

YOUR KNOWLEDGE



This month we focus on key developments and practical guidance for business owners, property holders, and SMSF trustees navigating complex tax obligations. We begin with a deep dive into Director Penalty Notices (DPNs), highlighting the Tax Ombudsman's review in response to a 136% surge in notices and the personal risks directors face if company taxes go unpaid. Next, we clarify the ATO's updated position on capital gains tax for home-based businesses, emphasising when small business CGT concessions apply—and when they don't. We also examine the ATO's draft ruling on inherited homes, exploring how changes to main residence exemptions could affect family estates and estate planning strategies. Finally, we provide practical reminders for SMSF trustees on maintaining compliance, focusing on the sole purpose test and arm's length requirements for related-party arrangements.

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DPN Review: A Wake-Up Call for Business Owners on Personal Tax Risks

Running a successful business is hard work—and sometimes, despite best intentions, tax obligations slip. If the business is being operated through a company structure, then the ATO can potentially issue a Director Penalty Notice (DPN), holding company directors personally liable for unpaid taxes.

In 2024–25, DPNs skyrocketed by 136%, reaching over 84,000 notices, affecting directors of around 64,000 companies. The stakes are high, and now the Tax Ombudsman is reviewing how the ATO issues and manages these notices—a development all directors should take seriously.

So, what exactly is a DPN? Put simply, if your company fails to pay certain taxes—like PAYG withholding, GST, or Superannuation Guarantee Charge (SGC)—the ATO can target directors personally. There are two types:

- **Non-lockdown DPNs:** These apply if the company has lodged its activity statements or SGC statements but hasn't made the relevant payments. In this case directors have 21 days to take appropriate action, such as arranging for payment of the debt, appointing an administrator, or entering liquidation. Acting promptly may allow the penalty to be remitted.
- **Lockdown DPNs:** These apply if reporting deadlines are missed as well. In this scenario directors can't avoid personal liability by putting the company into administration or liquidation.

The intent is to protect government revenue and employee entitlements—but for directors, the impact can be severe.

Why the Ombudsman is Involved

The review, announced in December 2025 by Tax Ombudsman Ruth Owen, responds to a surge in complaints, with DPNs topping the list. It will examine:

- How effectively the ATO uses DPNs to recover debts (\$54.2 billion in collectable amounts by mid-2025)
- The fairness of selecting cases for enforcement
- How directors are notified and communicated with

- Treatment of vulnerable directors, including those coerced into roles or facing financial abuse

The review also aligns with broader government initiatives, including support for gender-based violence survivors and more empathetic engagement with business owners. While timelines are flexible due to resources, the review is part of the 2025–26 work plan, alongside assessments of ATO services for agents, First Nations engagement, and interest charge remissions.

Commercial Takeaways for Directors

DPNs are more than a compliance issue—they're a real commercial risk. Ignoring a notice can disrupt personal finances, damage credit ratings, and even trigger bankruptcy. At the same time, the Ombudsman review could improve transparency and fairness, giving directors a clearer understanding of options if financial stress arises.

Practical steps to protect yourself now:

- **Stay on top of obligations:** make sure the company lodges returns and pays liabilities on time.
- **Lodge statements even if payment isn't possible:** Failing to lodge activity statements just makes things worse.
- **Consider using ATO payment plans** if cash flow is tight but remember that this won't necessarily enable directors to escape personal liability if a DPN has been issued already.
- **Monitor company cash flow and tax health closely,** especially during economic dips.
- **Act fast if you receive a DPN:** Consult immediately your accountant or lawyer to explore options because strict deadlines might apply.
- **Consider director insurance or business structuring** to limit personal exposure—but compliance always comes first.

The Ombudsman's review is a timely reminder: tax is a key business risk, not just paperwork. Being informed, proactive, and prepared can protect both your business and your personal assets.

Navigating CGT on Your Home: New ATO Clarity for Home-Based Businesses

Running a business from home—whether as a sole trader, freelancer, or small operator—has many perks. But when it comes to selling your home and potentially saving on tax, recent guidance from the ATO serves as a reality check.

The ATO has provided its views on how home-based businesses interact with the small business capital gains tax (CGT) concessions, providing a warning on how the ATO approaches a long-standing area of confusion.

See: [Home-based business and CGT implications](#)
| [Australian Taxation Office](#)

The Key Issue: Active Asset Test

When an individual sells their main residence, they will often enjoy a full CGT exemption. However, if part of the home is used for business purposes, this can potentially impact on the scope of the exemption.

If a full exemption isn't available under the main residence rules then we typically look to other CGT concessions, including the CGT discount for

assets that have been held for more than 12 months or the small business CGT concessions.

The small business CGT concessions can potentially reduce or eliminate a capital gain made on sale of a property, but only if certain conditions are passed. One of the key conditions is that the property must pass an active asset test.

In very broad terms, to pass the active asset test you need to show that the property has been actively used in a business activity for at least 7.5 years across the ownership period or for at least half of the ownership period.

The ATO is clear: the active asset test applies to the entire property, not just the business portion. When you are applying the active asset test, an asset either passes this test or fails it. It is not really possible for an asset to partially pass the active asset test. The entire property is either an active asset or it is not.

Simply having a home office, workshop, or even being able to claim home occupancy expenses as a deduction does not necessarily make your home an active asset. Where business use is incidental to the home's primary residential purpose, the ATO's view is that the small business CGT concessions generally do not apply.

Rus v FCT

The view that the entire property must qualify as an active asset—and that incidental or minor business use (such as a home office or storage in a largely residential setting) is insufficient—draws support from case law, particularly the Administrative Appeals Tribunal (AAT) decision in *Rus and Commissioner of Taxation* [2018] AATA 1854 (*Rus v FCT*).

In that case, a taxpayer sought access to the small business CGT concessions on the sale of a 16-hectare largely vacant rural property, where only a small portion (less than 10% by area) was used for business purposes: a home office, shed for storing tools/equipment/vehicles, and

related supplies tied to a plastering and construction business operated through a controlled company. The balance of the land remained vacant or used residentially.

The AAT upheld the ATO's ruling that the property as a whole did not satisfy the active asset test, reasoning that the business activities were not sufficiently integral to the asset overall.

Minor or incidental use did not make the entire property an active asset, especially where the business was primarily conducted off-site. This precedent reinforces the ATO's strict approach in home-based business scenarios: the property is assessed holistically. This means that limited business use typically fails to tip the scales toward qualifying for the concessions.

Practical Examples

Let's take a look at how the ATO approaches some common scenarios.

Minor home-based business: Harriet runs a hairdressing salon in a spare room, using 7% of the total floor space of the property and seeing clients eight hours a week. She claims deductions for occupancy expenses and gets a 93% main residence exemption. However, because her business use is minor, she cannot access small business CGT concessions. The 50% CGT discount can still apply.

Significant business use: Sue and Rob own a two-storey building, with the ground floor operating as a takeaway store (50% of the total floor area of the property) and the top floor as their private residence. The business has been running for decades with employees. Here, the property qualifies as an active asset, potentially giving them access to the small business CGT concessions for the portion of the capital gain that isn't covered by the main residence exemption.

What This Means for You

- A partial main residence exemption doesn't necessarily mean you have

access to the small business CGT concessions. Many homeowners mistakenly assume that business deductions or a home office automatically open the door. The ATO clearly doesn't share this view.

- Seek advice before changing the way your home will be used. Starting to operate a business from home can impact on deductions, CGT calculations and access to CGT concessions.
- Keep thorough records. Floor plans, hours of business use, and detailed deductions can help strengthen your position and may help in any future planning or audits.
- Consult your accountant. If selling your home is on the horizon, professional advice is critical to assess any potential CGT exposure and explore concessions that might be available.

The Bottom Line

The ATO's updated guidance suggests that many home-based business owners won't have access to the small business CGT concessions on sale of their home, but this always depends on the facts. Business owners need to plan proactively, rather than assume that tax relief will be available.

By understanding how your home's business use is treated, you can make smarter decisions. For example, will the profits generated from a small business operated at home end up being wiped out by a higher CGT liability on sale of the property down the track?

After all, when it comes to CGT, every dollar you keep counts toward your next venture or your retirement nest egg.

ATO Update on Inherited Homes: What it Means for Your Family's Wealth

The ATO has issued a Draft Taxation Determination TD 2026/D1 which looks at how inherited family homes are treated for CGT purposes. Some industry commentators have dubbed it a “death tax by stealth”, but it is a bit more complex than this. The draft guidance focuses on a specific aspect of the rules around applying the main residence exemption to inherited properties, potentially exposing deceased estates and beneficiaries to significant tax if not planned correctly.

Here's what you need to know in practical terms.

Why TD 2026/D1 Matters

Under current law, deceased estates or beneficiaries can potentially sell a deceased individual's former family home without paying CGT if certain conditions can be met. This exemption is particularly valuable for properties owned long-term, where unrealised gains could be substantial.

In order to access a full exemption you normally need to ensure that the property is sold within 2 years of the date of death (but the ATO can potentially extend this deadline) or that the property has been the main residence of certain qualifying individuals from the date of death until the property is sold.

These qualifying individuals can include the surviving spouse of the deceased individual, the beneficiary selling an interest in the property or

someone who has a right to occupy the dwelling under the deceased's will.

The draft ATO guidance focuses on this last point. That is, what does it mean for someone to have “a right to occupy the dwelling under the deceased's will.” In summary, the ATO's view is that:

- The right to live in the home must be explicitly granted in the will to a named individual.
- Broad discretionary powers given to trustees, separate agreements, or even testamentary trusts (TTs) are not sufficient in the ATO's view.

For example:

- A will giving an executor discretion to allow a family member to occupy the home does not meet this requirement.
- A trustee of a TT who allows a beneficiary to live in the house is seen as separate from the will and may trigger CGT on sale.

Some legal and real estate experts warn this could force families to sell homes within two years of death to avoid CGT, especially in high-value areas.

Consider this: inheriting a \$2 million home with a capital gain of \$1.5 million could expose the beneficiaries to \$300,000–\$600,000 in tax, depending on discounts and tax brackets.

However, it is important to remember that there are still other ways for the sale of the property to qualify for a full exemption.

Practical Steps to Protect Your Estate

While we are waiting for the ATO to finalise its guidance in this area, there are steps you can take to protect your family's assets:

- Review and update your will, especially if you are planning to provide certain individuals with the right to occupy a property. Does the will currently

provide this right to specifically named beneficiaries?

- Plan the timing of sales – The two-year exemption window remains, but if you inherit a property and intend to hold it longer than this, weigh any potential CGT exposure against future rental income or family needs. Partial CGT exemptions might still apply, but the rules and calculations can be complex.
- Seek professional advice, especially if your estate plan uses TTs. You will normally need to work closely with tax and legal advisors to structure the plan appropriately.
- Be market aware – Estate planning can intersect with market timing. Quick sales may preserve CGT exemptions, but this needs to be weighed up against non-tax factors.

The key takeaway is clear: estate planning is a complex area and needs to be navigated carefully to preserve family wealth and avoid unintended tax implications.

Keeping Your Self-Managed Super Fund Compliant

Self managed superannuation funds (SMSFs) can offer significant flexibility, allowing the members to make investments and enter arrangements that may not be available through retail or industry superannuation funds. However, being an SMSF trustee does come with important responsibilities to ensure that all dealings comply with superannuation law.

Two critical areas to keep front of mind are:

- The sole purpose test, and
- The arm's length requirements in both superannuation and taxation law.

The Sole Purpose Test

The sole purpose test requires that superannuation funds should be managed for the sole purpose of providing retirement benefits to fund members. While some SMSFs may have dealings with or/investments in related entities, these are subject to strict limits and when arrangements are entered into it is important that first and foremost SMSF trustees are considering the retirement benefits of the fund members rather than the needs of any external parties.

The example below illustrates how SMSF trustees should apply the sole purpose test when looking at making a related party investment.

Example: Investing in a Related Business?

Sachin and Deepthi have an SMSF which has a total balance of \$1.2m. Their son Hardik commenced a business 3 years ago using a company structure. Hardik has approached his parents to invest \$50,000 into his company via their SMSF.

Although Hardik is passionate about the business it has not grown as he would like, and Sachin and Deepthi are aware that the business has had cashflow issues and profits are not at a point where the business is growing or generating a profit.

Although the proposed investment amount is within the 5% in-house asset limit would Sachin and Deepthi invest member funds in an unrelated business knowing the business was in this same situation? That is, would they be placing their son's interests ahead of the interests of the fund members?

Based on Sachin and Deepthi's knowledge of the business, if the SMSF was to go ahead and make

this investment they as trustees may have contravened the sole purpose test.

Arm's Length Requirements

In addition to the sole purpose test there are superannuation and taxation law requirements that SMSF trustees always deal on arm's length commercial terms. This is again particularly important when arrangements are with fund members and/or related parties.

Where arrangements are not at arm's length, SMSF trustees can be liable for superannuation law penalties and in some cases fund income may be taxed at a higher rate.

Some common examples and key issues are discussed below.

Example: An SMSF Owns a Commercial Property Which is Leased to a Related Party Business

The rent should be on commercial terms and this needs to be evidenced by a rental appraisal from a professional such as a real estate agent when a lease is entered into.

The lease agreement should:

- Be in writing;
- Clearly cover who is responsible for particular outgoings and maintenance; and
- Be prepared by a legal professional.

Example: A Member of the SMSF or a Related Party Completes Work on an SMSF Property

SMSF trustees should seek professional advice before commencing any work on SMSF properties where the work may be performed by a member or a related party.

All arrangements with related entities should be commercial, including:

- If a related building company is used, the SMSF must pay market rates (same

as the general public) and this should be supported by documentation to satisfy the fund auditor.

- If members (who are also trustees) perform work personally, strict rules apply to whether they can be paid for their services.
- All materials should be purchased directly by the SMSF, not by individual members.

Please contact us to discuss these rules further if you are considering entering into any transactions or projects involving SMSF-owned property and related parties.