Years 7-12

Your Tax Activity 1

INCOME AND INCOME TAX

Fact sheet

WHEN DO WE NEED TO PAY TAX AND WHEN DON'T WE?

INCOME TAX

Individuals may be liable (responsible by law) for a range of personal taxes. These taxes can be imposed on income that is earned, purchasing goods or services, selling assets that are liable for capital gains tax (CGT), and other transactions. You have a legal responsibility to know what taxes you are liable to pay. You can't say, "I didn't know I had to pay tax on it".

The Australian income tax system relies on taxpayers self-assessing, which means you are responsible for working out how much you need to declare and can claim on your tax return. You provide this information to the Australian Taxation Office (ATO), which then calculates how much income tax you must pay. Details of how income tax works are described in other topics in this module.

What is assessable income?

Assessable income is income on which tax must be paid. Some examples of assessable income are:

- wages and salaries, bonuses and commission received as employment income
- income support payments from the government such as age pensions, and family and youth allowances
- money received from property or investments, for example, rent earned from leasing property or other items
- interest from assets such as bank deposits or bonds
- dividends earned from ownership of shares in a company
- a capital gain on the sale of a CGT asset for more than you paid for it.

What is not assessable income?

Not all money received by an individual is considered to be assessable income. Examples of non-assessable income are:

- pocket money
- inheritances
- lottery or prize winnings.

Money received from a hobby is not considered as assessable income unless the individual intends to create a business from the hobby. For example, if you have a regular job and enjoy painting pictures as an unrelated hobby in your spare time, any income from the paintings you sell is not regarded as assessable income.

Share income

People who own shares in a company are known as shareholders. The company may share any profits with the owners or shareholders. These payments are termed dividends and are included in the assessable income earned by the shareholder. There are two types of dividends:

- franked dividends
- unfranked dividends.

Franked dividends are a share of a company's distribution paid by an Australian company on which company tax has already been paid. That is, the company paid tax on its taxable income at the rate of 30% before distributing dividends. Franked dividends can be fully or partly franked. As tax has already been paid on the dividend, you will be entitled to claim a credit for the tax associated with the dividend. This is called a franking credit and will reduce the amount of tax payable by you as the shareholder.

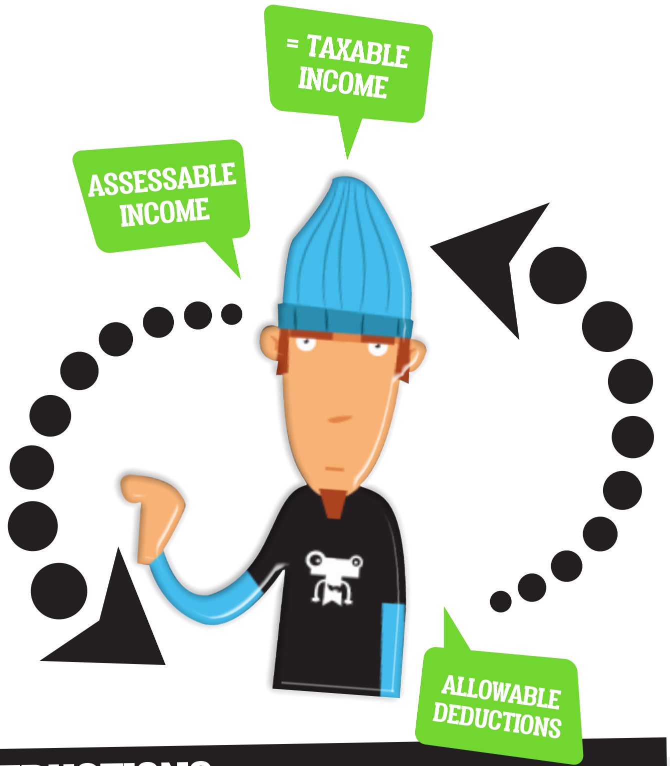
Unfranked dividends are a share of a company's distribution paid by an Australian company on which no company tax has been paid. This means there are no franking credits to offset any of the tax payable on the dividend.

Non-cash benefits

Sometimes an employer provides a benefit to an employee instead of paying them cash income. Typical examples are the private use of a motor car or payment of school fees. In a mining area, non-business accommodation may be provided to many employees.

Prior to 1986, these benefits were not included in taxable income and were not taxed under income tax laws. This was seen as unfair, so fringe benefits tax (FBT) was introduced. The employee does not pay FBT; the employer providing the benefit does. If an employee receives fringe benefits above $2,000, an amount of reportable fringe benefits will be recorded on their payment summary.

Some taxpayers receive income in the form of cash. This can range from the receipt of cash tips and gratuities to payment of wages as 'cash-in-hand', and includes bartering services in exchange for other goods and services. This income is part of assessable income, which is taxed.



TAXABLE INCOME AND ALLOWABLE DEDUCTIONS

Your taxable income is the total of your assessable income reduced by the amount of any allowable deductions. Allowable deductions are expenses incurred in gaining or producing assessable income or necessarily incurred in running a business for the purpose of producing your assessable income. Allowable deductions reduce the amount of income on which you have to pay tax.

TAX OFFSETS

Unlike allowable deductions, which reduce assessable income, tax offsets (sometimes referred to as rebates) directly reduce the amount of tax payable. Tax offsets include health insurance. There are offsets for those who live in certain zones, earn a low income or care for an invalid. The tax you have to pay is calculated on your taxable income and this amount is then reduced by the amount of any tax offsets you are entitled to. For example, if you pay premiums to a registered health insurer you may be entitled to a private health insurance offset (sometimes called a private health insurance rebate).

WHAT ARE YOUR RESPONSIBILITIES?

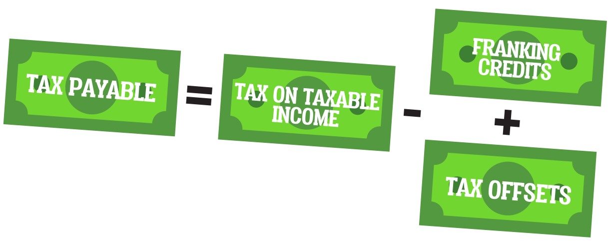
When you sign your tax return or lodge using myTax you are taking responsibility for the claims you are making. If you become aware that your tax return is incorrect, you must contact the ATO as soon as possible to correct the error.

Remember, even if someone else – including a registered tax agent – helps you to prepare your tax return, you are still legally responsible for the accuracy of the information.

DIFFERENCE BETWEEN MINIMISATION AND EVASION

Tax minimisation is when you legally arrange your tax affairs to reduce the amount of tax you pay.

Tax evasion is when you deliberately lie to the ATO to reduce your amount of tax payable. It causes a significant loss in tax revenue available to the government to spend on services like health, education and transport. Examples of tax evasion include not declaring assessable income, such as wages or tips, deliberately over-claiming expenses, avoiding GST, and not lodging a tax return to avoid paying tax. It is not tax avoidance if you get paid in cash. It becomes tax avoidance when you do not declare that cash income on your tax return.



Your Tax Activity 1: Income and income tax

Years 7-10

TASK 1 ASSESSABLE INCOME

Worksheet

YOU WILL:

- explore how income derives from different sources
- describe the difference between assessable and non-assessable income for tax purposes

YOU WILL NEED:

- *Fact sheet: Income and income tax*
- *Answer sheet: Task 1 – Assessable income*

TEST YOUR KNOWLEDGE

1. **Review** what you already know about income tax.
   - What is income?____
   - What is assessable income?____________________________________
2. **Read** *Fact sheet: Income and income tax.* Confirm whether your understanding of income and assessable income is correct.
3. **On your own,** read the scenarios below and mark whether you think the income is assessable or not. You may refer to the fact sheet.
4. Now **test your new knowledge:** In pairs or small groups, decide whether the source of income is considered to be an assessable income in each scenario. Be ready to present your decision and justify it to the whole class.

Source of income scenario	Solo	Together
	Is it assessable? Y/N	Justify your decision
Jane found a $50 note in the street.		
Molly works as an art teacher. She works part-time so her salary is less than that of a full- time teacher.		
Xavier was unemployed for five months and received the Newstart Allowance.		
Stacey has been left $20,000 in a will.		
Dave won $200 first prize in a footy tipping competition.		
Amelie earns wages from a part-time job in an office while she attends TAFE.		
Con works part-time as a waiter, and he earned $80 in tips on Friday night.		
Elly earned $100 interest on her bank account.		
Leonardo is an accountant who paints pictures in his spare time. He received a $150 prize from a picture he entered in the local art show.		
Tom earned $300,000 first prize in a poker tournament. He gave up his job as a baker to travel around to different tournaments and wins regularly.		
Lee earned $85 from the sale of carrots grown in his backyard veggie garden.		

Your Tax Activity 1: Income and income tax

Years 7-10

TASK 2 COMPREHENDING TAX TERMINOLOGY

Worksheet

YOU WILL:

- explain the terms you need to understand texts and issues that relate to income tax

YOU WILL NEED:

- *Fact sheet: Income and income tax*
- *Answer sheet: Task 2 – Comprehending tax terminology*

TEST YOUR UNDERSTANDING

1. With a partner, arrive at an **explanation** of the difference between these paired tax terms. Refer to the fact sheet to assist you but use your own words.
2. Be prepared to **present** your explanation to the class.

assessable income
non-assessable income

franked dividends
unfranked dividends

tax offsets (rebates)
tax deductions

tax evasion
tax minimisation