WALLACE PARTNERS
ACCOUNTANTS AND ADVISORS

AI AND QUALITY DATA:
A Powerful Tool for the Tax Office

After the September 11 attacks on the World Trade Center in New York in 2001, it was understood that intelligence and security authorities around the world dramatically increased their technological and detection capabilities.

continued overleaf ⇨

About this newsletter

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

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AI And Quality Data: A Powerful Tool for the Tax Office ... Cont

And, apparently, not long after, many revenue authorities around the world were said to similarly have sought better technological and detection capabilities.

In short, revenue authorities (like business) moved with the technological changes.

The same is now true of the use of AI by revenue authorities. Or at least by the Australian Taxation Office (ATO).

In a recent speech to "The AI Summit Australia", a Deputy Commissioner of Taxation emphasised that using AI in conjunction with the ATO's collected data is becoming an increasingly powerful tool for the ATO. And not just in relation to detecting tax fraud. The Deputy Commissioner also pointed out AI's ability in "analysing deductions" and "identifying income".

He concluded by saying that the ATO's approach is not to deploy AI just for the sake of AI, but to "combine quality data, strong analytics, AI capabilities and human judgement to solve real problems".

In other words, the ATO indicated that the combination of "AI" and "quality data" means it is becoming increasingly effective in matching its data with a taxpayer's information in determining whether taxpayers (of all sorts) are declaring all their income and properly claiming deductions and, in the end, paying the right amount of tax.

In this regard, the ATO recently advised that it will continue its passenger movements data-matching program, which will use passenger movement information from the Department of Home Affairs to help the ATO identify incorrect tax reporting. And this next round is due to run from the 2026-27 financial year through to the 2028-29 financial year.

And in relation to data matching generally, the ATO has advised that when using data matching information against tax returns, in relation to assessable income it looks at such things as interest and investment income, employment income, government payments, capital gains tax from the disposal of shares and property, employment-related foreign source income, payments made to contractors in the building and construction industry, and many other things.

And the upshot of this for all taxpayers is that at the very least it seems that gone are the days when taxpayers could take a "calculated risk" about whether to declare certain income or to claim certain deductions. At the most, it requires them to be very vigilant in their own tax affairs.

So, if you think this type of matter is relevant to you in any way in this new age of AI and data matching, make an appointment to see us to discuss the matter.

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Do you need to get a market value of your home at 30 June 2027?

Under the big tax changes announced in the May Budget, and now law, the generous 50% CGT discount will no longer apply from 1 July 2027 and will be replaced by the inflation-based "indexation" (except in limited circumstances).

However, it will still be available for the capital gain on an asset that accrues up to that date.

This will apply where you have acquired an asset before that date and sell it after that date (or where it is otherwise liable for CGT after that date).

In these circumstances you will need to obtain a market value of the asset as at 30 June 2027 in order to get the benefit of the 50% discount on any gain accrued up to that time (unless you choose to use the proposed alternative apportionment method).

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Do you need to get a market value of your home at 30 June 2027? ... Cont

However, you may be wondering if you will also be required to obtain a market value for your home under these new rules.

Well, this will depend on whether you already have a partial CGT liability on your home.

This will occur if, for example, before that date, you rented the home before you moved into it or where you rented it after you moved in and you cannot use the "absence concession" to preserve the exemption.

It will also be relevant if you used part of your home to produce assessable income – for example where you ran a business from home, or rented a room or a granny flat at commercial rates.

In these circumstances, you would need a market value of the home at 30 June 2027 to be able to apply the 50% discount to the partial capital gain that accrued up to 30 June 2027.

And the same would be true if the gain accrued after 1 July 2027 (i.e. where you used the home to produce assessable income after that date unless the absence concession can apply).

This is because the new rules will deem you to have sold the home and re-acquired it for its market value on 30 June 2027. This means it is treated as a newly acquired asset after that date. And any gain accruing after that date will be calculated by reference to this new market value cost base.

However, there is a major reason why a market valuation of your home is not required – or at least not at 30 June 2027.

And that is because of the peculiar rule that applies when you first use your home to produce assessable income (eg by way of renting it or for business use).

And that peculiar rule is that you are deemed to have acquired the home for its market value at the time you first use it to produce assessable income – with any capital gain being calculated by this new cost under the inflation-indexation method.

So, a market valuation may not necessarily be required on 30 June 2027 – but it will definitely be required on the date of any subsequent "first income use" of the home after that date.

The interaction of this rule and the new CGT rules for denying the discount can get a bit tricky.

It is definitely an area where you will need our expertise. So, make an appointment at any time to discuss the matter if you are in this type of scenario.

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Determining a person's residence for tax purposes is not an easy matter!

A recent Federal Court decision once again outlined the importance of determining a person's residency status for tax purposes – and moreover how difficult that may be. And that it may not just be a matter of having lived overseas for several years.

In that case, the taxpayer lived in Australia for 6 years with his young family before taking up an employment contract with a construction company in Dubai where he worked for 5 years. However, he returned to Australia to visit his family twice a year for periods of up to 5 weeks.

In addition, he only leased an apartment in Dubai – with most of his investments, belongings and personal ties remaining in Australia.

Even though he did not "reside" in Australia (in the ordinary sense of that phrase), the Court nevertheless found that he was a resident of Australia for tax purposes. This was essentially because under another element of the "tax residency test" he had not established a "permanent place of abode" outside of Australia and because his connections were still strongly with Australia.

In these circumstances, the Court held that he was "a resident of Australia" for tax purposes. Moreover, this meant that he was liable for tax in Australia on the wages he earned from working in Dubai and on any other foreign sourced income – as well as, of course, any income he earned in Australia (eg bank interest).

So, this is the main consequence of being a resident for tax purposes: you are liable for tax in Australia on income earned both in Australia and outside Australia – including capital gains from any property a person may own overseas (eg a rental property, shares).

But you also get some good tax advantages if you are a resident of Australia for tax purposes.

For a start, you are taxed at individual resident tax rates – which are far more generous than those that apply to a foreign resident. You can also access the CGT discount (at least until its general abolition from 1 July 2027) and thereafter the inflation adjusted indexation for any capital gains (whether sourced in Australia or overseas).

On the other hand, if you were a non-resident for tax purposes you could not access these concessions (albeit interestingly, a foreign resident can also use the generous CGT small business concessions if they qualify for them).

So obviously on the flip side, if you are a non-resident you will be taxed at harsher non-resident tax rates and, generally, you won't be able to access the CGT discount or the new indexation method for taxing capital gains.

But before any of these tax rules are applied, it is vital to determine a person's residency status for tax purposes. And this may not be an easy matter. As the above Federal Court case illustrates, even if you "live" overseas for a number of years you still may be considered to be a resident for tax purposes – depending on your exact circumstances.

And then there is the often more difficult issue of when exactly you become a non-resident for tax purposes, or resident (as the case may be) – and the tax rules that apply in that case. And this includes where you have a young adult child who is heading off to work and travel overseas.

So, if you or a loved one is in this type of scenario or think you will be, it is important to come and speak to us so that we can work things out and discuss the tax consequences with you.

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BRINGING YOUR OVERSEAS RETIREMENT SAVINGS HOME

If you worked overseas before settling here, you may still have money in a foreign retirement scheme. If the ATO recognises the scheme as a 'foreign super fund' you may be able to transfer it into an Australian super fund. Keep in mind the timing affects how much tax you pay.

Transfer within six months

There is generally no tax payable if the foreign super scheme is cashed or transferred to an Australian super fund within six months of becoming an Australian tax resident.

After this time, any growth on your foreign interest since you became a resident is taxed when it is cashed out or transferred into an Australian super fund. This growth is called applicable fund earnings.

Choose who pays the tax on the growth

When a foreign super fund is cashed or transferred into an Australian super fund after six months of becoming a tax resident, you are ordinarily assessed on the applicable fund earnings. However, if it is transferred into an Australian super fund the earnings can instead be included in your super fund's assessable income. In super it will be taxed at 15% instead of your marginal tax rate.

The choice is only available if you:

» transferred your whole foreign super fund interest to an Australian super fund; and

» no longer hold an interest in that fund.

Watch your contribution caps

The amount transferred into super ordinarily counts towards your non-concessional contribution cap. However, where you elect to have the applicable fund earnings treated as assessable income of the receiving super fund, any amount covered by that election does not count towards your contribution caps. Without the election, the applicable fund earnings are assessable to you personally and the full transfer counts towards your non-concessional contribution cap. If you are age 75 or over your super fund cannot receive the transfer or any member contribution.

Things to remember

There are some things to consider before cashing or transferring your foreign super. These include:

» There may be tax in the other country.

» You will need to confirm the scheme is a foreign super scheme with the ATO. If it is not a foreign super scheme different tax applies.

» The foreign super fund will have its own rules on how and when the super benefits can be taken. For example, UK pensions need to meet His Majesty's Revenue and Customs (HMRC) requirements.

Every overseas scheme has its own rules. The tax outcome depends on your circumstances. It also depends on the tax rules in the country it is coming from.

It is, therefore, important you speak to an adviser before moving your foreign super.

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SUPER AND MORTGAGE ARREARS:

What the rules already allow

It has been proposed that people who pay rent or have a mortgage be allowed to divert a quarter of their future super contributions into take-home pay for up to three years. Employers would keep paying the full 12%, but the super fund would pay 3% directly to members who opt in. Reaction to the proposal has been mixed.

However, did you know that it is already possible to access your super on compassionate grounds if you are about to lose your home due to foreclosure?

Know how much you can take

You can apply for a lump sum of up to three months of mortgage repayments plus 12 months' interest on the outstanding balance. If your repayments are $1,200 a month and 12 months' interest comes to $9,600, the most you can request in a 12-month period is (3 x $1,200) + $9,600 = $13,200.

DID YOU KNOW?

Accessing super under compassionate grounds to stop a forced sale applies to your home only. Investment properties do not qualify, and neither does rent. If you are renting and behind on payments, you may be eligible to draw a lump sum from super under severe financial hardship. To qualify you generally need to be unable to pay living expenses, such as rent, and be in continuous receipt of income support payments, such as JobSeeker, for 26 weeks.

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Super and Mortgage Arrears: What The Rules Already Allow ... Cont

To qualify you must satisfy the following:

- The property is your principal place of residence.
- You are legally responsible for the mortgage repayments or the council rates.
- You have written advice that the home is to be foreclosed, sold or repossessed, either a default notice from your lender or a council notice that rates have been outstanding for two or more years.
- You have no capacity to pay the amount needed to stop the sale.

Know which debts are covered

There are three debts that are covered under this option to access super:

- Mortgage arrears where the lender has issued a repossession or sale notice.
- Council rates in arrears for two or more years where the council has given written notice it will sell your home.
- A debt to a third party where a court order authorises an enforcement officer to sell your home to pay it.

Necessary paperwork

For mortgage arrears you need the default notice, a utility bill less than three months old in your name showing the property address, and a letter from each lender on its letterhead dated within 30 days of your application. That letter must state the overdue amount, the amount owing to stop the sale, the property address, three months of repayments, 12 months' interest, and who is responsible for the loan.

Council rates applications need the utility bill and an equivalent council letter itemising the arrears year by year. If you cleared the arrears by borrowing elsewhere, you can still apply, but you will need documents showing what was owing at the time.

REMINDER

Money taken out of super early can greatly impact your savings at retirement. Keep in mind withdrawals may also be subject to a maximum 22% tax (including Medicare levy). Don't forget to speak to your adviser to discuss your options.

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Government moves to tighten protections in super

Around 11,000 Australians invested about $1.1 billion of their retirement savings in the Shield and First Guardian Master Funds. These two managed investment schemes collapsed, costing investors their savings. Some investors have been compensated by their platform provider. However, many have not. The Government recently set out several changes to super to help protect members' retirement savings. Let's look at some of the proposed changes.

Watch for a cap on advice fees taken from your super

Your super fund cannot deduct personal advice fees from your account without your written consent. However, the law does not limit how much can be deducted where there is written consent. APRA-regulated fund trustees would have to set caps on how much may be deducted and keep watch that these caps are not breached. The Government is particularly concerned about people with small super balances paying fees that substantially erode their savings.

Expect much larger penalties for trustees of APRA-regulated super funds

The Government does not believe the current penalty level is large enough to deter APRA-regulated funds from breaches. The maximum civil penalty for core breaches of an APRA-regulated fund trustee's obligations would rise from 2,400 penalty units to 50,000 penalty units. From 1 July 2026, a penalty unit is $364. On that basis in dollar terms the maximum penalty would rise from about $873,600 to about $18.2 million.

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Government moves to tighten protections in super ... Cont

ASIC to get more powers

ASIC would also be able to direct an APRA-regulated fund trustee to compensate members if an investment option fails and the trustee has not met its obligations. This would be a faster and easier option for investors compared to complaining to AFCA.

Know what is changing for SMSFs

Several changes are proposed if you have an SMSF or are thinking about setting one up.

- The ATO would be able to block rollovers into a new SMSF while it investigates fraud, financial abuse or misconduct, or where it suspects potential harm. The ATO can already stop rollovers in practice by withholding new SMSFs' details from Super Fund Lookup. This new power would allow the ATO to stop rollovers even after the fund is registered and listed.
- Trustees would have to complete trustee education before registration. At present it is only necessary to sign a declaration confirming you understand your duties. There is no obligation to do any prior learning about your obligations as a trustee.
- Your fund would need a uniquely identifiable bank account. Treasury has not said what that would require in practice.
- New funds would need a written investment strategy from the start. The current rule is that SMSFs must have an investment strategy that is reviewed regularly. The changes would require the investment strategy to be in writing and in place from the start of the fund.
- The ATO would collect more information about advisers and others involved in setting up your SMSF, and about ongoing advice fee deductions.
- The supervisory levy would rise from $259 to $295, and new funds would pay their first levy when they are set up.

REMINDER

These measures still need to be legislated, so the detail and the start dates could change.

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