Tax Talk – October/November 2009

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Christmas Parties and Fringe Benefits Tax

Are Your Celebrations Tax Deductible?

As we approach the festive holiday season, the ATO has put out a reminder about the FBT and tax deduction implications for company Christmas parties. How is your organisation affected?

Exempt property benefits

The costs (such as food and drink) associated with Christmas parties are exempt from FBT if they are **provided on a working day on your business premises and consumed by current employees**. A taxable fringe benefit will arise in respect of an associate of an employee who attends the party if not otherwise exempt under the minor benefits exemption.

The provision of a Christmas party to an employee may be a minor benefit and exempt if the cost of the party is less than $300 per employee and certain conditions are met. The benefit provided to an associate of the employee may also be a minor benefit and exempt if the cost of the party for each associate of an employee is less than $300. For the FBT year beginning 1 April 2006 and prior years, the minor benefits threshold was less than $100 rather than less than $300.

Gifts provided to employees at a Christmas party

The provision of a gift to an employee at Christmas time may be a minor benefit that is an exempt benefit where the value of the gift is less than $300.

Where a Christmas gift is provided to an employee at a Christmas party that is also provided by the employer, the benefits are associated benefits, but each benefit needs to be considered separately to determine if they are less than $300 in value. If both the Christmas party and the gift are less than $300 in value and the other conditions of a minor benefit are met, they will both be exempt benefits.

Tax deductibility of a Christmas party

The cost of providing a Christmas party is income tax deductible only to the extent that it is subject to FBT. Therefore, any costs that are exempt from FBT (that is, exempt minor benefits and exempt property benefits) cannot be claimed as an income tax deduction. The costs of entertaining clients are not subject to FBT and are not income tax deductible.

Christmas party held on the business premises

A Christmas party provided to current employees on your business premises or worksite on a working day may be an exempt benefit. The cost of associates attending the Christmas party is not exempt, unless it is a minor benefit.

Example

A small manufacturing company decides to have a party on its business premises on a working day before Christmas. The company provides food, beer and wine. The implications for the employer in this situation would be as follows.

If…	Then…
current employees only attend	there are no FBT implications as it is an exempt property benefit.
current employees and their associates attend at a cost of $180 per head	there are no FBT implications as the minor benefit exemption applies.*
current employees, their associates and some clients attend at a cost of $365 per head	for employees – there are no FBT implications as it is an exempt property benefit for associates – a taxable fringe benefit will arise as the value is more than $300 for clients – no FBT payable and no income tax deduction.

* Where the benefits are indicated as qualifying for the minor benefits exemption, it is on the basis that the necessary conditions have been satisfied.

Christmas party held off business premises

The costs associated with Christmas parties held off your business premises (for example, a restaurant) will give rise to a taxable fringe benefit for employees and their associates unless the benefits are exempt minor benefits.

Example
Another company decides to hold its Christmas function at a restaurant on a working day before Christmas and provides meals, drinks and entertainment.
The implications for the employer in this situation would be as follows.

If…	Then…
current employees only attend at a cost of $195 per head	there are no FBT implications as the minor benefits exemption applies.*
current employees and their associates attend at a cost of $180 per head	there are no FBT implications as the minor benefits exemption applies.*
current employees, their associates and clients attend at a cost of $365 per head	for employees – a taxable fringe benefit will arise for associates – a taxable fringe benefit will arise, and for clients – there is no FBT payable and the cost of providing the entertainment is not income tax deductible.

* Where the benefits are indicated as qualifying for the minor benefits exemption, it is on the basis that the necessary conditions have been satisfied.

Economic Focus

A Slow Recovery

Economic data during the September quarter confirmed that a global economic recovery is underway but the strength and sustainability of that recovery remains questionable.

Volatility returned to share markets during October after inconsistent data created nervousness amongst investors. Markets are often vulnerable to negative surprises when expectations are high and there is a feeling that they have got ahead of themselves.

The US economy grew in the September quarter for the first time in a year but this news was negated by a sharp fall in consumer confidence and an unexpected decline in new home sales. Other data such as retail sales and manufacturing surprised on the upside but continues to lag the levels seen during robust economic times.

The sceptics claim the economic growth in the September quarter has been distorted by government stimulus such as the 'cash for clunkers' scheme and that the US needs more real, organic growth before a recovery can be properly established.

The key factor is a sustained increase in consumer spending and this will be hard to achieve while unemployment remains at current levels.

Most other developed economies recommenced growth in the last quarter, led by Germany, France and Japan. However, deteriorating labour markets and only slight increases in domestic demand point to a very slow recovery.

The UK economy continues to contract and may be in for another miserable winter. In contrast, China's economic growth is on target to reach 8% for the year.

Due to stronger economic conditions, Australia is the first developed economy to raise interest rates (closely followed by Israel and Norway). Most economic data released during October supports this decision with the sharp improvement in economic growth surprising even the most positive economists.

The Reserve Bank has promised to return rates to more normal levels and how aggressively they implement the tightening cycle will be seen in the next few months.

The seven month rally on major global share markets finally met with some resistance by the end of October. The general consensus is that shares have moved from being ridiculously cheap to fair value.

We may be looking at a period of consolidation as the market waits to see how the economic recovery affects corporate profits in the next six months.

Superannuation Focus

Excess contributions can cost you

As a result of the changes to the superannuation contribution caps, now is an appropriate time to review your contributions strategy for this financial year. Making excessive contributions could cost much more than you realise.

Concessional contributions made to superannuation are subject to an annual cap of $25,000. Concessional contributions include employer contributions and personal contributions claimed as a tax deduction by a self-employed individual. Until 30 June 2012, a transitional concessional contributions cap of $50,000 applies to people aged 50 or over.

Your fund is taxed at the rate of 15% for concessional contributions up to the cap but, in excess of that cap, the member is taxed at a further 31.5%. Your superannuation fund can release money to pay this excessive contributions tax or you can pay with monies outside superannuation. The excessive amount also counts towards your non-concessional contributions cap.

The non-concessional contributions cap is $150,000 per annum and those under 65 can bring forward two years worth of contributions, giving them a cap of $450,000 over three years. Where an excess non-concessional contributions event occurs, the excess amount is taxed at 46.5%.

But the real sting occurs if you simultaneously breach both the concessional and non-concessional caps.

Case Study

Harry, 64, is self-employed and plans to retire next year so he is trying to get as much money into superannuation while he is still eligible to contribute. Last year he made a non-concessional contribution of $450,000 so he cannot make further contributions this year without exceeding the cap. However, he can still make concessional contributions this year. Unfortunately, Harry is not aware that the concessional cap has been halved to $50,000 for the 2009-10 year and proceeds to make a $75,000 contribution.

Harry has exceeded the concessional contributions cap by $25,000. Therefore, he will pay the 15% contributions tax ($3,750) and another 31.5% ($7,875) because he has exceeded the concessional cap. The excess concessional amount also forms part of the non-concessional amount. As he has maximised the amount of non-concessional contributions he can make this year, a further 46.5% ($11,625) in tax is payable. This means that he pays 93% ($23,250) of the excessive $25,000 in taxes.

Insurance Focus

Business Insurance

People own life insurance to provide financial support to their spouse and/or family in the event of their untimely death. Life insurance is easily the most popular form of risk insurance in Australia because most people consider their family as their most important asset.

For many, their second most important asset is their business as this dictates the type of lifestyle that their family can have now and in the future.

Therefore, it would make sense to insure against an event that may prevent that business from functioning properly. There are three types of business cover which appear similar but can be differentiated when closely examined.

Business expense insurance covers the fixed costs of running a business if the insured cannot work due to sickness or injury. It is generally designed for the self-employed but some providers will cover small partnerships as well. It is paid as a monthly benefit for periods up to a year and has a waiting period as well.
Key person insurance is a life insurance policy that a company can purchase to insure against the death or incapacitation of a key executive or employee. The principle is that the proceeds go back into the business to help it survive the loss of the key person. The proceeds of a key person insurance benefit would ordinarily go towards offsetting the costs of hiring a temporary replacement or recruiting a successor. In this transitional phase, there will often be a temporary loss of production as well.

Buy-sell agreements are binding contracts between owners/partners about the future ownership of the business. It involves one partner being bound to buy out the other partner's share in the business should a specific event occur e.g. death, divorce, disability or retirement.

The most common type is the cross-sell agreement where upon the death or serious illness of the owner, the other business owner(s) purchase the share.

The agreement is often linked to an insurance policy on each partner's life and, therefore, becomes part of the partner's estate planning. In most cases, legal advice would be required.

Happy Holidays!

Whatever your holiday plans this season, whether you are planning to celebrate here in the local area or travel elsewhere, the entire staff of both offices of CRM Business Advisors wish you and your families the happiest of holidays.

Our offices will be closed for the holiday season from 12pm on Thursday the 24th of December until 8:30am on Monday the 11th of January.

The next issue of Tax Talk will be published in mid-January.

Merry Christmas!