



THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2016

PAPER 2.01 – AUSTRALIA OPTION

ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

TIME ALLOWED – 3¼ HOURS

You should answer **FIVE** out of the eight questions: **BOTH** questions from Part A; **ONE** question from Part B; and **TWO** questions from Part C.

Part A questions are worth 25 marks each. Part B questions are worth 20 marks. Part C questions are worth 15 marks each.

You should aim to spend approximately half of your exam time answering Part A, and the remaining half answering Parts B and C. The amount of time you spend answering each question should correspond broadly to the number of marks available for that question.

Start each answer on a new page. If you are using the on-screen method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.

All workings should be made to the nearest month and Australian Dollar, unless the question requires otherwise.

Marks are specifically allocated for presentation.

PART A

You are required to answer BOTH questions from this Part.

1. Harold Battersby is an Australian resident who entered into a contract to purchase a property in Surrey Hills, in Sydney, on 1 May 2014 for \$800,000. The contract for purchase was settled on 4 August 2014.

The property was bought without vacant possession. The tenant continued to occupy the property, paying \$820 per week.

To finance the acquisition, Harold borrowed \$900,000 (the full acquisition price plus extras such as stamp duty, legal fees and insurance costs) at an interest rate of 5.7%. The security on the loan comprised the Surrey Hills property as well as Harold's domestic residence in Kensington, Sydney.

You are required to advise Harold regarding the following specific issues:

- 1) **Is the interest Harold pays fully deductible? Harold has real concerns, especially because of the security provided in the form of his residence and the fact that interest will exceed the rent that will flow from the property investment at least for the first few years.** (6)
- 2) **Shortly after purchasing, Harold organised some roof repairs for some \$18,000. Is this amount deductible?** (6)
- 3) **Harold purchased a gas water heater in October 2015 for \$6,500. Can he deduct that amount for the year to 30 June 2016? If not, then how should he treat the expense for tax purposes?** (5)
- 4) **If he were to sell the property by an exchange of contracts in early 2016 but with a delayed settlement in late 2016, when would Harold be treated as having purchased and sold the property for tax purposes? What would be the relevance of the exact date of purchase and the exact date of sale?** (4)
- 5) **If Harold were to sell the property in early 2016, would he be required to pay Goods and Services Tax (GST) on the sale and, if so, how would it be calculated? You may use hypothetical numbers to explain your answer.** (4)

Total (25)

2. BGE Pty Ltd (BGE) is an Australian resident private company which, on 15 April 2015, declares and pays a fully franked dividend of \$70,000 to each of its five equal shareholders. The shareholders are:

- (a) Ms Rebecca Johnson, a widow resident in Australia who receives Age Pension and derives no income other than her pension and the dividend from BGE;
- (b) Ms Tammy Fernandez, a wealthy heiress who is resident in Australia with income in excess of \$2 million per year;
- (c) Growth Co Pty Ltd, an Australian resident company;
- (d) Jack Law, a resident of the USA; and
- (e) The XYZ Superannuation Fund, a complying Australian superannuation fund.

Continued

2. Continuation

You are required to answer the following questions:

- 1) **Explain, in relation to each of the shareholders, how (if at all) tax will be payable on the dividend received from BGE. In each case, perform an approximate calculation based only on the information you have available, as to the tax each shareholder is likely to pay. (18)**
- 2) **After the close of the 2015 year of income, BGE realises that it had over-franked the dividend paid on 15 April 2015. On revised calculations, it should only have franked the dividend to 80%.**

What are the ramifications of this error, for BGE and for each of the five shareholders? (7)

Total (25)

PART B

You are required to answer ONE question from this Part.

3. A company incorporated and tax resident in the People's Republic of China, Company Q, purchased the following assets in Australia in November 2010:
- 30,000 shares in Masfarmers Ltd, an Australian public company which has as its main business the Johnson supermarket chain, at a price of \$24 per share;
 - 30,000 shares in Wight, an Australian private company, which holds as its main assets an amount of real estate situated in Australia, at a price of \$2.20 per share;
 - Real estate consisting of farmland in central New South Wales, at a price of \$6,200,000; and
 - A milk producing business, DairyVic, based in rural Victoria, for a global price of \$2,600,000. The business's assets comprised land, plant and equipment, inventory, a trademark, and goodwill.

Company Q decided to sell the assets in May 2016, at the following prices:

- 1) The shares in Masfarmers Ltd at \$44 per share;
- 2) The shares in Wight at \$3 per share;
- 3) The farmland in New South Wales, at \$8 million; and
- 4) DairyVic, at \$14 million.

You are required to detail the Australian tax to be paid by Company Q on each of these sales. (20)

4. A recently passed Act of the Federal Republic of Selesia (the FRS) contains the following Division:

Division 26 – Withholding Tax in the FRS

LIABILITY

Withholding Tax is payable in respect of all prescribed payments.

RATE

The Rate of withholding tax is to be 20% in all cases unless the payment is an amount for which a deduction is not and cannot be claimed in the FRS. In that case the rate of withholding tax is 15%.

BASE

Withholding tax is applied to the gross payment made from FRS with no reductions.

FINAL TAX

Withholding tax is a final tax.

Continued

4. Continuation

PRESCRIBED PAYMENT

Prescribed payment means a payment of interest dividend royalty and rent paid by a resident of the FRS to a person or entity resident outside the FRS.

You are required to answer the following questions:

- 1) Explain how the FRS withholding tax rules differ to those in Australia. (8)**
- 2) Are there deficiencies in the FRS rules that are dealt with in the Australian rules? (8)**
- 3) Are there deficiencies in the Australian rules which are dealt with in the FRS rules? (4)**

Total (20)

PART C

You are required to answer TWO questions from this Part.

5. You are required to calculate the amount of goods and services tax (GST) included in each of the following transactions:
- 1) A module fee of \$2,200 paid to a university for tuition, in which the module forms part of a diploma course. (2)
 - 2) A fee of \$330 paid to the same university for the residential component of the course. (2)
 - 3) A private health insurance premium of \$2,200. (2)
 - 4) A contract fee of \$22,000 paid to a manufacturer in France for goods being delivered in Paris. (1)
 - 5) A total payment of \$198,000 for the purchase of a business. The total cost is broken down between the various business components as follows: machinery, \$30,000; raw materials, \$20,000; brand name, \$40,000; and goodwill, \$108,000. (2)
 - 6) A fee of \$4,400 for the import into Australia of a sophisticated wheelchair from Germany, for use by a disabled person. (2)
 - 7) The sale for \$880,000 of residential property which had been used by the vendor for the purpose of deriving rent from residential leases. (2)
 - 8) The sale for \$880,000 of commercial property which had been used by the vendor for the purpose of deriving rent from commercial leases. (2)
- Total (15)
6. You are required to complete any TWO of the following three tasks:
- 1) Explain in your own words the operation of Part IVA of the Income Tax Assessment Act 1936, how it compares to, and in particular how it differs from, Division 165 of the Goods and Services Tax Act.
 - 2) Explain in your own words how trusts are taxed in Australia in cases when only Australian resident beneficiaries and income are involved. You should explain, in particular, what happens both to income to which a beneficiary is presently entitled, and to income to which no beneficiary is entitled.
 - 3) Explain how a partnership is taxed in Australia and how, if at all, this differs from the way in which a company is taxed. You should consider whether there are any cogent arguments to support the view that trusts should be taxed like companies, and what problems this could give rise to.
- Total (15)
7. You are required to explain how dividends paid by a foreign resident to an Australian shareholder are taxed, when derived by the Australian shareholder. Your answer should focus, in particular, on the circumstances which lead to different results, and the key factors which determine the tax treatment. (15)

8. You have been asked by the Treasury Department of a foreign country, Merilania, to answer the following questions relating to the operation of the Australian fringe benefits tax (FBT):

- 1) What benefits are covered by FBT?
- 2) Who is liable to pay FBT?
- 3) When is FBT payable, and at what rate?
- 4) Is FBT deductible for income tax purposes?
- 5) How can FBT be avoided or minimised, and are there ways to stop such practices?

You should note that the Treasury Department is especially interested in understanding the practical workings of FBT and, while you are invited to make general observations, you are required to cover the above matters in particular.

(15)