

# client alert | explanatory memorandum

October 2023

**CURRENCY:**

This issue of **Client Alert** takes into account developments up to and including 25 September 2023.

## ASIC calls on lenders to support customers

With the cost of living crisis and increase in interest rates hitting Australian households, there is growing evidence that many are falling into financial stress. It is with this background that the Australian Securities and Investments Commission (ASIC) has issued an open letter to various banks, credit institutions, and lenders, calling on them to ensure that their customers have the appropriate level of support. It reminds lenders that they must have suitable arrangements in place to respond to the requests for assistance from customers and work cooperatively to find sustainable solutions.

There is increasing evidence that a growing number of consumers are starting to report high levels of financial stress. For example, the National Debt Hotline has received a 28% increase in calls this year compared to the last financial year, and delinquencies and hardship application volumes are also starting to increase. Based on early engagement information obtained by ASIC, several important areas of focus for banks and credit institutions were identified.

ASIC has reminded lenders that under s 72 of the National Credit Code, providers must consider varying a customer's credit contract if they are notified that these credit obligations are unable to be met. Credit providers must also ensure that credit activities authorised by their licence are engaged in efficiently, honestly and fairly. First and foremost, to meet their obligations, lenders must proactively communicate to customers about the circumstances in which they can seek hardship assistance and the options that are available.

Hardship options may be temporary (eg deferring a payment) or permanent (eg setting up a payment plan or altering/varying loan repayments). Applications for financial hardship will usually be required to provide proof of hardship including reasons for the hardship, current income and other major financial expenses, as well as the level of repayments that can be afforded at the current time.

Customers worried that seeking hardship arrangements will permanently affect their future credit scores can rest easy knowing the effects are only temporary. While hardship arrangements for certain credit products such as loans or credit cards can appear in credit reports, the report will only show the months the arrangement is in place, or if the arrangement is permanent, the month the loan is varied, no other details are included and the listing will be deleted after 12 months.

Where a hardship application is granted, lenders should contact customers as the period of assistance comes to an end, to understand their most up-to-date financial circumstance and consider whether further assistance is required. This includes ensuring that customers understand what happens to any arrears that may exist at the end of the hardship assistance period. Where a customer's hardship assistance is denied, written reasons must be provided along with other options including making a complaint to the Australian Financial Complaints Authority (AFCA) about the decision. Lenders should also encourage customers to reach out and talk about further options including non-hardship arrangements on offer.

Ensuring customers receive the appropriate level of support will be an important compliance area for ASIC over the next 12 months. To facilitate that, it will commence data collection, involving 30 large lenders, to collect application-level information relating to financial hardship. ASIC will also initiate a review of 10 large home lenders to understand their approach to hardship through the use of questionnaires, review documents, and meetings with staff of selected lenders. Differences in lenders' approach to hardship will be gleaned from case studies and hypothetical applicant exercises with results and insights to be released early to mid-2024.

Source: <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2023-releases/23-235mr-as-cost-of-living-pressures-persist-asic-calls-on-lenders-to-support-customers-in-financial-hardship/>

## Subscriptions included in digital adoption boost: ATO clarification

The ATO has advised that new and ongoing subscription costs can also qualify as eligible expenditure for the purposes of the digital adoption boost. This was not specified in the ATO's original release on the measure.

The bonus deduction was announced in the October 2022 Federal Budget and was enacted by the *Treasury Laws Amendment (2022 Measures No 4) Act 2023*.

The additional 20% tax deduction applies to eligible expenditure incurred between 7:30 pm AEDT on 29 March 2022 and 30 June 2023. The boost is for business expenses and depreciating assets and is capped at \$100,000 of expenditure per income year. Eligible claimants can receive a maximum bonus deduction of \$20,000 per income year. It is only available for small and medium business entities – that is, those with aggregated annual turnover of less than \$50 million for the income year in which the expenditure is incurred.

### Eligible expenditure

In the original release, the ATO stated that eligible expenditure may include, but is not limited to, business expenditure on:

- digital enabling items – computer and telecommunications hardware and equipment, software, internet costs, systems and services that form and facilitate the use of computer networks;
- digital media and marketing – audio and visual content that can be created, accessed, stored or viewed on digital devices, including web page design;
- e-commerce – goods or services supporting digitally ordered or platform-enabled online transactions, portable payment devices, digital inventory management, subscriptions to cloud-based services and advice on digital operations or digitising operations, such as advice about digital tools to support business continuity and growth; and
- cyber security – cyber security systems, backup management and monitoring services.

### ATO clarification

In its latest release, the ATO states that a good rule of thumb is to consider “if the small business would have incurred the expense if they didn't operate digitally. That is, if they hadn't sought to adopt digital technologies in the running of their business”. Using this rule of thumb, the ATO confirms that these costs are eligible:

- advice about digitising a business;
- leasing digital equipment; and
- repairs and improvements to eligible assets that aren't capital works.

Whether some expenditure is eligible for the boost will depend on its purpose and its link to digitising the operations of the specific small business. For example, “the cost of a multifunction printer would not be eligible if it were intended to only make copies of paper documents. However, it would be claimable if being used to convert paper documents for digital use and storage”.

Importantly, the ATO states that new and ongoing subscription costs can also qualify as eligible expenditure if it relates to a taxpayer's digital operations: “For example, your clients' ongoing subscription to an accounting software platform for their business would qualify. Likewise, a new subscription for digital content that is used in developing web content to advertise their business would be eligible.”

### Ineligible expenditure

The original release states that the following expenses are not eligible for the boost:

- salary and wages;
- capital works costs (but see depreciation below);
- financing costs;
- training or education costs (noting though these may be eligible for the skills and training boost); or
- expenses that form part of trading stock costs.

Those eligible for the research and development (R&D) tax incentive can claim both the bonus deduction and the R&D notional deduction. The bonus deduction will not affect the amount of the R&D notional deduction. However, the R&D notional deduction amount is the actual expenditure amount, not the expenditure amount and the bonus deduction amount.

## Depreciating assets

The original ATO release reminds taxpayers that the bonus deduction can also apply to expenditure on a depreciating asset. The asset must be first used or installed ready for use for a taxable purpose between 7:30 pm AEDT 29 March 2022 and 30 June 2023. This rule does not apply to expenses incurred in the development of in-house software allocated to a software development pool, consistent with current pooling rules.

Source: [www.ato.gov.au/Business/Income-and-deductions-for-business/Deductions/Small-business-technology-investment-boost/](http://www.ato.gov.au/Business/Income-and-deductions-for-business/Deductions/Small-business-technology-investment-boost/)

[www.ato.gov.au/Tax-professionals/Newsroom/Income-tax/Questions-about-the-technology-investment-boost/](http://www.ato.gov.au/Tax-professionals/Newsroom/Income-tax/Questions-about-the-technology-investment-boost/)

## Small business litigation funding: improvements recommended

A recent Inspector-General of Taxation and Taxation Ombudsman (IGTO) has recommended improvements to the small business litigation funding program. The report from the IGTO was mainly based on two completed dispute investigations, with a further three investigations under way. The original intention of the funding program was to mitigate the disadvantage that small business taxpayers face against the ATO, which is a well-resourced and experienced litigant in proceedings which are often complex and costly.

The IGTO report presents recommendations aimed at delivering better access to justice and fairness for small businesses by improving the operation of the small business litigation funding program. The investigation program was announced in 2019 with the original intention of mitigating the disadvantage that small business taxpayers face against the ATO, which is a well-resourced and experienced litigant in proceedings that are often complex and costly.

Taxpayers that are self-represented in the Administrative Appeals Tribunal Small Business Taxation Division (AAT SBTB) in disputes with the Commissioner of Taxation are generally eligible for litigation funding where the ATO engages external legal representation. Eligible small business taxpayers will have reasonable costs of engaging an equivalent level of legal representation covered. A litigation funding offer will be made to eligible taxpayers and should it be accepted, a letter of agreement containing terms of funding will need to be signed for the funding to commence.

After signing the agreement, taxpayers will need to provide the ATO with an estimate of the costs that they are expected to incur in relation to the legal representation for the AAT SBTB within 30 days of the date of the agreement. Any updated estimate of costs of representation that are likely to exceed the original estimate are required to be provided to the ATO as soon as practicable.

In the IGTO's two completed dispute investigations, taxpayers expressed concerns that the ATO had attempted to cap the funding to levels below that necessary to run their matter. In addition, there were also questions as to the ATO's calculation basis for reimbursements which taxpayers were not made aware of when entering these agreements, and the ATO's "numerous emails to the taxpayers' legal representatives questioning the bills which ... detracted from case preparation".

To mitigate these concerns in future cases, the IGTO produced recommendations, including:

- for the ATO to amend the template funding agreement entered into between the ATO and taxpayer applicants in the Tribunal to accord with underlying policy objectives of the program, provide greater up-front clarity on what expenses will and will not be paid, and to ensure that relevant terms are incorporated into the contractual agreement;
- in consultation with the small business community, the legal profession and the Australian Small Business and Family Enterprise Ombudsman, for ATO guidance material and internal instructions to be amended to provide greater up-front clarity to taxpayers, their representatives and internal ATO staff;
- considering whether additional steps are necessary to preserve the integrity of the program with respect to applicants that are related or otherwise connected to their legal representatives, and to raise applicants' awareness of the fees charged by their legal representatives and the extent to which they are reimbursed by the ATO; and
- for ATO procedures to be amended to establish a process for appropriately dealing with supporting claim documentation that contains information which is confidential, privileged, or the disclosure of which might otherwise prejudice the applicant in active litigation.

The IGTO notes that without the adoption of its suggested improvements to litigation funding by the ATO, further dispute investigations should be expected. Meanwhile, in response, the ATO considers itself to be no longer bound by the original policy intent of the program, and have continued to confine the findings of the report to the two cases investigated, notwithstanding similar ATO actions and decisions that have been subject to further complaints to the IGTO.

However, it is understood that the ATO does have the intention to consult with stakeholders before committing to any improvements and that the IGTO recommendations contained in the report will be considered as a part of this process. While changes may not be forthcoming for the small business litigation program, the takeaway for taxpayers is that they can always turn to the IGTO which provides an independent body to investigate the ATO's decisions.

Source: [www.igt.gov.au/investigation-reports/improving-the-operation-of-the-small-business-litigation-funding-program/](http://www.igt.gov.au/investigation-reports/improving-the-operation-of-the-small-business-litigation-funding-program/)

## **SMSF compliance activity escalation**

The ATO has ramped up compliance activity in the self managed super fund (SMSF) space in response to an increasing number of funds that have been identified as not complying with superannuation obligations. For the 2023 year, the ATO says it has issued double the amount of tax and penalties when compared with the 2022 income year, and the number of disqualifications has tripled. According to the ATO, the most common reason for applying penalties was SMSFs allowing illegal early access of super benefits by fund members.

After a relatively quiet period in the SMSF compliance space due to the effects of the pandemic and its aftermath, the ATO is once again bolstering its compliance activities. This has occurred in response to an increasing number of funds being identified as not complying with their superannuation obligations.

For the 2023 year, ATO compliance actions included issuing an additional \$29 million in income tax liabilities, administrative and tax shortfall penalties, and interest on SMSF trustees and/or members, which is double the amount of tax and penalties the ATO issued in 2022. In addition, a total of 753 trustees were disqualified in the 2023 income year, and that is more than triple the amount of disqualifications in the 2022 income year.

According to the ATO, the most common reason for applying penalties was the illegal early access of super benefits by fund members. It reminds SMSF trustees that they have a responsibility to ensure that members have met a condition of release before any funds are released. Trustees should also be aware that some conditions of release have cashing restrictions which restrict the form of benefit (ie lump sum or pension) or the amount of benefit that can be paid.

Common conditions of release include the fund member having reached preservation age and retired, or commenced a transition-to-retirement income stream; ceasing an employment arrangement on or after the age of 60; being 65 years old even though they haven't retired; or having died.

If the common conditions of release aren't met, where a member meets eligibility requirements under certain special circumstances, they are able to have at least part of their super benefits released before reaching preservation age. These special circumstances include that the fund member:

- has terminated gainful employment;
- is temporarily or permanently incapacitated;
- is suffering severe financial hardship;
- meets conditions for compassionate grounds;
- has a terminal medical condition; or
- is taking part in the first home super saver scheme.

Trustees should note that each of the special circumstances has its own eligibility conditions; for example, in the case of severe financial hardship, the trustee must first be satisfied that the member cannot meet reasonable and immediate family living expenses, has been receiving relevant government income support payments for a continuous period of 26 weeks and was receiving that support at the time they applied to the trustees. Cashing restrictions also apply – in the example of severe financial hardship, the super payment must be a single gross lump sum of no more than \$10,000 and no less than \$1,000.

Another special condition of release which may be confusing for trustees is compassionate grounds. Not only do trustees have to be satisfied that the member qualifies under certain circumstances, prior ATO approval must be received by the trustee before any funds can be released. The amount of super that can be paid on compassionate grounds must be in the form of a lump sum and is limited to what is reasonably needed for the circumstances (eg medical treatment, palliative care, payment on home loan, council rates, accommodating disability, funeral expenses etc).

Besides targeting illegal early release, the ATO has reminded trustees of SMSFs that their fund must be audited every year by a suitably qualified auditor and an annual return must be lodged by the due date. This blitz on the SMSF compliance is set to continue all through until the end of the 2024 income year, with the ATO explicitly stating it will take "firm action" against trustees who persistently fail to comply with their obligations and seriously breach the superannuation laws.

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