
Tax Case Study: Calculations Of Taxable Income

Answer to Question 1

The amounts that Joe should include in his taxable income for the year ended 30 June 2019 is as follows:

- Income received from clients for electrical services of \$150000 should be included in the tax returns under section 6-5 as ordinary income under ITAA 1997. Any deductions that can be claimed against this income is allowed as a deduction from the taxable income earned by the person during a year and the net amount should be shown in the tax returns. The PAYG withholding tax that he has paid to the relevant tax authorities is allowed as deduction in his hands from the annual assessable income earned by him (Ato.gov.au 2019). Hence the PAYG tax of \$45000 paid by him is to be deducted from the annual assessable income earned by him during the course of the year;
- Under Section 30-15 of ITAA 1997, amount contributed as a donation to any charitable institution that is located in Australia and is covered under subdivision 30-B of the act can be deductible in the hands of the taxpayer. Under section 30-315, the Australian Red Cross Society is covered as a charity and the payments made to it are allowed as a deduction in the hands of the taxpayer (Ato.gov.au 2019). In this case, although the payment is not being received directly but being sent to a charity, the deduction is still applicable. Hence, the total amount of \$3000, that has been sent as a contribution to Red Cross but not received directly by Joe can be deducted from the income earned during the year;
- According to the rules of ATO, any amount that is earned by a person in the form of a gift for personal purposes like birthday or on any other special occasions is not taxable in his hands. However, if the same amount is received for providing a service to a client or for any other unstated purposes, then the amount is not allowed as a deduction in the hands of the person receiving the gift (Ato.gov.au 2019). The iPad received as a gift from the client is to be declared in the income tax returns as it has been received for the services provided by him and it has not even been received on a special occasion. Hence, tax will be charged on the market value of the IPod, which is \$5000;
- The non-transferable voucher and all expenses paid trip received from the client are gifts that are not a part of those received from family on personal occasions. Hence, these should be included in the taxable income of a person for the year in which they are earned. Therefore, the entire amount of \$2000 and \$1250 cannot be claimed as a deduction from the income earned during the year and hence are included in the aspect of other income earned by Joe during the financial year;
- Capital gains tax is applicable on the sale of shares if they are acquired on or after 20 September 1985. This is because CGT started to become applicable in Australia from that particular date. For assets acquired before this date, tax is not charged on the amount earned from the sale of the assets. If the business of the taxpayer is that of trading in shares, then the amount received on sale of shares is treated as ordinary income earned by him during the year (Ato.gov.au). In this case, ignoring indexation, the amount of capital gains earned by Joe, \$680000 are to be treated as taxable income in his hands for the year;

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- The sports car comes under the purview of section 118.5 of ITAA 1997. This section suggests that the capital gain or capital loss earned on the sale of motor car or other related assets is to be disregarded (Legislation.gov.au. 2019). Hence, as the car has been purchased and used by Joe, it is a part of his assets. As per the guidelines of ATO, a vehicle that does not have the capacity to carry more than 9 people at once and a weight of less than one tonne constitutes a car. Hence, car is a part of a personal use asset that However, the capital gains earned on its sale are not covered under the taxable income earned during a year;
 - According to section 118.10 of ITAA 1997, a capital gain or capital loss earned from the sale of a collectible is to be disregarded if the cost of acquiring it was less than \$500. As the cost of acquisition of both the paintings are greater than \$500, capital gains or losses earned from them are to be included in the assessable income earned by Joe for the financial year;
 - Speedboat is a personal use asset as defined by section 108.20 of ITAA 1997. According to section 118.10, the amount of capital gains earned from the sale of an asset are to be exempted if the cost of acquiring the asset was less than \$10000. If the cost of acquiring the asset was more than that, then the capital gains or losses earned from the sale are to be charged in the hands of the taxpayer. In this situation, as the cost of the speedboat is more than \$10000, the amount earned on its sale is liable for being charged under the capital gains tax as per the rules of the ATO.
 - Apart from the above mentioned expenses, Joe is also the owner of a shop that is responsible for the income earned by him during the course of a year. He is involved in renting out the shop to others and making income from the same. As it is a part of his business income, the rent earned by Joe should be considered to be a part of the ordinary income earned by him during the course of a year under section 6-5(2) of ITAA 1997. Hence, all the expenses that are incurred by him in relation to the rental property are to be included in the income tax returns filed during the year. They are also allowed as a deduction from the income assessable in his hands during the financial year.

Answer to Question 2

The taxable income on which Joe is liable to pay his taxes for the given financial year during which his income is being assessed is as follows:

- Particulars
- Amount

Amount

Income from business

Payments received from clients for electrical services 150000

Other Income

Rental Income received during the year 60000

IPad gift from client 500

Non-transferable voucher received from client 2000

Cost of trip to Melbourne Expo 1250

Income from Capital Gains

Capital gains on sale of shares 680000

Capital gains on sale of Painting A 300

Capital gains on sale of Painting B 200

Capital loss on sale of speedboat (8000)

Net Income 886250

Less: Amount eligible to deducted

PAYG instalments (45000)

Amount contributed to Red Cross (3100)

Telephone calls to clients (350)

Council Rates (1680)

Insurance (850)

Paintings on the internal walls of the shop (1025)

Paintings on the external walls of the shop (1160)

Trimming of shop (750)

Replacement of floor (1200)

Interest on shop mortgage (5078)

Fees paid to tax agent (1500)

Net Expenditure (61693)

Taxable Income 824557

References

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3. Ato.gov.au. 2019. Claiming mobile phone, internet and home phone expenses. [Online] Available at: <https://www.ato.gov.au/Individuals/Income-and-deductions/Deductions-you-can-claim/Other-work-related-deductions/Claiming-mobile-phone,-internet-and-home-phone-expenses/> [Accessed 24 Sep. 2019].
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