CHARTERED ACCOUNTANTS PROGRAM AUSTRALIA · NEW ZEALAND

Taxation (2) 2017 (TAXAU)

Taxation Australia

Assumed knowledge quiz questions and solutions

Assumed knowledge quiz

Questions

Question 1

Which of the following statements most accurately describes assessable income under s. 6-5?

(a) Assessable income consists of ordinary income and statutory income.

(b) Assessable income includes all amounts over the tax-free threshold of $18,200.

(c) Assessable income is the difference between total incomes less allowable deductions.

(d) Assessable income does not include statutory income.

Question 2

A prepayment for trading stock is not an allowable deduction because:

(a) It is not incurred for the purpose of s. 8-1.

(b) It is incurred under s. 8-1, but is of a capital nature.

(c) It is incurred under s. 8-1, but qualified by s. 70-15 (in that it must be 'on hand').

(d) Prepayments are not an allowable deduction under s. 8-1.

Question 3

Jason and Kevin formed a partnership in which it was agreed to share profits and losses equally. As Kevin would be the more active partner in the business it was agreed that he be paid a $20,000 salary.

The accountant has finalised the partnership results for the 2016–2017 tax year and has advised the partners that the partnership net result was a loss of $10,000 after paying Kevin the agreed salary.

For the purposes of completing the statement of distribution on the partnership tax return, what is the partnership net income or loss?

(a) Loss of $10,000.

(b) Nil taxable income.

(c) Profit of $10,000

(d) Loss of $30,000.

Question 4

Which of the following legal jurisdictions is not appropriate if a taxpayer is dissatisfied with an objection decision, and wishes to appeal the decision?

(a) Administrative Appeals Tribunal (AAT).

(b) Federal Court.

(c) High Court.

(d) District Court.

Question 5

Which of the following statements most accurately reflects the pay as you go (PAYG) withholding system?

(a) Applies to companies, super funds, and individuals with business or investment income.

(b) It is used to collect income tax, higher education loan program repayments, and Medicare payments.

(c) The notional tax adjusted for movements in the consumer price index (CPI) payable in instalments to the Australian Taxation Office (ATO).

(d) The amount withheld from contractors who do not supply an Australian Business Number (ABN).

Question 6

You are a graduate accountant working in a professional accounting office. You have been asked to prepare an analysis of which items would be included as assessable income for a client who is an individual resident taxpayer. From the list below, which items would you include as assessable income?

1. A trust distribution of $6,000 from the Smith Family Trust.
2. Interest from Australian sources: $600.
3. Interest received from the United Kingdom: $900.
4. Gross-up interest for withholding tax: $100.
5. Dividend from Australian sources: $500.
6. Franking credit for dividend: $214.
7. Recoupment of Medicare: $250.
8. Capital gain from the sale of taxpayer's home: $200,000.
9. Capital gain from the sale of shares held prior to 20 September 1985.
10. Legacy from the estate of the late L. Jones: $25,000.
11. Income from the estate of the late L. Jones as advised by the trustee: $7,550.

(a) 1, 2, 5, 6, 10, 11.

(b) 1, 2, 3, 4, 5, 6, 11.

(c) 1, 2, 3, 4, 5, 6, 7, 11.

(d) 1, 2, 3, 4, 5, 6, 9, 10, 11.

Question 7

You are provided with the following information on the accounts receivable of Havelock Limited for the year ended 30 June 2017. What is the amount included in the taxable income for Havelock Limited based on the cash and accrual methods of deriving income?

Opening debtors (01.07.2016)	$300,000
Cash received	$600,000
Closing debtors	$250,000

	Accrual basis	Cash basis
(a)	$300,000	$600,000
(b)	$650,000	$600,000
(c)	$550,000	$600,000
(d)	$250,000	$600,000

Question 8

Morris Mansfield, aged 55, derived $92,000 in salary and received $3,820 in fully franked dividends from companies with a corporate tax rate for imputation purposes of 30%. His deductions, which all relate to earning his salary, totalled $5,780. Morris has the highest level of private hospital health insurance cover. Tax paid during the 2016–2017 year on Morris's salary totalled $29,985.

On the basis of this information, what will be Morris's tax refund for the 2016–2017 tax year?

Current tax rates (excluding Medicare levy 2%)

Taxable income $	Tax payable $
0 – 18,200	Nil
18,201 – 37,000	Nil + 19% of excess over $18,200
37,001 – 87,000	3,572 + 32.5% of excess over $37,000
87,001 – 180,000	19,822 + 37% of excess over $87,000
180,001 +	54,232 + 47% of excess over $180,000 (includes 2% temporary budget repair levy)

(a) $8,236.11.

(b) $7,237.40.

(c) $6,598.97.

(d) $8,432.51.

Question 9

In determining assessable income for a taxpayer carrying on a business, it is necessary to determine when income is derived. In this case, the taxpayer was a gymnasium, and accepted prepayments for a 12-month membership. A discount was also offered to encourage membership.

From case law listed below, which is the most likely to represent the precedent for derivation of income for prepayments?

(a) *FC of T v. Applegate* 79 ATC 4307.

(b) *FC of T v. Western Suburbs Cinemas Ltd* (1952).

(c) *RACV Insurance Pty Ltd v. FC of T* 74.

(d) *Arthur Murray (NSW) Pty Ltd v. FC of T* (1965) 114 CLR 314.

Question 10

At 30 June, a company has franking account credits of $19,000 and debits of $20,000. Which of the following statements is the least likely explanation for this position?

(a) The company has over-franked.

(b) The company has paid less tax than expected.

(c) The company has received less dividends than expected.

(d) The benchmark rate for all dividend distributions was not the same during the tax year (i.e. 12 months).

Question 11

For tax purposes, private and public companies must be distinguished for which of the following reasons?

(a) Private companies are taxed at a higher rate.

(b) Dividends paid by private companies can only be franked to 50%.

(c) Certain loans and payments to persons associated with private companies may be deemed as dividends.

(d) A rebate of tax applies to private company dividends.

Question 12

Phillip Rich is employed by a local bank and receives as part of his salary package a low interest loan. On 1 April 2016, Phillip borrows $100,000 at 4% to fund the purchase of a residential property. The benchmark interest rate for fringe benefits tax (FBT) is 5.65%.

Which of the following amounts is the annual taxable value of the loan fringe benefit (before ‘gross-up’)?

(a) $4,000.

(b) $1,650.

(c) $3,235.

(d) $5,650.

Question 13

Which of the following is not an essential feature of FBT for the FBT year ended 31 March 2017?

(a) FBT is a broad-based consumption tax.

(b) The FBT tax is levied at 49% of the grossed-up value for the current FBT year.

(c) The FBT tax is paid by employers regardless of the type of entity.

(d) FBT is available as a deduction to the employer in respect of benefits provided.

Question 14

For the FBT year commencing 1 April 2016, the telephone bills of Jean Lock are paid by the employer. The bills totalled $660. Jean contributes $220 to the cost, and the business use is 30%.

What would be the taxable value of the benefit for FBT purposes?

(a) $440.

(b) $462.

(c) $242.

(d) $519.

Question 15

David Brown pays John Stone $50,000 in a non-competition contract not to open a pizza restaurant in the same suburb as David's restaurant. He also pays John $5,000 to advertise his (David's) restaurant on his (John's) car. How much income according to ordinary concepts is earned by John?

(a) $55,000.

(b) $0.

(c) $5,000.

(d) $50,000.

Question 16

Which of the following represents the FBT year of tax?

(a) 1 April to 31 March.

(b) 1 January to 31 December.

(c) 1 July to 30 June.

(d) 1 February to 31 January.

Question 17

In *FCT v. Dixon* (1952) 86 CLR 540, the taxpayer voluntarily enlisted in the armed services to serve as a soldier. Prior to the taxpayer's enlistment, the Company had sent a circular to its staff which stated that should any of its staff enlist in the armed services it would endeavour to make up the difference between their civilian and military wages. In the income year ending 30 June 1943, the taxpayer was paid £104 by way of periodic payments from the Company in accordance with its earlier undertaking. These payments supplemented his military wages, providing him with the equivalent of what his civilian wages would have been had he remained employed by the Company.

Which of the following definitions is most likely to uphold the High Court decision in relation to the characteristics of ordinary income?

(a) Income has the characteristics of a lump sum benefit.

(b) Income is a quantifiable amount, calculated with reference to a predetermined rate.

(c) Income is periodic, regular, expected and relied upon.

(d) Income can only exist between the relationship of employer and employee.

Question 18

On 1 July 2016, a taxpayer that is not a small business entity acquired a new depreciating asset at a cost of $3,000,000.

The taxpayer elects to use self-assessment to determine the effective life of the asset. The life of the asset is six years, with a residual value of $100,000. As the taxpayer wishes to maximise its deductions for the 2016–2017 tax year, it has chosen to use the diminishing value method in claiming a deduction for the decline in value of the asset.

What is the decline in value for the year ended 30 June 2017 (ignoring the impact of leap years)?

(a) $483,333.

(b) $500,000.

(c) $1,000,000.

(d) $966,667.

Question 19

Fastforward Pty Ltd is a resident company that is not a small business entity. It acquired a depreciating asset for $60,000 on 1 October 2016 and first used the asset on the same day solely for a taxable purpose. The estimated effective life of the asset is eight years and the company elects to use the prime cost method.

What is the decline in value for the year ended 30 June 2017 (ignoring the impact of leap years)?

(a) $7,500.

(b) $5,625.

(c) $5,610.

(d) $11,250.

Question 20

Which of the following statements best describes the anti-avoidance provision in Part IVA of the ITAA 1936?

(a) A scheme, a tax benefit and the dominant or principal purpose of obtaining a tax benefit.

(b) A financing arrangement, a deduction and tax evasion.

(c) Fraud, non-disclosure and non-lodgement of an income tax return.

(d) Voluntary disclosure of tax avoidance, the non-lodgement of the income tax return and tax evasion.

Question 21

In preparing the business activity statement (BAS) for the period July to September 2015, the following information is supplied.

	$
Total sales that are taxable supplies (including GST)	33,000
GST-free sales	1,500
Export sales	4,400
Purchases related to taxable supplies (including GST)	22,000
Input taxed supplies	1,100
PAYG income tax instalment	5,000
PAYG instalment	2,500

What amount will be remitted to the ATO for the September 2015 BAS?

(a) $8,500.

(b) $8,400.

(c) $8,800.

(d) $8,900.

Question 22

Elis Yang, a dentist, commenced practice on 1 July 2015 when she purchased the client base and the premises of a retiring dentist. During the year ended 30 June 2017, Elis incurred the following expenses:

10 July 2017	Replaced the front window of the surgery which had rotted – $2,000
16 August 2017	Removed part of the front fence to allow patients better access to the car park – $1,000
4 May 2017	Replaced three roof tiles after a tree branch had fallen over the roof – $200

What will be the deduction claimed for repairs under s. 25-10 for the year ended 30 June 2017?

(a) $200.

(b) $3,000.

(c) $1,000.

(d) Nil.

Question 23

An individual taxpayer carries on a business in their own name. Assume the business does not satisfy the definition of a small business entity. The individual incurred the following expenditure in connection with obtaining a 10-year bank loan of $200,000 at a rate of 7.5% from 31 March 2017:

Legal fees	$1,600
Procuration fees	$400
Valuation of security (taxpayer's home)	$80

The loan proceeds were used by the taxpayer as follows:

Discharge of existing mortgage on taxpayer's home	$40,000
Expansion of factory	$100,000
Financing working capital needs of taxpayer's business	$60,000

What is the total deductions the taxpayer can claim on their 30 June 2017 income tax return?

(a) $3,820.

(b) $2,992.

(c) $3,740.

(d) $3,072.

Question 24

The small business entity (SBE) provisions contain the following capital allowance concessions for depreciating assets:

Description	Method	Depreciation rate
Asset cost less than threshold The threshold is: • From 1 Jan 2014 (excluding the period from 7:30pm 12 May 2015 to 30 Jun 2017) – $1,000 • For the period from 7:30pm 12 May 2015 to 30 June 2017 – $20,000	Immediate write-off	100%
Asset cost greater than threshold and acquired in current year	Allocate to a general small business pool	15% diminishing value
Asset cost greater than threshold and acquired in prior year	Allocate to a general small business pool	30% diminishing value

Lauritz operates a restaurant. The restaurant is a small business entity (SBE) and Lauritz has chosen to apply the SBE capital allowance concessions.

The fixed asset register maintained by Lauritz shows that the restaurant business first used all of the following assets from 1 July 2016.

Description	Cost $	Estimated life (years)
Tables 60 @ $400 each	24,000	13
Chairs 180 @ $150 each	27,000	13
Refrigeration unit	30,000	10
Oven	25,000	20
Cooking hotplate	22,000	20
Stainless steel bench	28,000	13
Cutlery and crockery	21,000	5

What is Lauritz's tax deduction from the use of the assets in income year ended 30 June 2017?

(a) $72,000.

(b) $87,750.

(c) $26,550.

(d) $103,500.

Question 25

Jordon Electrics Pty Ltd (JEL) is a resident private company. It provided the following information in relation to the current income tax year:

	$
Accounting net profit	800,000
Details of amounts included in the accounting net profit:	
Accounting depreciation	90,000
Profit on disposal of capital assets	150,000
Provision for long service leave	160,000
Provision for doubtful debts	60,000
Details of amounts not included in the accounting net profit:	
Net capital gain	80,000
Depreciation for taxation purposes	120,000
Bad debts written off	30,000

What is JEL's taxable income in the current income year?

(a) $1,040,000.

(b) $890,000.

(c) $920,000.

(d) $500,000.

Question 26

Bowen Night Pty Ltd (Bowen) is a resident private company and is not a small business entity (i.e. it has a corporate tax rate of 30%). Its taxable income (excluding franking credits) for the current income tax year is $248,000, comprising trading income of $200,000, dividend income of $28,000 that is fully franked from a resident public company with a corporate tax rate for imputation purposes of 30%, and dividends of $20,000 that are franked to 70% from a resident private company with a corporate tax rate for imputation purposes of 30%.

What is Bowen's net tax payable for the current income tax year?

(a) $79,800.

(b) $74,400.

(c) $61,800.

(d) $60,000.

Question 27

Leisure Goods Pty Ltd (Leisure) is a resident private company. It has income from the provision of professional services of $180,000 per quarter and realised capital gains of $6,000. The instalment rate issued by the Commissioner of Taxation is 12%.

What is Leisure's PAYG amount per quarter?

(a) $21,600.

(b) $22,320.

(c) $27,000.

(d) $54,000.

Question 28

On 1 May 2017, Ritz Limited (Ritz), a car manufacturer, ordered parts from the United States. The invoice price at this order date was $US250,000 and the exchange rate was A$1.00 = US$0.65. The goods were delivered on 21 May 2017 when the exchange rate was A$1.00 = US$0.65. However, when the account was paid, on 15 June 2017, the exchange rate was A$1.00 = US$0.60.

What is Ritz's foreign exchange gain or loss for taxation purposes for the income year ended 30 June 2017?

(a) $12,500 gain.

(b) No exchange gain or loss.

(c) $12,500 loss.

(d) $32,052 loss.

Question 29

During the current income tax year a taxpayer, Adele Ho, made a capital gain of $100,000 from the sale of land and a capital loss of $10,000 from the sale of shares. She also has prior year carry forward capital losses from the sale of shares that total $30,000. Adele elects to use the capital gains tax (CGT) discount method to determine her net capital gain.

What is Adele's assessable net capital gain for the current income tax year?

(a) $30,000.

(b) $60,000.

(c) $15,000.

(d) $45,000.

Question 30

Jennifer is a member of the Australian women's basketball team, and was hit by a motor vehicle while crossing a road in Queensland, Australia. Jennifer was no longer able to play basketball due to her injuries. The driver was insured with a Queensland insurance company, RACQ Insurance, which paid her an undissected lump sum of $2 million in settlement for claims of loss of earning capacity and medical costs.

ITAA 1997 lists 12 discrete categories of CGT events. Some events, such as the disposal of a CGT asset, occur frequently, while other events have limited application. The 12 categories of CGT events are as follows:

1. Disposal of a CGT asset – CGT event A1.
2. Use and enjoyment of the asset before title passes – CGT event B1.
3. End of a CGT asset – CGT events C1–C3.
4. Bringing into existence a CGT asset – CGT events D1–D4.
5. Events relating to trusts – CGT event E1–E9.
6. Events relating to leases – CGT events F1–F5.
7. Events relating to shares – CGT events G1–G3.
8. Special capital receipts – CGT events H1 and H2.
9. Australian residency ends – CGT events I1 and I2.
10. CGT events relating to rollovers – CGT events J1, J2, J4–J6.
11. Other CGT events – CGT events K2–K12.
12. Events relating to consolidated groups and multiple entry consolidated (MEC) Groups – CGT events L1–L8.

Which CGT categories, from the list above, would the lump sum payment of $2 million fall into?

(a) D1–D4 and C1–C3.

(b) K2–K12.

(c) A1.

(d) H1–H2.

Question 31

Jason Rawlins accepts employment with a firm of accountants. He learns that promotion within the firm depends upon the standard of his work and the attainment of a degree in accounting. As a consequence of this knowledge, Jason enrols as a part-time student in an accounting degree program and incurs the following expenses:

	$
Student union fees	$89
Books	247
Photocopying	45
Purchases of writing materials	70
Travelling expenses from work to university	276
Higher Education Assistance/HECS/HELP	983

What deductions, if any, is Jason entitled to claim?

(a) $477.

(b) $727.

(c) $1,460.

(d) $201.

Question 32

Complete Tapware is a small manufacturer of tapware. In order to secure new warehouse premises, Complete Tapware was required to prepay two years rent at a cost of $25,000 per annum. The lease commenced on the 1 May 2017. The taxpayer has elected not to apply the small business entity (SBE) concessions.

What is Complete Tapware's deduction in respect of prepaid rent for the year ended 30 June 2017 (ignoring the impact of leap years)?

(a) $25,000.

(b) $50,000.

(c) $4,178.

(d) $8,616.

Question 33

The trustee of the XYZ Trust makes a distribution of $40,000 to James Bennett, who is mentally handicapped, and presently entitled to the distribution.

Which of the following statements most accurately reflects the status of the beneficiary?

(a) The beneficiary is presently entitled to a share of the net income of a trust estate.

(b) The beneficiary is presently entitled to a share of the net income of a trust estate but is under a legal disability.

(c) The beneficiary is not presently entitled.

(d) The beneficiary cannot receive any distribution from the trust.

Question 34

Sue and Allan are the only two beneficiaries of a discretionary trust created by their grandfather. Sue resides in the United States and Allan is a resident of Australia.

The beneficiaries are aged 22 and 17 respectively.

During the 2016–2017 year, the trustee received a net dividend of $3,400 from a company resident in the USA, on which withholding tax at 15% had been deducted at source, and a fully franked dividend of $3,300 that is fully franked from a resident Australian company that has a corporate tax rate for imputation purposes of 30%.

What amount is included in Sue's taxable income if the trust distribution is distributed equally between the beneficiaries?

(a) Nil.

(b) $4,357.

(c) $2,357.

(d) $4,057.

Question 35

Which of the following statements is true of trusts?

(a) Dividends are 'grossed-up' for partnerships but not for trusts.

(b) Trust losses are trapped within the trust and cannot be distributed to beneficiaries.

(c) Beneficiaries with a legal disability are not considered to be 'presently entitled'.

(d) Capital gains/losses in trusts must be distributed equally to each beneficiary.

Question 36

Which of the following statements most accurately reflects the status of a complying superannuation fund?

(a) A complying superannuation fund is taxed concessionally at 15% (except for special income).

(b) A complying superannuation fund does not receive concessional tax rates.

(c) Investment earnings received by a complying superannuation fund from its investments are taxed at 30%.

(d) Rollovers into a complying superannuation fund are taxed at 5%.

Question 37

Jane Wakefield is aged 59 years and is eligible for a pension under the Veteran's Entitlement Act 1986 (Cth). During the 2016–2017 income tax year her income comprised:

- Superannuation pension (income stream from her complying superannuation fund made up of $10,000 taxable component and $6,670 tax-free component).
- Interest as per Australian bank statements: $47.
- Net interest received from the UK: $900 (10% withholding tax was deducted).

Jane is entitled to tax deductions of $247 and her bank statements showed that $22 in TFN tax was paid.

What is Jane's taxable income for the income year ended 30 June 2017?

(a) $17,470.

(b) $800.

(c) $10,800.

(d) $11,047.

Question 38

Read the following extract from *FC of T v. Applegate* 79 ATC 4307 and then answer the question below.

> The taxpayer, a solicitor employed by a Sydney firm, was sent to Vila in the New Hebrides to establish a branch office for the firm. On being posted to Vila, the taxpayer surrendered the lease on his Sydney flat and left with his wife, who was expecting their first child. After spending the first two weeks in a hotel, the couple moved into leased premises (the term of the lease being one year with an option to renew for a further year).
>
> The taxpayer obtained a New Hebrides residency permit and was also admitted to practice as a legal practitioner in the New Hebrides. He left no assets in Australia but retained membership of a hospital benefits fund.
>
> It had been anticipated by the taxpayer and his firm that his stay in Vila would be of a substantial (but undefined) period. However, it was always intended that he would ultimately return to live in Australia and work in the Sydney office of the firm. In fact, after a stay of only two years in Vila, the taxpayer's ill-health forced him to end his stay early and return to Australia.

Which of the following statements most accurately reflects the taxpayer's residency status?

(a) The taxpayer ultimately intended to return to Australia, and therefore was a non-resident during the two-year period.

(b) The taxpayer's 'permanent place of abode outside Australia' is to be read as something less than a 'permanent place of abode' in which the taxpayer intends to reside for the rest of his life.

(c) The taxpayer had established a 'permanent place of abode' outside Australia, and therefore was a non-resident during the two-year period.

(d) The taxpayer's stay is purely temporary and intends to move on or to return to Australia, and therefore is a resident for taxation purposes.

Question 39

Read the following extract from *FC of T v. The Myer Emporium Ltd* (1987) 87 ATC 4363, 163 CLR 199 and then answer the question below.

> The taxpayer carried on the business of retail trading and property development and also acted as a finance company for other companies in its group. In order to obtain funding to diversify its operations the taxpayer entered into the following prearranged series of transactions:
>
> (a) On 6 March 1981, the taxpayer lent $80 million to Myer Finance Ltd (Myer Finance), a shelf company of the taxpayer, acquired on 20 February 1981. The loan agreement between the taxpayer and Myer Finance provided that Myer Finance was required to repay the loan 'on but not prior to' 30 June 1988 and that interest at the commercial rate of 12.5% per annum was to be payable on the loaned funds on dates set out in the loan agreement. The total interest to be payable amounted to $72 million. An initial payment of interest only, in the sum of $82,182, was paid on the date the loan was made.
>
> (b) On 9 March 1981, the taxpayer assigned to Citicorp Canberra Pty Ltd (Citicorp) (which had accumulated tax losses) 'the moneys due or to become due as the interest payments and interest thereon' in consideration of Citicorp paying the taxpayer a lump sum of $45.37 million on the day.
>
> The above transactions were interrelated in that the taxpayer would not have made the loan to Myer Finance unless Citicorp had agreed in advance to pay for the assigned interest.

Which of the following statements most accurately describes the $45.37 million lump sum payment?

(a) The transaction was an isolated transaction outside the ordinary course of business, and therefore a capital asset was extinguished with the payment of $45.37 million.

(b) The two transactions, namely the loan agreement and the assignment, were essential and integral elements of an overall scheme, that being a profit-making scheme.

(c) The two transactions arose outside the ordinary course of business, and therefore were capital by nature.

(d) There had been no profit arising from the transaction as the $45.37 million received was merely an amount equal to the value of the chose in action which it had assigned, namely the right to receive future interest from the debt.

Question 40

Read the following extract from *RACV Insurance Pty Ltd v. FC of T* 74 ATC 4169 and then answer the question below.

> The taxpayer carried on both a 'comprehensive' and a 'compulsory third party' motor car insurance business.
>
> Under the Motor Car Act 1958 (Vic.), the taxpayer was liable to indemnify its insured in respect of compulsory third party personal injury claims even if no notice of the claims had been given to the taxpayer by its insured.
>
> In the relevant year of income, the taxpayer claimed a $1.5 million deduction under s. 51(1) of the ITAA 1936 in respect of 'unreported claims' in relation to its compulsory third party insurance business. The unreported claims represented the taxpayer's estimate of its liability in respect of claims arising out of accidents which had occurred before the end of the income year but which had not been reported to the taxpayer by such time. The taxpayer's estimate was based on estimates provided by its experienced claims officers. The taxpayer argued that its estimate in respect of unreported claims should be an allowable deduction because the accidents were events which gave rise to its liability to indemnify its insured and as these events were incurred in the relevant income year they should be deductible in that year.

Which of the following statements most accurately describes the $1.5 million deduction in respect of 'unreported claims'?

(a) The taxpayer had incurred a loss or outgoing in the relevant year of income in respect of its unreported claims, as the liability to indemnify its insured had arisen in the relevant year and the liability was subject to reasonable estimate.

(b) The amount of the outgoing for unreported claims could not be precisely determined, and therefore a deduction could not be claimed.

(c) The taxpayer incurred no liability to indemnify its insured until it had been determined by settlement or court order that its insured were liable to pay to third parties a quantified sum and that no loss or outgoing had been incurred until such time.

(d) In order for a loss or outgoing to have been incurred in gaining or producing assessable income or in carrying on the business which produces the assessable income, the taxpayer must have 'completely subjected himself' to the loss or outgoing.

Solutions

Question 1

The correct answer is (a).

Section 6-1 states that assessable income consists of ordinary income and statutory income.

Feedback for incorrect answer (b): If your taxable income for the year is less than $18,200 then you pay no tax.

Feedback for incorrect answer (c): Taxable income is the difference between total assessable income less allowable deductions.

Feedback for incorrect answer (d): Assessable income does include statutory income.

For further information: Optional textbook – *Australian Taxation Law*.

Question 2

The correct answer is (c).

In *FCT v. Raymor (NSW) Pty Ltd* (1990) the court allowed a deduction where a prepayment was made for trading stock at the end of one income year, with the trading stock not being delivered until the following income year.

Feedback for incorrect answer (a): Trading stock is incurred in gaining or producing assessable income.

Feedback for incorrect answer (b): Trading stock is not of a capital nature

Feedback for incorrect answer (d): Prepayments are allowable deductions but generally the taxpayer must apportion the expense over the income year that the expense relates to.

Section 70-15 now defers the deduction until the stock is on hand or an amount is included in assessable income in relation to trading stock.

For further information: Optional textbook – *Australian Taxation Law*.

Question 3

The correct answer is (c).

Net partnership loss	$10,000
Add back salary paid to Kevin	$20,000
Net income of partnership	$10,000

Partner salaries are not expenses of the partnership but are a means by which partnership profits are distributed. Consequently, they are not deductible in calculating the partnership income or loss for tax purposes.

The $20,000 salary paid to Kevin as partner represents a distribution of partnership profits in advance. As the partnership's net income was only $10,000, which has all been allocated to Kevin due to his salary entitlement, the excess of $10,000 of available profits will be assessable to him in a future year when sufficient profits are available.

Feedback for incorrect answer (a): This answer would only recognise the $10,000 loss and ignore salaries paid of $20,000.

Feedback for incorrect answer (b): This answer would not recognise a loss in the partnership.

Feedback for incorrect answer (d): This answer would recognise the salaries as allowable deductions in the partnership, increasing the loss to $30,000.

For further information: Optional textbook – *Australian Taxation Law*.

Question 4

Correct answer is (d).

Australia has two distinct court systems:

1. Federal
2. State and territory.

The District Court or (County Court in Victoria) is a state jurisdiction court.

Feedback for incorrect answer (a): The Administrative Appeals Tribunal is not a court, but has the jurisdiction to review decisions made under the Commonwealth jurisdiction.

Feedback for incorrect answer (b): The Federal Court has the jurisdiction to hear an appeal decision.

Feedback for incorrect answer (c): The High Court has the jurisdiction to hear an appeal decision.

For further information: Optional textbook – *Australian Taxation Law*.

Question 5

The correct answer is (b).

PAYG is the Australian taxation system for withholding tax from employees, and other payees, in their regular payments from employers. The system calculates an annual income on the basis of weekly or fortnightly payment. The appropriate amount of tax is then withheld until it is passed onto the ATO.

Feedback for incorrect answer (a): The PAYG instalment system most accurately describes the collection of taxation for companies, superfunds and individuals with business or investment income.

Feedback for incorrect (c): The notional tax adjusted for movement in the CPI describes the calculation of the amount to be remitted to the ATO in the PAYG instalment system.

Feedback for incorrect (d): Amounts withheld from contractors who do not supply an ABN apply to the GST system of collecting tax.

For further information: Optional textbook – *Australian Taxation Law*.

Question 6

The correct answer is (b).

Items 1, 2, 3, 4, 5, 6, 11 are included as assessable income. Items 7, 8, 9, 10 are not included.

Feedback for incorrect answer (a): Item 10 is not included as assessable income.

Feedback for incorrect answer (c): Item 7 is not included as assessable income.

Feedback for incorrect answer (d): Items 9 and 10 are not included as assessable income.

For further information: Optional textbook – *Australian Taxation Law*.

Question 7

The correct answer is (c).

Opening balance (01.07.2016)	$300,000 Cash Received	$600,000
Income	$550,000 Closing Balance (30.06.2017)	$250,000
	$850,000	$850,000

The issue of when income is derived is crucial for determining when income will be taxed. Under a progressive tax system, this means that the point of derivation of income can have practical effects on the tax rate and tax payable, with obvious cash flow consequences.

One must decide whether the accounting basis provides a 'correct reflex of the true income of the taxpayer' (*Carden's case*.).

The court upheld in *Carden's case* (a country doctor in South Australia) that the 'cash or receipts method' of returning income more accurately reflected the income derived during the tax year than the 'earnings or accruals' basis.

Feedback for incorrect answer (a): Is incorrect as the opening debtors of $300,000 is used as the accrual amount.

Feedback for incorrect answer (b): Is incorrect as the calculation is:

Opening debtors $300,000 + $600,000 – closing debtors $250,000 = $650,000

Feedback for incorrect answer (d): Is incorrect as the closing debtors of $250,000 is used as the accrual amount.

For further information: Refer guidelines in Taxation Ruling TR98/1, Optional textbook – *Australian Taxation Law*

Question 8

The correct answer is (a).

	$
Taxable income	91,677
Tax payable	21,552.49
Add: Medicare levy	1,833.54
Less: Franking credit	(1,637.14)
PAYG payments	(29,985)
Refund	(8,236.11)

Feedback for incorrect answer (b): Franking credit ($1,637.14) not grossed-up and included in assessable income.

Feedback for incorrect answer (c): Franking credit ($1,637.14) not taken into the calculation for the refund.

Feedback for incorrect answer (d): Medicare levy ($1,833.54) not calculated.

	(b) Franking credit ($1,637.14) not grossed-up and included in assessable income $	(c) Franking credit ($1,637.14) not taken in the calculation of the refund $	(d) Medicare levy ($1,833.54) not calculated and franking credit not taken in the calculation of the refund $
Taxable income	90,040	91,677	91,677
Tax payable	20,946.80	21,552.49	21,552.49
Add: Medicare levy	1,800.80	1,833.54	–
Less: Franking Credit	–	–	–
PAYG payments	(29,985)	(29,985)	(29,985)
Refund	(7,237.40)	(6,598.97)	(8,432.51)

For further information: Optional textbook – *Australian Taxation Law*.

Question 9

The correct answer is (d).

Income is not taken to be derived until the service or goods has been supplied. Full High Court Decision:

1. The taxpayer derived the prepaid tuition tees in the year in which the tuition was provided rather than the year in which the fees were received.
2. As a general rule fees received in advance of the performance of services for which they are paid are not at the moment of receipt to be regarded as income of the taxpayer.

Feedback for incorrect answer (a): This case is about foreign source income derived by a non-resident.

Feedback for incorrect answer (b): This case is about the nature of capital expenditure and claiming a deduction for repairs.

Feedback for incorrect answer (c): This case concerns the relevant year of income in which the taxpayer claimed a $1.5 million deduction under s. 51(1) of the ITAA 1936 in relation to estimated insurance claims that were incurred but unreported.

For further information: Optional textbook – *Australian Taxation Law*.

Question 10

The correct answer is (d).

The application of the benchmark rule does not always result in a company having a franking deficit balance. There is not enough information to determine whether the application of the benchmark rule has resulted in the company having a franking deficit balance.

Feedback for incorrect answer (a): Overfranking dividends can result in excess debits to the franking account leading to a franking deficit balance.

Feedback for incorrect answer (b) and (c): Income tax payments and franking credits received are credited to the franking account. Insufficient income tax payments and franking credits can result in less credits in the franking account and a franking deficit balance.

For further information: Optional textbook – *Australian Taxation Law*.

Question 11

The correct answer is (c).

Division 7A provisions are anti-avoidance measures aimed at preventing private companies from making tax-free distributions of profits to shareholders (or their associates).

Unless they come within specific exclusions, amounts paid or loaned to shareholders, or shareholder debts (owed to the company) that are forgiven, are deemed to be dividends to the extent that a private company has a distributable surplus.

Feedback for incorrect answer (a): Private companies are taxed at a lower rate to public companies if they satisfy the definition of a small business entity (or base rate entity) for tax purposes.

Feedback for incorrect answer (b): Dividends paid by private companies can be franked to 100%.

Feedback for incorrect answer (d): A rebate of tax does not exist for private company dividends.

For further information: Optional textbook – *Australian Taxation Law*.

Question 12

The correct answer is (b).

There would be a fringe benefit with a taxable value of $100,000 × 1.65% = $1,650. The FBT taxable value amount is calculated using the difference between the actual interest rate and the statutory interest rate.

Feedback for incorrect answer (a): The amount is calculated as:

> $100, 000 × 4.0% = $4,000. The amount is calculated using the loan interest rate only.

Feedback for incorrect answer (c): This amount is calculated as:

> $1,650× 1.9608 = $3,235. This is the grossed-up value for FBT. While the grossed-up amount is correct, it is not what the question asked for.

Feedback for incorrect answer (d): The amount is calculated as:

> $100,000 x 5.65% = $5,650. The amount is calculated using the statutory interest rate only.

For further information: Optional textbook – *Australian Taxation Law*.

Question 13

The correct answer is (a).

GST is a broad-based consumption tax not FBT.

Feedback for incorrect answer (b): The FBT tax rate is 49% of the grossed-up value for the current FBT year.

Feedback for incorrect answer (c): All taxable entities must pay FBT tax (if they are liable for FBT).

Feedback for incorrect answer (d): FBT is an allowable deduction to the employer in each tax year.

For further information: Optional textbook – *Australian Taxation Law*.

Question 14

The correct answer is (c).

The taxable value is:

	$
Total benefit	660
Less: Business component - 30%	(198)
Private component - 70%	462
Less: employee contributions	(220)
Taxable value	242

Feedback for incorrect answer (a): Business component not reduced.

Feedback for incorrect answer (b): Taxable value of $462 not reduced by the employee contribution of $220.

Feedback for incorrect answer (d): Taxable value of $242 is grossed-up. While this is the correct grossed-up value, it is not what the question asked for.

	(a) Business component not deducted	(b) Taxable value of $462 ignores the employee contribution of $220	(d) Taxable value of $242 × 2.1463 (gross-up factor)
Total benefit	$660	$660	$660
Less: Business component	Nil	$198	$198
Private component		$462	$462
Less: Employee contributions	$220	Nil	$220
Taxable value	$440	$462	$242
Gross-up factor (2.1463)			$519

For further information: Optional textbook – *Australian Taxation Law*.

Question 15

The correct answer is (c).

The $50,000 paid for John agreeing not to compete is on capital count because John is giving up his right to compete (an asset) in exchange for the sum (*Dickenson v. FCT*). The $5,000 John received for advertising David's business is income according to ordinary concepts, being income earned from the provision of services (*Dixon v. FCT*).

Feedback for incorrect answer (a): The $50,000 payment is on capital account. Only the $5,000 advertising payment is ordinary income.

Feedback for incorrect answer (b): Nil is incorrect. The $5,000 advertising payment is ordinarily income.

Feedback for incorrect answer (d): $50,000 is incorrect as the payment is on capital account (see correct feedback).

For further information: Optional textbook – *Australian Taxation Law*.

Question 16

The correct answer is (a).

The FBT year of tax is 1 April to 31 March.

Feedback for incorrect answer (b): The FBT year is not the calendar year.

Feedback for incorrect answer (c): The FBT year is not the financial year.

Feedback for incorrect answer (d): The FBT year is not correct.

For further information: Optional textbook – *Australian Taxation Law*.

Question 17

The correct answer is (c).

The payments were of an income nature as the taxpayer was able to enlist with the expectation that he could depend on the supplement received from his employer.

The payments were of an income nature as they were a substitute for wages that the taxpayer would otherwise have received.

Feedback for incorrect answer (a): Income must be received on a regular basis, and is not a lump sum benefit.

Feedback for incorrect answer (b): Whilst income may be a quantifiable amount, there is no reference in the scenario to it being received on a regular basis.

Feedback for incorrect answer (d): The relationship does not need to always be between employer and employee.

For further information: Optional textbook – *Australian Taxation Law*.

Question 18

The correct answer is (c).

$3,000,000 × $^2/_6$ = $1,000,000

The formula for diminishing value (ignoring the impact of leap years) is:

$$\frac{\text{Base value} \times \text{Days held}}{365} \times \frac{200\%}{\text{Asset's effective life}}$$

Feedback for incorrect answer (a): ($3,000,000 – $100,000) × $^1/_6$ = $483,333. The prime cost method has been used and the base value has been reduced by the residual value.

Feedback for incorrect answer (b): $3,000,000 × $^1/_6$ = $500,000. The prime cost method has been used.

Feedback for incorrect answer (d): ($3,000,000 – $100,000) × $^2/_6$ = $966,667. The base value has been reduced by the residual value.

For further information: Optional textbook – *Australian Taxation Law*.

Question 19

The correct answer is (c).

$\$60{,}000 \times {}^{273}/_{365} \times {}^{1}/_{8} = \$5{,}610$

The formula for prime cost (ignoring the impact of leap years) is:

$$\frac{\text{Base value} \times \text{Days held}}{365} \times \frac{100\%}{\text{Asset's effective life}}$$

Feedback for incorrect answer (a): $60,000 ÷ 8 = $7,500. This does not apportion for the days held.

Feedback for incorrect answer (b): $\$60{,}000 \div 8 \times {}^{9}/_{12} = \$5{,}625$. This uses monthly apportionment when the formula requires days apportionment.

Feedback for incorrect answer (d): $\$60{,}000 \times {}^{9}/_{12} \times {}^{2}/_{8} = \$11{,}250$. This uses monthly apportionment and the diminishing value method.

For further information: Optional textbook – *Australian Taxation Law*.

Question 20

The correct answer is (a).

To prove Part IVA:

- there must be a scheme, and
- there must be a tax benefit – compare the actual tax position with that which might reasonably have occurred but for the transaction being entered into, and
- The taxpayer must have entered into a scheme with the purpose of enabling them to obtain a tax benefit (the 'dominant purpose' test or 'principal purpose' test for significant global entities).

Feedback for incorrect answer (b): (1) It must be defined as a scheme, (2) no tax benefit mentioned.

Feedback for incorrect answer (c): None of the three tests is present.

Feedback for incorrect answer (d): None of the three tests is present.

For further information: Optional textbook – *Australian Taxation Law*.

Question 21

The correct answer is (a).

GST sales	$3,000
GST purchases	($2,000)
PAYG income tax instalment	$5,000
PAYG instalment	$2,500
	$8,500

Feedback for incorrect answer (b), (c) and (d):

	(b)	(c)	(d)
GST sales	$3,000	$3,000	$3,000
Export sales		$400	$400
GST purchases	($2,000)	($2,000)	($2,000)
Input tax supplies	($100)	($100)	
PAYG income tax instalment	$5,000	$5,000	$5,000
PAYG instalment	$2,500	$2,500	$2,500
	$8,400	$8,800	$8,900

For further information: Optional textbook – *Australian Taxation Law*.

Question 22

The correct answer is (a).

The cost of replacing the three tiles ($200) to restore the roof to its former undamaged state, would be a repair and deductible under s. 25-10.

Feedback for incorrect answer (b): The replacement of the front window only 10 days after acquiring the property would be classed as an initial repair. Likewise, the removal of part of the front fence would not be a repair because there was no decay or damage to the fence that required its restoration.

Feedback for incorrect answer (c): The removal of part of front fence would not be a repair because there was no decay or damage to the fence that required its restoration.

Feedback for incorrect answer (d): Claiming a nil repair deduction would not take into account the necessity to replace three roof tiles after a tree branch had fallen over the roof. This would be a repair to the roof of $200.

For further information: Optional textbook – *Australian Taxation Law*.

Question 23

The correct answer is (d).

Section 25-25 provides that expenditure incurred in borrowing money is deductible if the money is used by the taxpayer to produce assessable income. Legal fees of $1,600, procuration fees of $400 and the valuation fee of $80 each qualify as a borrowing expense. However, only $160,000 of the $200,000 borrowed is used to produce assessable income. The $80 valuation fee is not deductible (or apportionable) as it relates exclusively to the taxpayer's home.

As the loan has not been repaid, s. 25-25(5) requires the deduction to be spread over the period of the loan or five years, whichever is the shorter.

The borrowing cost deduction for the 2016–2017 year would be $80, determined as follows:

$2,000 ÷ 1825 days (ignoring the impact of leap years) = $1.10 per day

91 days in 2016–2017 tax year × $1.10 = $100

$100 × $160,000 ÷ $200,000 = $80

The amount paid to discharge the mortgage on the taxpayer's home is not deductible under s. 25-30 as the expenditure is used to repay money used to acquire the taxpayer's home rather than to produce assessable income.

The interest deduction for the 2016-2017 year would be $2,992, determined as follows:

$160,000 × 0.075 × 91 ÷ 365 days = $2,992

The total deduction for 2016–2017 = $80 + $2,992 = $3,072.

Feedback for incorrect answer (a): Following the above calculation for interest but on total loan:

$200,000 × 0.075 × 91 ÷ 365 days = $3,740 plus $80 = $3,820

Feedback for incorrect answer (b): Only claiming the interest on the business portion of the loan (see above).

Feedback for incorrect answer (c): Only claiming the interest but on the total amount of the loan (see (a) above).

For further information: Optional textbook – *Australian Taxation Law*.

Question 24

The correct answer is (b).

	$
Tables	24,000
Chairs	27,000
Cutlery and crockery	21,000
Other assets 15% × $105,000	15,750
Depreciation	87,750

Feedback for incorrect answer (a), (c) and (d):

(a)	$	(c)	$	(d)	$
Tables	24,000	Tables	24,000	Tables	24,000
Chair	27,000	Chairs	27,000	Chairs	27,000
Cutlery and crockery	21,000	Cutlery and crockery	21,000	Cutlery and crockery	21,000

(a)	$	(c)	$	(d)	$
Other assets	–	Other assets	105,000	Other assets – 30% × $105,000	31,500
Depreciation	72,000	Total	177,000	Depreciation	103,500
		Depreciation @ 15% × $177,000	26,550		

For further information: Optional textbook – *Australian Taxation Law.*

Question 25

The correct answer is (b).

	$	$
Net profit		800,000
Add back:		
Accounting depreciation	90,000	
LSL provision	160,000	
Doubtful debts	60,000	
Net capital gain	80,000	390,000
		1,190,000
Less:		
Capital profit	(150,000)	
Tax depreciation	(120,000)	
Bad debts written off	(30,000)	(300,000)
Taxable income		890,000

Feedback for incorrect answer (a):

	$	$
Net profit		800,000
Add back:		
Accounting depreciation	90,000	
LSL provision	160,000	
Doubtful debts	60,000	
Net capital gain	80,000	390,000
		1,190,000
Less:		
Tax depreciation	(120,000)	
Bad debts written off	(30,000)	(150,000)
Taxable income		1,040,000

Feedback for incorrect answer (c):

	$	$
Net profit		800,000
Add back:		
Accounting depreciation	90,000	
LSL provision	160,000	
Doubtful debts	60,000	
Net capital gain	80,000	390,000
		1,190,000
Less:		
Tax depreciation	(120,000)	
Capital profits	(150,000)	(270,000)
Taxable income		920,000

Feedback for incorrect answer (d):

	$	$
Net profit		800,000
Add back:		–
Less:		
Tax depreciation	(120,000)	
Bad debts written off	(30,000)	
Capital profits	(150,000)	(300,000)
Taxable income		500,000

For further information: Optional textbook – *Australian Taxation Law*.

Question 26

The correct answer is (c).

	$
Net profit per account	248,000
Add: franking credits ($28,000 x 30/70) + ($20,000 x 30/70) = (12,000 + 6,000)	18,000
Total taxable income	266,000
Tax on taxable income of $266,000 × 30%	79,800
Less: franking credit tax offset	(18,000)
Net tax payable	61,800

Feedback for incorrect answer (a), (b) and (d):

(a)	$	(b)	$	(d)	$
Net profit per account	248,000	Net profit per account	248,000	Net Profit per account	248,000
Add: franking credits ($12,000 + $6,000)	18,000			*Add*: franking credits ($12,000 + $8,571)	20,571
Total taxable income	266,000	Total taxable income	248,000	Total taxable income	268,571
Primary tax on taxable income of $266,000 × 30%	79,800	Primary tax on taxable income of $248,000 × 30%	74,400	Primary tax on taxable income of $268,571 × 30%	80,571
				Less: franking credit tax offset	(20,571)
				Net tax payable	60,000

For further information: Optional textbook – *Australian Taxation Law*.

Question 27

The correct answer is (a).

$180,000 (ordinary income) × 12% = $21,600 per quarter.

Capital gains are not included in instalment income, and are therefore ignored when calculating PAYG instalments.

Feedback for incorrect answer (b): $180,000 + $6,000 = $186,000 × 12% = $22,320 (capital gains included in the calculation).

Feedback for incorrect answer (c): $180,000 (ordinary income) x 15% = $27,000 (incorrect instalment rate).

Feedback for incorrect answer (d): $180,000 × 30% = $54,000 (ignores the 12% rate).

For further information: Optional textbook – *Australian Taxation Law*.

Question 28

The correct answer is (d).

21 May = US$250,000 ÷ 0.65 = A$384,615.

15 June = US$250,000 ÷ 0.60 = A$416,667.

Difference = A$416,667 – A$384,615 = A$32,052 (loss).

Feedback for incorrect answers (a):

1 May = US$250,000 × 0.65 = A$162,500

15 June = US$250,000 × 0.60 = A$150,000

Difference = $162,500 – $150,000 = A$12,500 gain.

Feedback for incorrect answer (b): No exchange gain or loss is based on paying the original amount of the invoice: A$384,615.

Feedback for incorrect answer (c): Interpreting the calculation in (a) above for an exchange loss of $12,500.

For further information: Optional textbook – *Australian Taxation Law*.

Question 29

The correct answer is (a).

	$
Capital gain	100,000
Less: current year capital loss	(10,000)
prior year capital loss	(30,000)
	60,000
Less:50% general discount	(30,000)
Net capital gain	30,000

Feedback for incorrect answers (b), (c) and (d):

(b)	$	(c)	$	(d)	$
Capital gain	100,000	Capital gain	100,000	Capital gain	100,000
Less:current capital loss	(10,000)	*Less*: current capital loss	(10,000)	*Less*: current capital loss	(10,000)
prior capital loss	(30,000)	prior capital loss	–	prior capital loss	–
			90,000		90,000
Less:50% general disc	–	*Less*:50% general disc	(45,000)	*Less*:50% general disc	(45,000)
prior capital loss	–	prior capital loss	(30,000)	prior capital loss	–
Net capital gain	60,000	Net capital gain	15,000	Net capital gain	45,000

For further information: Optional textbook – *Australian Taxation Law*.

Question 30

The correct answer is (a).

As a result of the accident, Jennifer has acquired a CGT asset – the right to seek compensation for the losses sustained – at the time the injury was suffered (CGT event D1). Jennifer disposed of her asset (the right to compensation) when the claim was settled (at which time CGT event C2 occurred).

Feedback for incorrect answer (b): The CGT event is covered by D1 and C2 and therefore the category other CGT events is not required.

Feedback for incorrect answer (c): CGT event A1 (disposal of CGT asset) is not correct as the asset was not disposed.

Feedback for incorrect answer (d): CGT events H1 and H2 are also not special capital receipts but rather are covered by D1 and C2.

For further information: Optional textbook – *Australian Taxation Law*.

Question 31

The correct answer is (a).

$89 + $247 + $45 + $70 + $276 – $250 = $477

All expenses excluding the HECS amount of $983 (s. 26-20) would be allowable deductions; however, the first $250 of all education expenses incurred at an educational institution would be treated as self-education under s. 82A(2), and denied as a deduction.

Feedback for incorrect answer (b): The first $250 incurred has not been deducted (see above).

Feedback for incorrect answer (c): This amount includes the higher education amount of $983 (after deducting the first $250).

Feedback for incorrect answer (d): This amount does not include the $276 travelling expenses from work to university and the higher education amount of $983.

For further information: Optional textbook – *Australian Taxation Law*.

Question 32

The correct answer is (c).

The expenditure must be apportioned over the eligible service period to which the expenditure relates as per ss 82KZMA and 82KZMD. The eligible service period is 730 days and there are 61 days in the current year. Therefore the deduction calculation would be as follows:

61 ÷ 730 × $50,000 = $4,178

Feedback for incorrect answer (a): To claim $25,000 would ignore the requirement to apportion the deduction over the eligible service period as per s. 82KZMD in determining the amount to claim as a deduction. The amount paid must be apportioned over the period of the lease.

Feedback for incorrect answer (b): To claim $50,000 would ignore the requirement to apportion the deduction over the eligible service period as per s. 82KZMD in determining the amount to claim as a deduction. The amount paid must be apportioned over the period of the lease.

Feedback for incorrect answer (d): This would be an incorrect calculation using the following formula: 61 ÷ 354 × $50,000 = $8,616.

For further information: Optional textbook – *Australian Taxation Law*.

Question 33

The correct answer is (b).

A beneficiary who is presently entitled to or has a vested and indefeasible interest in any of the income of a trust estate, but is under a legal disability, will have his or her share of net income assessed to tax in the hands of the trustee. The trustee will be liable to pay tax thereon as if it were the income of an individual taxpayer not subject to any deductions (s. 98).

Feedback for incorrect answer (a): A beneficiary who is presently entitled to or has a vested and indefeasible interest in any of the income of a trust estate, cannot be under a legal disability.

Feedback for incorrect answer (c): For a beneficiary to be not presently entitled only occurs in a limited range of circumstances, of which the most important are deceased estates, bankruptcy and insolvent estates.

Feedback for incorrect answer (d): Even though James Bennett has a mental disability he is still entitled to receive distributions from the trust.

For further information: Optional textbook – *Australian Taxation Law*.

Question 34

The correct answer is (a).

Sue is a beneficiary who is presently entitled to trust income and is not under a legal disability. As a non-resident she is only liable for tax on Australian-sourced trust income. The distribution to her includes an Australian-sourced fully franked dividend. However, as it is a dividend paid to a non-resident (indirectly via a trust in this case), it is subject to Australia's withholding tax rules and is treated as non-assessable, non-exempt income of Sue. Note: As it is fully franked, there is no withholding tax obligation.

Feedback for incorrect answer (b):

	$
Australian dividends	3,300
Gross-up franking credit	1,414
Dividend from the USA	3,400
Gross-up for withholding tax	600
Net income	8,714
Distribution as per trustee's resolution:	
Allan (aged 17)	4,357
Sue (aged 22)	4,357

The distribution is not taxable to Sue in Australia for the reasons stated in (a) above.

Feedback for incorrect answer (c):

	$
Australian dividends	3,300
Gross-up for franking credit	1,414
Net income	4,714
Distribution as per trustee's resolution:	
Allan (aged 17)	2,357
Sue (aged 22)	2,357

This answer excludes the dividend from the USA and the gross-up for withholding tax.

Feedback for incorrect answer (d):

	$
Australian dividends	3,300
Gross-up for franking credit	1,414
Dividend from the USA	3,400
Net Income	8,114
Distribution as per trustee's resolution:	
Allan (aged 17)	4.,057
Sue (aged 22)	4,057

This answer excludes the withholding tax gross-up from the USA dividend.

For further information: Optional textbook – *Australian Taxation Law*.

Question 35

The correct answer is (b).

Unlike partnerships, loses incurred by a trust are trapped in the trust and cannot be distributed to beneficiaries. The loss can be carried forward within the trust for offset against future assessable income.

Feedback for incorrect answer (a): Dividends are grossed-up for partnerships and trusts.

Feedback for incorrect answer (c): Beneficiaries with a legal disability are presently entitled to a distribution; however, the trustee will be liable to pay tax thereon.

Feedback for incorrect answer (d): The trust deed will determine if the trustee has the power to stream net capital gains and/or franked dividends to specific beneficiaries

For further information: Optional textbook – *Australian Taxation Law*.

Question 36

The correct answer is (a).

Funds which comply with the Superannuation Industry (Supervision) Act 1993 (SISA) qualify for concessional tax rates. A complying super fund is taxed at 15%.

Feedback for incorrect answer (b): Complying superannuation funds are taxed concessionally at 15%.

Feedback for incorrect answer (c): Investments earnings are taxed at 15%.

Feedback for incorrect answer (d): There is generally no tax payable. A rollover is the mechanism by which a superannuation balance is transferred from one super fund to another super fund.

For further information: Optional textbook – *Australian Taxation Law*.

Question 37

The correct answer is (c).

	(a) $
Superannuation pension (taxable component only)	10,000
Interest from Australian sources	47
Interest received from UK	900
Gross-up interest for withholding tax	100
Total	11,047
Less: Deductions	(247)
Taxable income	10,800

Feedback for incorrect answer (a), (b) and (d):

	(a) $	(b) $	(d) $
Superannuation pension (taxable component only)	10,000		10,000
Superannuation pension – tax free	6,670		Nil
Interest from Australian sources	47	47	47
Interest received from UK	900	900	900
Gross-up interest for withholding tax	100	100	100
Total	17,717	1,047	11,047
Less: Deductions	(247)	(247)	Nil
Taxable income	17,470	800	11,047

For further information: Optional textbook – *Australian Taxation Law*.

Question 38

The correct answer is (c).

The Full Federal Court decision:

> The taxpayer, during the period of his stay in Vila, had established a permanent place of abode outside Australia within the meaning of that term in the definition of resident, notwithstanding that he ultimately intended to return to Australia.
>
> Accordingly, the taxpayer was a non-resident during the two-year period he spent in Vila and the salary earned by him in Vila was therefore exempt from Australian tax under Section 23(r) of the Act.

Feedback for incorrect answer (a): Even though the taxpayer intended to return to Australia, he had established 'a permanent place of abode' outside Australia.

Feedback for incorrect answer (b): Permanent in this context does not mean 'everlasting'.

Feedback for incorrect answer (d): The taxpayer's stay in Vila for two years could not be considered temporary when testing for 'permanent place of abode'.

For further information: Optional textbook – *Australian Taxation Law*.

Question 39

The correct answer is (b).

The Full High Court Decision per Mason ACJ:

> Although it is well settled that a profit or gain made in the ordinary course of carrying on a business constitutes income, it does not follow that a profit or gain made in a transaction entered into otherwise than in the ordinary course of carrying on the taxpayer's business is not income.

The Commissioner treated the lump sum of $45.37 million received as an income receipt assessable to the taxpayer under s. 25 (1) of the ITAA 1936.

The Commissioner also contended that $45.37 million constituted a profit assessable under the second limb of s. 26 (a) as a profit arising from the carrying on or carrying out of a profit-making undertaking or scheme of the taxpayer.

Both the Victorian Supreme Court and the Full Federal Court held that the lump sum was a capital receipt. The Commissioner appealed to the Full High Court.

Feedback for incorrect answer (a): The fact that this was an isolated transaction does not exclude it from the possibility of being a transaction in the ordinary course of a taxpayer's profit-making business and income.

Feedback for incorrect answer (c): Although the transactions, more particularly the assignment, were novel in the sense that it was the first time that the taxpayer had entered into such an arrangement, this fact did not take the transactions outside the ordinary course of the carrying on of the taxpayer's profit-making business and on capital account.

Feedback for incorrect answer (d): The consideration payable for the assignment reflected the true value of the chosen action which [the taxpayer] assigned. But once the two transactions are seen as integral elements in one profit-making scheme, it is apparent that [the taxpayer] made a relevant profit.

For further information: Optional textbook – *Australian Taxation Law*.

Question 40

The correct answer is (a).

The Supreme Court of Victoria Decision per Menhennitt J:

> The taxpayer had incurred a loss or outgoing in the relevant year of income in respect of its unreported claims under Section 51 (1) as the liability to indemnify its insured had arisen in the relevant year and the liability was subject to reasonable estimate.

Feedback for incorrect answer (b): The fact that an amount cannot be precisely determined, does not prevent the loss or outgoing from being deductible under s. 51 (1).

Feedback for incorrect answer (c): It is necessary to consider the nature of the business being carried on. The essence of insurance business is that, in respect of each class of risk insured against, the insurance company aims to satisfy its liabilities to the policy holders who actually experience the risk primarily out of the total of the premiums paid by all the policy holders, most of whom normally do not experience the risk.

Feedback for incorrect answer (d): 'Incurred' includes 'encountered', 'run into', or 'fallen upon'. The taxpayer had 'completely subjected himself' (*James Flood Pty Ltd*) to the loss or outgoing.

For further information: Optional textbook – *Australian Taxation Law*.

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