a spouse?

Both SATO and LITO are non-refundable rebates and therefore the order of application of SATO and LITO will not be relevant. This sequence of application is also not relevant when calculating the transfer portion of unused SATO to a spouse because this unused portion is the difference between the entitlement to the pension rebate and tax calculated on the greater of the taxable income or notional taxable income without taking into account other tax offsets and credits.

Note: Notional taxable income is taxable income plus any exempt Social Security and Veteran's Entitlement pension income.

## CLOSURE OF OFFICE

We will be closing the office from mid-day on Friday 21 December 2007 until 9am Monday 14 January 2008. This period covers the Christmas/New Year break, plus an extra week.

Therefore on behalf of us all here, I wish everyone a Happy and Holy Christmas and a prosperous New Year.