



# Fogarty Partners

CHARTERED ACCOUNTANTS  
BUSINESS ADVISORS

Client Information Newsletter — Tax & Super

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## Bitcoin: Its place in your wallet or SMSF portfolio

While bitcoin may be the most well-known cryptocurrency, there are nearly 1,500 in existence. In its simplest form, a cryptocurrency is a “peer-to-peer electronic cash system”, which means that the currency is not in a physical form like cash but sits in an electronic register.

### About this newsletter

Welcome to our monthly client information news letter, keeping you up to date with emerging tax and superannuation issues, news and changes that you may need to know about. If you require further information on any of the topics covered, please contact us.

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What makes bitcoin work, where previous attempts at electronic cash did not, is in the magic of something called blockchain. One of the problems with earlier electronic cash was that it was possible for those with the skills to fool the system and allow multiple transactions of the same piece of currency.

Bitcoin and other forms of blockchain get around this. Rather than having a central ledger of all transactions, blockchain relies on a decentralised network of ledgers, all of which have a complete record of every transaction of every bitcoin. Every one of these ledgers must be the same before the system recognises a transfer of a

## **Bitcoin: Its place in your wallet or SMSF portfolio cont**

bitcoin or part thereof. There is extensive cryptography to secure the transactions.

As a digital currency, bitcoins are sent and received via digital addresses. The system uses public key cryptography to make and verify digital signatures used in bitcoin transactions. Users are assigned a private access key enabling access to bitcoins stored in a digital wallet. Users are able to transfer money without utilising centralised banks and third-party payment channels.

To further enhance the system, there is a permanent limit on the number of bitcoins that will ever be created. This ensures that the value of the bitcoin isn't destroyed by the electronic equivalent of just printing money. The consequence of this however is that bitcoins are scarce. As we know, if a commodity is scarce but in demand, the value of that commodity will increase, as we have seen with bitcoin and other cryptocurrencies.

The problem this creates though is that the commodity can be used for speculative purposes, which isn't bad when you buy low and sell high but can be very damaging in a boom-and-bust scenario.

The other thing about bitcoin and the like is that ownership can be relatively anonymous, with the ability to hide transactions from governments and regulators. For this reason it is favoured by crime syndicates, money launderers and terrorist networks (and the odd white collar criminal too). It is this element that has brought cryptocurrencies to the attention of regulators and why they may in the future be subject to regulation.

### **Tax and bitcoins**

Cryptocurrency in Australia had until recently been subject to what was labelled "double taxation". Legislation effective from July 1, 2017 aligned the goods and services tax (GST) treatment of digital currency with money. Before this, anyone using cryptocurrency as payment effectively paid GST twice — once when buying the bitcoin and again on its use in exchange for goods and services subject to GST.

The ATO deems bitcoin to be neither money nor foreign currency, but also holds that it can be regarded as an asset for capital gains tax (CGT) purposes.

As far as conducting transactions with bitcoin, the ATO states that it views such transactions as akin to barter arrangements.

In conducting a business transaction therefore, the same process would be followed as when, for example, receiving a non-cash consideration under a barter transaction, with the consideration recorded at fair

market value. This can be obtained from a reputable bitcoin exchange. For individuals, when buying items online for personal use or consumption, there is generally no income tax or GST implications. Any capital gain or loss realised by disposing of bitcoin is generally disregarded (as a personal use asset), provided the value of the bitcoin is less than \$10,000.

ATO advice is that certain records should be kept for any bitcoin transactions, including:

- the date of the transactions
- the amount in Australian dollars (which can be taken from a reputable online exchange)
- what the transaction was for
- who the other party was (even if it's just their bitcoin address).

### **SMSF investment**

The dramatic rise in value (and then fall) of bitcoin and other cryptocurrencies has sparked interest among SMSF trustees on its potential as an investment, particularly in a marketplace of low-interest rates, erratic sharemarkets and an easing in property value.

But its relatively short history makes it hard to predict, and there is uncertainty what (if any) regulation will be placed on it. There are also uncertainties on how to manage cryptocurrencies within the tightly regulated SMSF space.

The ATO has made it clear that, at the moment, it cannot stop an SMSF investing in a cryptocurrency like bitcoin. There is no specific prohibition in the relevant legislation, and it is permissible as long as it meets the other rules for investment. But this does not mean there are no pitfalls for SMSF trustees.

The first thing a trustee or administrator must do is to check the trust deed. As it is a relatively new investment vehicle few, if any, trust deeds will deal with it directly, and may need amending.

It will also be necessary to review the investment strategy. Bitcoin is volatile, and in its short history there have been many booms and just as many busts. Therefore bitcoin only suits those investment strategies that are prepared to take risks. As it pays no income and is subject to wide variation, it is also unlikely to be suitable for fund members in or near retirement phase.

Another thing to realise with cryptocurrencies is that they have no physical assets backing them up — if they fail, you lose everything. They are only as valuable as someone is willing to pay for them, which also makes them particularly hard to value.

**Bitcoin: Its place in your wallet or SMSF portfolio cont**

Given the electronic nature of cryptocurrencies, there is a need to ensure that there is a clear separation between the fund’s assets and those of trustees. Thus, if you have both personal and SMSF investments in bitcoin, they need to be clearly separated. The ATO has highlighted this as an issue of concern, and something they will look out for when reviewing SMSFs with cryptocurrency investments.

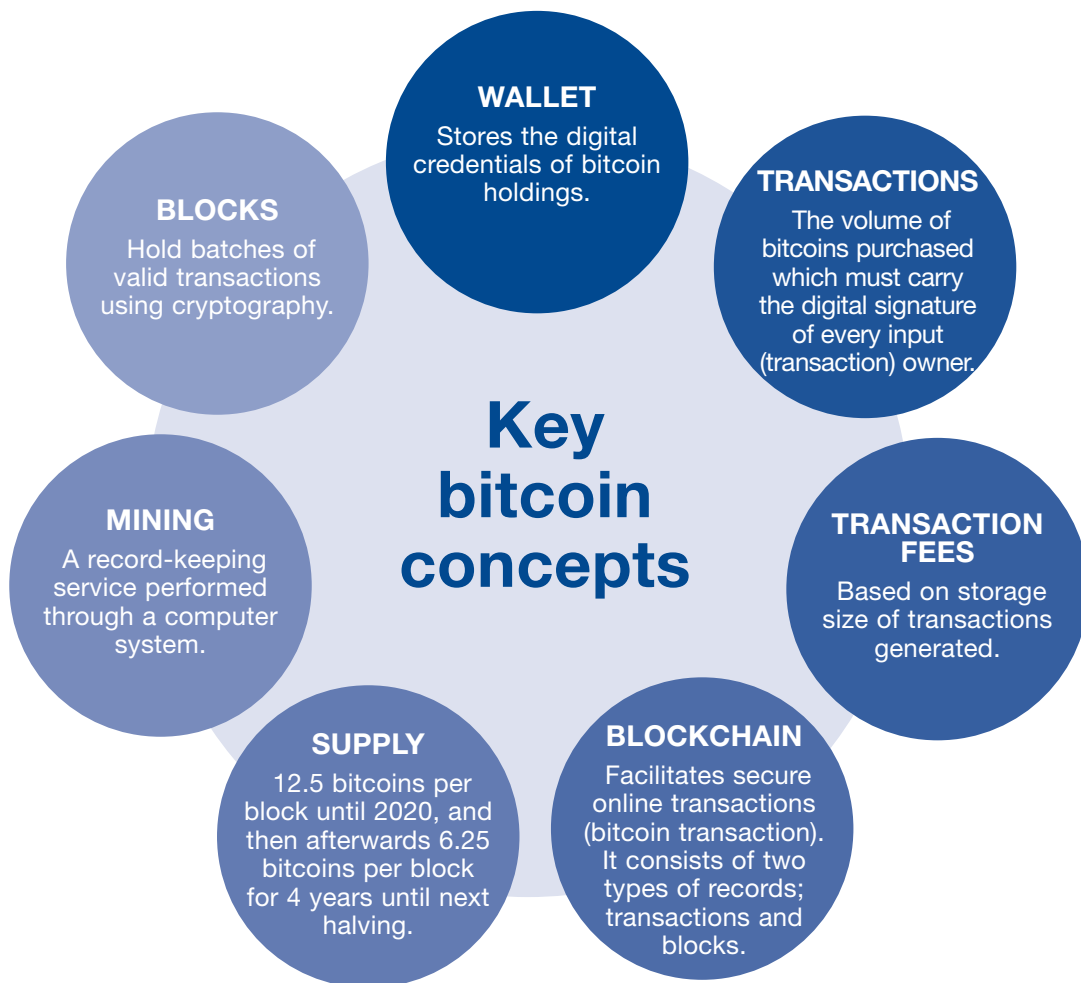
One advantage though of cryptocurrencies is that all transactions are recorded. Therefore they can be checked by auditors (and regulators), however it is advisable to also keep a written note of all transactions including buying and selling prices and dates.

A new issue of concern for SMSFs that invest in bitcoin is that given the wide fluctuations in value, a fund may unwittingly breach the transfer balance cap of \$1.6

million and have to wear the headaches and restrictions that breaching the cap brings, in particular if other contributions have been made to the fund.

Both the ATO and ASIC have issued a warning to SMSFs investing in cryptocurrencies. They are a highly speculative investment and not recommended for those who are not willing to make riskier investments. There is little long-term history of their performance, so it is difficult to understand how they will perform over time.

Having said that, there is nothing currently preventing an SMSF from investing in cryptocurrencies like bitcoin. Just make sure you do your homework and are prepared for the risk they present. Also, be aware that while at the moment they are lightly regulated (if at all) this is unlikely to be the case long term. ■





# SMSF commutation requests: How to get the green light from the ATO

The ATO has issued guidance on its approach to commutation requests, which is an essential piece of information for SMSF trustees because it explains which commutation requests will not be subject to an ATO review. With recently introduced superannuation rules now in effect (from 1 July 2017), superannuation members with income streams that are valued in excess of \$1.6 million will need to commute the excess by 30 June at the latest in order not to exceed their transfer balance cap.

## Commutations: brief overview

The term “commutation” is not defined in either income tax acts or superannuation law. Consequently, it takes its natural meaning in the context in which it appears.

A superannuation income stream ceases when a request from a member to fully commute their entitlements to future superannuation pension payments (in exchange for an entitlement to a lump sum) takes effect.

Such a request becomes effective as soon as the trustee’s liability to pay superannuation income stream benefits to the member is substituted with a liability to pay that member a superannuation lump sum.

## Commutation requests affected

All of the following conditions must be satisfied in relation to such commutation requests:

- A method is specified in the request that allows an exact calculation of the amount to be commuted
- The superannuation income stream, which will be subject to the commutation, is specified. If there are more than one income streams subject to commutation, the order of priority in which the commutations will occur must be stated
- The request is not in conflict with a similar commutation request that was accepted by a different superannuation fund.

A possible method to determine the amount to be commuted is to compare the account balance on 30 June to the transfer balance cap of \$1.6 million. The difference, if any, would be the amount to commute.

The amount of the commutation is required to be worked out by the trustee of the SMSF, and reflected in the SMSF’s financial accounts for the year ended 30 June, no later than the due date of the SMSF’s annual return.

## Commutation requests must be non-revocable

A further warning from the ATO is that the trustee should not be able to revoke the acceptance to commute the amount. If the agreement to commute or the governing rules of the superannuation fund allowed discretion for either the member or the trustee of the SMSF to revoke the agreement, it would be questionable whether a valid commutation had in fact been made.

## Certainty of the commutation requests

In order for the commutation request to be valid under the ATO’s guidelines, it must not be subject to the discretion of the fund’s trustee or a member at a later date. Likewise, the commutation request must not be dependent on certain events occurring in the future.

*continued on page 6* ➡



# Duties and taxes when you buy online from overseas

Items that you buy over the internet from an overseas source are generally required to abide by the same rules and screening processes that apply to any other “import”. Also the usual duties or taxes should apply.

Customs duties are regulated by the Department of Home Affairs (a recently formed body from December 2017, which now oversees the Australian Customs Service as well as Immigration and Border Protection).

Relevant facts to keep in mind include:

- For goods that are worth \$1,000 or less, there are at the present time no duties, taxes or charges to pay (however see below\*).
- For goods that are worth more than \$1,000, you are generally required to fill out a special form called an Import Declaration, and pay duties, taxes and charges.
- You will need to pay duties and taxes on some goods (like tobacco or alcohol) regardless of their value.
- Certain types of goods are not allowed to be brought into Australia, such as firearms, or else need special permits.

The Department of Home Affairs may screen, x-ray or examine your goods just like any other imported items to make sure the goods are allowed into Australia. The Department of Agriculture may also need to clear and inspect items before they can be delivered to you.

## THERE CAN BE A COST

How much the goods are worth, and how they arrive in Australia, will determine how the Department of Home Affairs clears them for delivery to you and what duty, taxes and charges may apply.

Sometimes goods bought over the internet, even from an Australian company, may be sent to you directly from overseas. However this means that you may still have to pay import duty and taxes when this happens.

## GOODS WITH A VALUE OF \$1,000 OR LESS

At present, you do not have to pay duty and taxes on goods (excluding tobacco, tobacco products and alcohol) with a value of less than \$1,000. These are called low value imports (but see note\* at right).

If these goods arrive in Australia by air or sea cargo, they generally must be accompanied by a “self-assessed clearance” declaration. This will generally be taken care of by the cargo company, and there is no charge for this declaration. Goods arriving by post do not require such a declaration.

## GOODS WITH A VALUE OF MORE THAN \$1,000

To import goods with a value of more than \$1,000, you may be required to make an “import declaration”, which provides information about the items being brought into the country, including that GST has been applied. There is a processing charge for making an import declaration, and you will also be required to pay the duty and taxes for your goods.

Depending on the number of goods you plan to bring into Australia, you may wish to use the services of a licensed customs broker to help you import your goods.

## PAID CUSTOMS DUTY BUT CHANGED YOUR MIND?

Unfortunately “a change of mind”, or “they don’t fit”, or simply “I don’t like them” is not a customs duty refund circumstance under the legislation. However as an alternative option, if you go on to export the previously imported goods, subject to certain conditions, you may be entitled to a drawback of the duty paid.

*continued on page 6* ➡



\*GST is to be extended to low value imports from 1 July 2018.

Also at the time of writing Home Affairs has issued a proposal to apply a levy, estimated to be around \$5, to low value imports. The levy is to offset costs of bio-security and other screening for the roughly 40 million low value parcels entering Australia each year, which is expected to keep increasing.



**Duties and taxes when you buy online from overseas *continued from previous page***

**BEFORE YOU BUY ONLINE**

Gas and electrical goods that do not meet Australian safety and technical standards may be a serious safety risk. Those for sale online from overseas may not meet Australia’s standards. Some goods, like barbeques and personal grooming items, may not be able to be modified to meet the Australian standards.

If you buy pirated or counterfeit items, you are buying a flawed product and supporting an illegal trade that could involve serious criminal activity and harm. In some cases, Customs and Border Protection will seize imported pirated and counterfeit goods.

**ALCOHOLIC BEVERAGES, TOBACCO AND TOBACCO PRODUCTS**

If you import alcoholic beverages, tobacco or tobacco products by mail with a value equal to or less than \$1,000, Home Affairs will send you an invoice advising

the duty and taxes payable. You need to pay this invoice before your goods will be delivered to you.

If the goods have a value of more than \$1,000 you must lodge an import declaration.

If you choose not to pay for the duty and GST on the alcohol products within 30 days of the payment advice, the goods may be returned to sender.

If you choose not to pay the duty and taxes on the tobacco or tobacco products within 30 days of the invoice, the goods will be treated as abandoned and will be destroyed (tobacco or tobacco products cannot be returned to sender). ■



If relevant, ask this office for more information on the Duty Drawback Scheme.

**SMSF commutation requests *continued from page 4***

The ATO also gives an example of an ineligible commutation request. In this hypothetical case, the member specifies an amount to be commuted that is the excess amount over the member’s transfer balance cap, taking into account all superannuation income streams the member has in multiple funds, and the member providing a similar request to commute to a trustee of a different fund.

In this situation, neither request specifies a methodology that allows the precise quantum of the amount commuted to be calculated. The amount to be commuted under each request is dependent on the amount to be commuted under the other request.

**EXAMPLE (adapted from ATO guidelines)**

On 1 May, Diane has the following two superannuation interests supporting superannuation income streams in SMSF X:

- superannuation income stream A – valued at \$100,000
- superannuation income stream B – valued at \$1,200,000.

Diane also has a superannuation interest supporting a superannuation income stream in large APRA Fund Y valued at \$800,000 on 1 May.

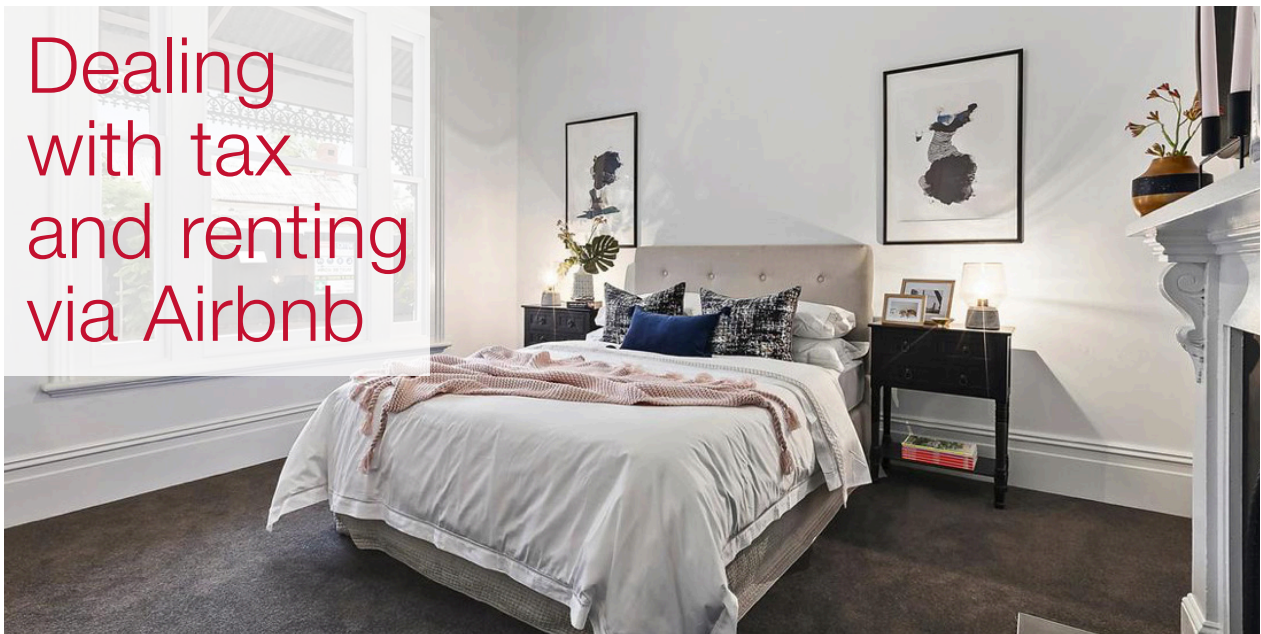
Diane requests the trustee of SMSF X in writing to commute amounts on 30 June in excess of \$1.6 million based on the value of all of her superannuation interests supporting her superannuation income streams. This includes the value of her superannuation interest supporting her superannuation income stream in APRA Fund Y. The trustee of the SMSF X accepts the request, which is documented.

The amount of the commutation is worked out by the trustee of her SMSF and is reflected in the SMSF’s financial accounts for the year ended 30 June by the due date of the SMSF’s annual return for the financial year. The amount of the commutation takes into account the value of Diane’s superannuation interest in APRA Fund Y.

According to rules, the ATO will not review the commutation provided that:

- the commutation request specifies the superannuation income streams that will be subject to the commutation within SMSF X and the order in which the superannuation income streams will be commuted, and
- Diane has not entered into a similar agreement with APRA Fund Y.

Diane will need to advise the trustee of SMSF X of the value of her interest supporting her superannuation income stream in APRA Fund Y as at 30 June in order to calculate the amount to be commuted from the superannuation income stream(s) in SMSF X. ■



# Dealing with tax and renting via Airbnb

Airbnb is one of many examples of the “sharing economy” — connecting buyers (users) and sellers (providers) through a facilitator that usually operates an app or a website. Airbnb acts as this facilitator by allowing individuals, referred to as “hosts”, to rent out a room of their house or their whole house for a short-time basis via its online platforms.

While the focus here is on Airbnb, the tax concepts outlined could be applied in a more general sense to anyone seeking to rent out a part of their home, whether through Gumtree, Realestate.com.au, Flatmates.com.au and so on.

The tax issues raised relate to hosts who:

- own their own home
- live in it full time, and
- want to generate some dollars by putting up an identifiable area of their home for rent.

As a host, the three major tax considerations that you need to be aware of are rental income, rental expenses, and capital gains tax.

## RENTAL INCOME

The main question hosts need to ask themselves here is whether a commercial amount of rent is being charged. Generally, where a room is advertised for rent at market rates to the general public through Airbnb (or a similar online directory, but we'll use Airbnb as the generic term) the arrangement is likely to be at “arms-length” and hosts would be required to declare their rental income.

## RENTAL EXPENSES

Where the rental arrangement is at “arms-length” and income is declared, hosts would be entitled to tax deductions for expenses incurred in deriving that rental income.

Expenses incurred by hosts can be split into three categories:

- Expenses that are directly associated with the rented area – deductible in full.
- Expenses that relate to shared areas – apportionment required.
- Expenses that relate to the host's private area only – not deductible.

Depreciation on furniture purchased for use in the rented room is a good example of an expense that is directly associated with the rented area of the host's home, and would be deductible in full.

Some examples of other expenses that may be deductible in full include:

- commercial cleaning of a rented area
- repairs and maintenance
- professional photography for the listing, and
- host service fees charged by Airbnb.

Where there are expenses that relate to the entire property, apportionment is required. The ATO has indicated that floor space can be used as a general approach for apportioning expenses.

*continued overleaf* ➡

### Dealing with tax and renting via Airbnb continued

Some examples of expenses that relate to the entire property and may be deducted in this way include:

- mortgage interest
- council rates
- utilities, and
- insurance.

It is important to note that where capital works are undertaken in relation to the property, capital works deductions are generally not available to hosts, as they are also using the property for their own residential accommodation.

Expenses that relate to shared areas can be apportioned based on access. In regard to using floor space as an indicator, if say one tenant and one host had equal access to shared areas, the host could therefore claim for 50% of these expenses.

Examples of expenses that relate to shared areas only, and may be deductible in this way, include:

- depreciation on furniture and appliances located in shared areas
- internet, and
- cable TV.

One final thing to note in relation to expenses is that they are only deductible where an area of the house is either actually rented out, or genuinely available for rent. For example, where a room in the host's home is only available for rent for 90 days a year, say while a housemate is away, then only the portion of rental expenses that were incurred during that 90-day period would be deductible and further apportionment may be required.

### **CAPITAL GAINS TAX**

In general terms, the sale of an individual's primary residence is CGT-free under the main residence exemption if the dwelling was their main residence for the entire time they owned it, and it was not used to produce assessable income.

However as hosts are renting out a portion of their home on Airbnb, they are using a portion of it to produce assessable rental income and therefore would only be eligible for a partial main residence exemption. This means that hosts may be taxed on a portion of any capital gain realised upon the sale of their main residence.

Remember that "pre-CGT" assets (bought before 20 September 1985) are not subject to CGT, regardless of whether they are used to derive rental income.

### **DEALING WITH A POST-CGT MAIN RESIDENCE**

The below scenarios assume the following:

- the host purchased their home post-20 September 1985 (and therefore may be subject to CGT on the sale), and
- the host would have been eligible for the main residence exemption from the time that they purchased their home until the time that they started renting out a portion of their home.

A basic scenario would be one in which a host rented out the same part of their home from the time that they purchased it until the time that they sold it. In this case, the part of the home used to produce assessable income would be subject to CGT and the private portion of the home would be CGT free under the main residence exemption. As with expenses, an apportionment based on floor space may be used to determine the portion of the property that is subject to CGT.

A more common scenario may be where the host began renting out a part of their home some time after moving in. Calculations under this scenario can differ depending on whether the host first began using their home to produce income before or after 7.30pm on 20 August 1996.

The reference "first used to produce assessable income" would generally be the first time a host rented a part of their home out (whether on Airbnb or otherwise). However, if the host had previously used part of their home as a home office or workshop at some time in the past, it may actually be that time that the home was "first used" to produce assessable income.

### **Pre-20 August 1996 property**

Where the host first used their home to produce assessable income prior to 7.30pm on 20 August 1996, they would need to calculate the portion of the ownership period in which they used the entire house for private purposes and the portion in which they were renting part of the house out.

**Purchased:** 1 July 1991 (used 100% for private purposes)

**First rented a portion of house:** 1 July 1995 (30% of total floor space apportioned to tenant)

**Sold:** 1 July 2012

**Total days house was owned:** 7,671

**Total days portion was rented out:** 6,210

**Gain on sale:** \$100,000

**Calculation:**  $\$100,000 \times 6,210/7,671 \times 30\% = \$24,286$  gross capital gain.

*continued overleaf* ⇨



### **Dealing with tax and renting via Airbnb continued**

This gross capital gain could then be reduced further by either indexation or the general 50% CGT discount, as the property was held for at least 12 months.

#### **Post-20 August 1996 property**

Where the host first used their home to produce assessable income post-20 August 1996, the calculation is slightly different. Firstly, the host is deemed for tax purposes to have acquired the property as at the date that the house was first used to produce assessable income and secondly, a market valuation, calculated at that date, may be required, which is then taken to be their deemed cost base to be used in calculating any future capital gain. This valuation could come from a registered valuer or could be calculated by the host, however it is important to note that the ATO has the power to challenge valuations.

**Purchased:** 1 July 1991 (used 100% for private purposes)

**First rented a portion of house:** 1 July 1998 (30% of total floor space attributable to tenant)

**Market value @ 1 July 1998:** \$200,000

**Sold:** 1 July 2012

**Sale price:** \$500,000

**Calculation:**  $(\$500,000 - \$200,000) \times 30\% = \$90,000$  gross capital gain.

This amount may be reduced further by either indexation or the general 50% CGT discount.

These two scenarios are relatively straightforward. Where different portions of the house were available for rent during the host's ownership period, or where the entire house was rented during some periods and was used 100% for private purposes during other periods, the CGT calculations can become very complex.

### **GOODS AND SERVICES TAX**

Income from renting out part of a residential property is typically "input-taxed". This means that hosts should not charge GST on the rent that they earn from guests. Conversely, hosts cannot claim input tax credits for any rental expenses that they incur, but are entitled to claim the GST inclusive amount of any rental expenses as a tax deduction.

Be aware however that GST may apply if a host is taken to provide "commercial residential premises" – which includes, among other things, accommodation that is a hotel, motel, inn, hostel or boarding house. Remember also that being registered for GST is subject to the host exceeding the \$75,000 turnover threshold.

### **PAYG INSTALMENTS**

If hosts report more than \$2,000 of rental income on their latest lodged tax return, they may receive a letter from the ATO notifying them that they are required to begin making periodic PAYG instalments. These are essentially prepayments of tax that are offset against the host's final tax liability at the end of the year upon lodging their tax return. ■

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This information has been prepared without taking into account your objectives, financial situation or needs. Because of this, you should, before acting on this information, consider its appropriateness, having regard to your objectives, financial situation or needs.