TAX TIPS FOR SMALL BUSINESS

The ATO continues its focus on small business as part of its efforts to close the [$10 billion tax gap] indicated by the Commissioner earlier this year. The ATO has received additional funding through the Black Economy Taskforce and its enhanced enforcement covers lodgment, employee entitlements, mobile strike teams, tax system integrity and the use of data and technology. The new Tax Integrity Centre and whistleblower protections will allow the community to report suspected or known black economy, tax evasion and illegal phoenix activities to a Black Economy Hotline.

Small businesses need to ensure their bookkeeping and lodgments are correct and up-to-date. You should obtain professional tax advice, especially in areas where more complex tax issues arise. This includes structures, capital gains tax, personal services income, trust declarations and distributions, and private company loans.

PRE-1 JULY 2019 TO-DO LIST

- Make trust resolutions
- Document the streaming of trust capital gains and franked dividends
- Review private company loans
- Consider deferring certain income, and bringing forward certain deductible expenses
- Write-off bad debts
- Pay employee bonuses and employee superannuation entitlements

RECORD-KEEPING TIPS

- Record cash income and expenses
- Account for personal drawings
- Record goods for your own use
- Separate private expenses from business expenses
- Keep valid tax invoices for creditable acquisitions when registered for the goods and services tax (GST)
- Keep adequate stock records
- Keep adequate records to substantiate motor vehicle claims

BE UP-FRONT AND HONEST WITH YOUR AGENT AND THE ATO

Getting the basics right has never been more important – good record keeping, substantiation, correct account codes, properly accounting for private use and declaring all cash transactions are essential to assure yourself, your tax agent and the ATO that your tax affairs are in order.

The ATO is getting smarter with its data, and taxpayers are increasingly being contacted regarding their income and expense claims. With a focus on discrepancies in returns when compared against pre-fill data or business benchmarks, and increased resources to deal with the cash economy, the onus is on business owners to correctly report their income, claim their expenses and have the appropriate records.

Your tax agent is required to take reasonable care when preparing your return, which means they may ask you detailed questions about your cashflow, business performance, personal use of assets and records.

MAXIMISE DEPRECIATION DEDUCTIONS

A key feature for small business in the 2019-20 Federal Budget on 2 April 2019 was the announcement that a small business entity (SBE) may potentially qualify for an asset write-off one under one of three varying caps during the year ended 30 June 2019.

A medium sized business entity (MSBE) will also be able to claim the instant asset write-off in respect of a depreciating asset that is both first acquired for a cost of less than $30,000 on or after 7.30pm on 2 April 2019 which is used or installed ready for use by 30 June 2020.

The write-off amount will depend on the date the asset is first used or installed ready for use for a taxable purpose. For businesses registered for GST, the threshold is calculated on a GST-exclusive basis, but for businesses not registered for GST, the threshold is calculated on a GST-inclusive basis.

Entity type	**Data acquired**	**Time depreciating asset first used or installed ready for use for a taxable purpose**	**Asset cost threshold**
Small business entity	From 7.30pm 12 May 2015	1 July 2018 – 28 January 2019	$20,000
Small business entity	From 7.30pm 12 May 2015	29 January 2019 – 7.30pm 2 April 2019	$25,000
Small business entity	From 7.30pm 12 May 2015	7.30pm 2 April 2019 – 30 June 2020	$30,000

Where the cost of the asset is not available for the instant asset write-off deduction, it will be allocated to the general small business pool and depreciated at a rate of 15 per cent regardless of the date of acquisition during the 2019 year, provided the asset starts to be used or is installed ready for use during the year ended 30 June 2019.

For assets included in the pool at the start of the 2019 year, the opening pool balance will be depreciated at the rate of 30 per cent. Where a balancing adjustment occurs during the year, the asset’s termination value must be deducted from the pool.

However, where the closing balance of the SBE’s general small business pool is less than $30,000 as at 30 June 2019, the SBE will be entitled to a full deduction for the amount of the pool’s closing balance.

MAKE SURE YOU PAY THE CORRECT COMPANY TAX RATE AND APPLY THE CORRECT RATE FOR IMPUTAION

Most companies with an aggregated annual turnover of less than $50 million will pay tax at 27.5 per cent in 2018-19. However, some companies with a turnover below $50 million will continue to pay tax at 30 per cent, especially companies that earn nearly all their income from passive investments such as rental income or interest income.

To qualify for the lower tax rate in 2018-19:

- a company must have an aggregated turnover of less than $50 million, where aggregated turnover is the sum of the company's ordinary income and the ordinary income of any connected affiliate or entity
- no more than 80 per cent of their assessable income is base rate entity passive income (replacing the requirement to be carrying on a business).

The full company tax rate of 30 per cent applies to all companies that are not eligible for the lower company tax rate.

As a corollary to the base rate passive entity income rules in determining the tax rate of a company, there have also been changes to the dividend imputation rules that apply to the franking of dividends by a company.

The company tax rate for franking distributions needs to assume that the aggregated turnover, assessable income, and base rate entity passive income is the same as 2017-18.
Where the company did not exist in the previous year, its corporate tax rate for imputation purposes will be deemed to be at the lower corporate tax rate of 27.5 per cent for that initial year.

SMALL BUSINESS INCOME TAX OFFSET

You will be entitled to the small business income tax offset for the year ended 30 June 2019 if you carry on business and your aggregated turnover for the 2019 year is less than $5 million. The offset rate is 8 per cent of the income tax payable on the portion of an individual's taxable income that is their 'total net small business income'.

The ATO will work out the offset based on the net small business income earned as a sole trader and share of net small business income from a partnership or trust, as reported in the income tax return.

SMALL BUSINESS CGT CONCESSIONS

There are significant tax savings potentially available where an eligible active asset used in a business is sold for a profit and the taxpayer can satisfy either the $6 million maximum net asset value test immediately before the CGT event or the $2 million CGT small business entity test for the 2019 year.

Additional conditions must now be met when a taxpayer disposes of an active asset being a share in a company or an interest in a trust on or after 8 February 2018.

MAKE TRUST RESOLUTIONS BY 30 JUNE

As always, trustees of discretionary trusts are required to make and document resolutions on how trust income should be distributed to beneficiaries for the 2018-19 financial year by 30 June.

If a valid resolution is not executed by 30 June, any default beneficiaries under the deed will become presently entitled to trust income and subject to tax (even where they do not receive any cash distribution), or the trustee will be assessed at the highest marginal tax rate on any taxable income derived but not distributed by the trust.

A trustee must be able to show how an effective resolution was made through minutes, file notes or an exchange of correspondence documented before year end. However, the trust's accounts do not need to be prepared by 30 June.

As a corporate trustee may need time to notify its directors that a meeting must be convened to pass and record a resolution, such a notice should be sent out well before the 30 June deadline.

DOCUMENT THE STREAMING OF TRUST CAPITAL GAINS AND FRANKED DIVIDENDS TO BENEFICIARIES

Broadly, trustees of discretionary trusts can stream capital gains and franked dividends to different beneficiaries if the trust deed allows the trustee to make a beneficiary “specifically entitled” to those amounts. The trustee must document this resolution before 30 June and the beneficiary receives or is entitled to receive an amount equal to the net financial benefit of that gain or dividend.

CLAIM DEDUCTIONS FOR PROFESSIONAL ADVICE WHEN STARTING A BUSINESS

Professional expenses associated with starting a new business, such as legal and accounting fees, are deductible in the financial year those expenses are incurred rather than deductible over a five-year period as was the case previously.

CONSIDER TAX IMPACTS FROM ANY RESTRUCTURING

Small businesses can change the legal structure of their business without incurring any income tax liability when active assets are transferred by one entity to another.

This rollover applies to active assets that are CGT assets, trading stock, revenue assets and depreciating assets used, or held ready for use, in the course of carrying on a business.

REVIEW YOUR PRIVATE COMPANY LOANS

The income tax laws can potentially treat the following as an unfranked deemed dividend for a taxpayer unless an exemption applies:

- a payment or a loan by a private company to a shareholder or an associate (like a family member)
- the forgiveness of a shareholder’s or associate’s debt
- the use of a company asset by a shareholder or their associate
- the transfer of a company asset to a shareholder or their associate.

The most common exemption is to enter into a written loan agreement requiring minimum interest and principal repayments over a specified loan term, which may be seven or 25 years depending on whether or not the loan is secured.

There are various things a private company can do before its 2018-19 income tax return needs to be lodged to minimise the risk of a shareholder or an associate deriving a deemed dividend.

Depending on the circumstances, these strategies may include repaying a loan, declaring a dividend or entering a complying loan agreement before the return needs to be lodged.

PREVENT DEEMED DIVIDENDS IN RESPECT OF UNPAID TRUST DISTRIBUTIONS

An unpaid distribution owed by a trust to a related private company beneficiary that arises on or after 1 July 2016 will be treated as a loan by the company, if the trustee and the company are controlled by the same family group. In these circumstances, the associated trust may be taken to have derived a deemed dividend for the unpaid trust distribution in 2018-19.

However, a deemed dividend may be prevented if the unpaid distribution is paid out, or a complying loan agreement is entered into before the company's 2018-19 income tax return needs to be lodged.

Alternatively, a deemed dividend will not arise if the amount is held in an eligible sub-trust arrangement for the sole benefit of the private company, and other conditions are satisfied.

INCREASED ACCESS TO COMPANY LOSSES

The ‘same business test’ for losses has been supplemented with the ‘similar business test’ for losses made in income years starting on or after 1 July 2015. The new test will expand access to past year losses when companies enter into new transactions or business activities.

The similar business test allows a company (and certain trusts) to access losses following a change in ownership where its business, while not the same, is similar, having regard to a number of considerations.

The 'same business test' and the 'similar business test' will be collectively known as the 'business continuity test'.

WRITE-OFF BAD DEBTS

Businesses can only obtain income tax deductions for bad debts when various conditions are met.

A deduction will only be available if the debt still exists at the time it is written off. Thus, if the debt is forgiven or compromised before it is written off as bad in the accounts, no deduction will be available.

The debt must also be effectively unrecoverable and written off in the accounts as bad in the year the deduction is claimed. The bad debt must have been previously brought to account as assessable income or lent in the ordinary course of carrying on a money-lending business.

Certain additional requirements must be met where the creditor is either a company or trust.

CHECK IF THE PERSONAL SERVICES INCOME RULES APPLY

Personal services income (PSI) is income produced mainly from your personal skills or efforts as an individual. You can receive PSI even if you're not a sole trader. If you're producing PSI through a company, partnership or trust and the PSI rules apply, the income will be treated as your individual income for tax purposes.

If the PSI rules apply, they affect how you report your PSI to the ATO and the deductions you can claim.

PAYING EMPLOYEE BONUSES

If you pay staff bonuses and you want to bring expenses into the 2018-19 year, ensure they are quantified and documented in a properly authorised resolution – for example, board minutes – prior to year-end to enable a deduction to be incurred for employee bonuses where such amounts are not paid or credited until the subsequent year.

PAY ANY OUTSTANDING SUPERANNUATION ENTITLEMENTS

Ensure superannuation guarantee payments for employees are up-to-date, and report and rectify any missed payments to the ATO.

From 1 April 2019, there are new powers and offence penalties related to the payment of superannuation guarantee obligations.

Employers can also claim deductions for superannuation contributions made on behalf of their employees in the financial year they are made.

PREPARE FOR SINGLE TOUCH PAYROLL

Single touch payroll (STP) reporting has been extended to all employers from 1 July 2019. A number of options are available depending on the number of employees you have, whether they are closely held and whether you report via your tax or BAS agent.

Check with your payroll software provider to find out if your software is STP compliant.

If you don't currently use payroll software, please see us.

SEEK INDEPENDENT ADVICE ON INVESTMENT PRODUCTS PROMOTED AS BEING TAX EFFECTIVE

The end of the financial year often sees the promotion of investment products that may claim to be tax effective.

If you are considering such an investment, see us before making a decision.

ADDITIONAL TIPS FOR PRIMARY PRODUCERS

Farm management deposits

One of the best tax planning measures available to primary producers is effectively utilising the farm management deposits scheme (FMDs). They are an effective business and cash flow planning tool.

Primary producers can deposit up to $800,000 in a FMD account, they can have early access to their FMD account during times of drought, and they may be able to offset the interest costs on primary production business debt.

Income averaging

Tax averaging enables primary producers to even out their income and tax payable over a maximum of five years to allow for good and bad years. This ensures that farmers don't pay more tax over time than taxpayers on comparable but steady incomes.

Primary producers who opted out of income tax averaging for 2008-09 will be automatically reinstated in 2018-19 but can choose to withdraw from averaging and pay tax at ordinary rates for 10 years.

Other primary producer-specific tax specific concessions

Don't forget to consider:

- the uncapped immediate write-off for capital expenditure on water facilities and fencing assets
- the deduction for the full cost of a fodder storage asset if the expense was incurred or it was first used or installed ready for use on or after 19 August 2018
- the outright deduction for capital expenditure for landcare operations and carbon sink forests
- the accelerated write-off for horticultural plants and grapevines.