The Case Of Input Tax Credit Entitlement And The Case Of Capital Gains Tax

Question 1: The Case of Input Tax Credit Entitlement

A. Outline

Real estate firm, City Sky Co. deals in property in two main ways:

a. Construction

City Sky Co. has commenced a project related to constructing and developing residential apartments, which will be sold after they are completed. The company has even registered for Goods and Services Tax (GST), as an important legal and accounting aspect of selling in the market.

b. Facilitating transactions in property

This includes buying, selling, advising, and providing investment services in real estate

City Sky Co. has hired a registered local lawyer, Maurice Blackburn, to assist in all the legal aspects related to the construction project in particular. Mr. Blackburn practices as a sole proprietor and earns approximately three-hundred thousand dollars in income per year.

B. Details

Following are the details of the legal aspect of operating City Sky Co.

a. Rules and Regulations

GST is a value-added tax levied on goods at different stages of production, till they reach the end consumer. The name suggests that the tax is applied at each stage that the value is added to the goods. In Australia, the main regulation dealing with GST and the legislations related to it is the Goods and Services Act 1999, which is also known as the New Tax System Act 1999.

i. Why is GST needed?

Payment of GST is mandatory by law, on all the goods and services that are sold in the market, with a few exceptions. The New Tax System Act 1999 under Section 7-1 accounts for the GST. The law allows those registered entities with the right to utilize input tax credit entitlements on acquisitions, that is, all the things that they paid GST for, through the process of value addition.

- The items that are to be taxed are known as “taxable” under Section 9-5, these include:
- Those items which are provided or traded against money
- Those items that are provided or supplied by an entity that is registered for GST, and

required by law to register for GST
- Those items that come under indirect taxation as per the law in Australia

ii. GST-Free supplies

Property is one of those items that are input taxed, however, there are regulations pertaining to its use. Under Section 40-65, the property used to carry out any commercial activity such as sale of commercial or residential property for sales is compulsorily subject to GST, and not input tax. There are a few items that are classified as GST-Free or input taxed. GST-Free items are part of Division 38, and explains details where no obligation is present. The Division 40 pertains to the rules related to items on which GST is not levied, however input tax is mandatory. The items exempted to pay GST or input tax, their registered enterprises do not receive input tax credit entitlements either.

b. Legal Guidance

In order to take benefit of input tax credit entitlements, City Sky Co. would require to satisfy two necessities:

- Its products are subject to tax
- It should be registered for GST

Both the necessities are satisfied. Moreover some more requirements need to be satisfied as City Sky Co. is involved in construction or property and investments. The property that is built should be:

- A commercial building
- A residential building and used for commercial activity
- A residential building that will be sold

City Sky Co. aims to construct apartments on this piece of land and so the third criteria is satisfied for this to be considered input tax. In any case, the apartments have to be registered for GST. The company is also entitled for input tax returns or credit for the materials or services that are creditable. In the current scenario, the legal services that are obtained by City Sky Co. for the building of new apartments are also beneficial for getting input tax return. So one could conclude that City Sky could get input tax returns or credit on two criteria:

- The service should be creditable acquirement
- The service provided should operate under a license registered for GST

City Sky fulfils both these conditions because the lawyer is GST registered, and the legal service will have input tax credit.

Value of Input tax credit

The amount that City Sky Co. will receive in input tax credit will be the same as the amount of GST that has been paid for it, either it is in the form of goods or services. This can be determined by calculating the value of the good or service and then finding 10% of this value.

C. Conclusion

As per the discussion above, the products and services provided by City Sky Co. have to pay GST as per the law in Australia. However the company could take benefit of input tax credit on all the acquirements during the construction process as it qualifies for such criteria. The input tax credit obtained through legal services from Mr. Blackburn who is a registered lawyer is valued at $3,000.

Question 2: The Case of Capital Gains Tax (CGT)

A. Outline

During the year 2015, four assets were sold by Emma, namely:

1. A plot of property which was obtained for investment in 1991
2. Few collectable stamps bought in January 2015
3. A large piano obtained in 2000
4. Shares in Rio Tinto, bought in 1982

B. Details

The above situation will be analyzed as per relevant laws.

a. Rules and Regulation

Capital gains of the profit from selling assets is part of taxable income in Australia, and the Income Tax Assessment Act 1997 is the pertinent act for legislation of income tax. The legislation for income tax is pertinent for capital gains tax as well. In the current situation at hand of Emma, below are the rules and regulations that need to be elaborated on.

i. Capital Gains Tax Assets and Events

The Income Tax Assessment Act 1997 has Section 100-10 about an individual who performs transactions pertaining to capital gains events, has to satisfy the requirements for any possible capital gains or losses. More information is provided in Division 104 about the events that can give rise to capital gains tax requirements. Of these is event A1 where a capital gains tax asset is sold is of high value. Section 100-25 states that CGT assets include land, shares, and personal assets with worth more than $10,000; and units in a trust and collections with value more than $500, as liable for capital gains tax.

ii. Calculations

Section 100-50 states the following procedure for capital gains tax calculations:

Some other major concepts in this regard are discount gains and losses, Division 115 pertains to it. Section 115-100 is about the % of discount that is levied capital gain that is discount gain. Australian resident who stays in the country during the entire ownership has to give the percentage of 50%. Moreover, certain criteria has to be met of an asset can only be considered

as a discount asset. The criteria is given below:

1. The asset's acquirement, purchases and sales should be through a person, insurance firm, or trust (as per Section 115-10).
2. The asset should be sold after 21st September 1999, 11.45 am according to the Australian Capital Territory time – ACT (as per Section 115-15)
3. The cost of acquirement, purchase and sales should not be indexed (as per Section 115-20)
4. The assets should be under the ownership of same person for twelve month before it is sold to someone else (as per Section 115-25)

iii. Compliance

Compliance with capital gains tax is stated in Income Tax Compliance Act 1997, Section 100-55. It can be of the following two forms:

1. In case the net capital gain arises after the sale of asset(s), it needs to be recorded as income while the income tax returns are filed for the same year in which the capital gains event occurs.
2. in case a net capital loss in incurred in a particular year, it can be transferred to the upcoming financial year

b. Legal Guidance

The following points could be made use of as legal guidance for any person who may have capital gains or losses during a year. The case in point here is of Emma.

i. Capital Gains Tax

Considering the case of Emma, the assets need to be analyzed to check of they qualify for being considered for capital gains tax or not. Her assets were property, shares, collectables and piano. According to the law, the property and shares are clearly classified as assets that have capital gains tax. As for piano and stamps, the cost should be more than $500. In this case, the piano is worth $80,000, and the stamps are worth $50,000, so clearly they too classify as capital gains taxable assets.

ii. Capital Gains Event

There are four assets that are sold, so four capital gain events have occurred. All four of these will be considered separately and cannot be amalgamated to consider a single event. It was mentioned earlier that a CGT event A1 is when the asset is purchased or sold after 21st September 1999, such as the shares bought by her in 1982, so the requirement has not been met. And so in Emma's case, three capital gains tax events have occurred.

Conclusion

During the year 2015, Emma sold four assets which include land, shares, stamps and piano. All four of these qualified as capital gains taxable assets due to their nature and value. However

only three were classified as capital gains taxable events because of the date at which they were bought. Her shares of Rio Tinto were purchased in 1982, before the legislation of Income Tax Assessment act of 1997 came into being. Two events lead Emma to have capital gains, however one event where the asset was not kept for more than 12 months will levy calculating discount gain.

The final calculation reveals that Emma make a capital gain of $266,750 during the financial year 2015. She needs to record this amount as part of her assessable income in the income tax returns for the year 2015, as it is her legal obligation.