News Bulletin

Accountants & Business Advisors

APRIL 2016

IN THIS ISSUE:

TAX DEVELOPMENTS UPDATE

ATO data matching

In continuation of its data matching program intended to catch taxpayers that are not complying with their tax and other obligations in relation to their real property dealings, the ATO has flagged that it will acquire details of real property transactions for the period of 20 September 1985 to 30 June 2017 from various sources, including state revenue offices, rental bond authorities and land title offices.

The ATO expects to match over one million records from rental bond authorities and 30 million records from the revenue and land title offices with its records of 11.3 million individuals.

The ATO will use the intelligence to identify risks and trends in non-compliance, identify appropriate compliance activities and to promote voluntary compliance by publicising the outcomes of the data matching program.

IMPORTANTANCE OF COST CONTROL

In tough market conditions when sales are restrained and profit margins squeezed, business owners will inevitably look towards reducing their costs. It is therefore important to understand the impact of cost control on the profitability of the business.

It is important to understand that *depending on the profit margin* of the business, if the expenses increase, the sales will have to increase by significantly more to compensate.

For example, assuming that a business has a net profit of 15%, then if its expenses increased by 5%, this would reduce the profit margin from 15% to 10.75% (as illustrated in the table below).

As can be seen from the Table below, once expenses increase by 5.0% to (in this example) 89.25% of sales, and then to maintain the profit of $150, sales would need to increase to $1,395.

In effect, for this business to maintain its profit margin, it would need to increase its sales volume by a massive 39.5%!....not an easy task!

	$	%	$	%	$	%
Sales	1,000	100	1,000	100	1,395	100
Expenses	850	0.85	893	89.25	1,245	89.25
Net profit	150	0.15	108	10.75	150	10.75

While cost control is only one component of profit, in times of sluggish economic activity cost control should be a key focus for any business.

END OF FINANCIAL YEAR TAX PLANNING STRATEGIES

As the financial year draws to a close, it is time to start thinking about whether your year-end tax planning is in order.

A starting point in conducting year end tax planning is to prepare a preliminary assessment of your taxable income for the year to date, so that it can be seen whether or not there is a problem to fix.

The process of Tax Planning starts with the *preparation of interim profit figures for the business, and conducting a review of all income and expenses of the business and examining all legal avenues to minimise the tax otherwise payable.*

Below we provide an outline of some tax issues that should be considered before year-end.

However, it should be noted this is not intended to be a comprehensive document covering all taxation issues that may require consideration.

Business Income

Generally speaking, business activity income is typically brought to account on an accruals basis, while passive income and personal services income are typically brought to account on a cash basis.

A taxpayer will typically derive business income when an invoice has been raised, or where the taxpayer is legally entitled to the amount. All trade debtor amounts at year-end are generally included in the assessable income of a taxpayer deriving business income

Year-End Planning Considerations

- Determine whether you have brought income to account in the correct year. Some income is brought to account on a cash basis (eg interest), while other income is brought to account on an accruals basis (eg business income).
- Consider invoices to be issued in June 2016 and July 2016 and whether they are in the appropriate period.
- Consider whether it is possible to defer the recognition of accrued income to the next income year. Such income may, or may not, be derived for tax purposes depending on the legal entitlement to the amounts at the time.
- Determine whether income has been received or receivable in advance of goods or services being supplied or provided (ie unearned income amounts). Generally, if a contract or arrangement requires that the fee be paid in advance, the income may be derived in the income year in which the work is completed to which the fee relates. Such income should be credited to an unearned income account so that it is not included as normal income.

- Determine as to whether the amount is income or capital – income is generally fully taxable, whereas items of a capital nature are generally tax free or subject to the concessionally taxed Capital gains.

FBT CHANGES FOR WORK-RELATED DEVICES

From 1 April 2016, small businesses will not incur an FBT liability if they provide their employees with multiple work-related portable electronic devices even if they have similar functions.
These include devices that are primarily used for work, such as laptops, tablets, calculators, GPS navigation receivers and mobile phones

REDUCED TAX RATES FOR SBE's

As from 1 July 2015, income derived by a SBE Business can benefit from a reduction in tax rates:-

- for SBE companies, they can benefit from the 1.5% cut in the company tax rate.
- for individuals who derive income from an unincorporated business which is a SBE, a discount of 5% will apply on the income tax payable on the business income received from the unincorporated SBE (capped at $1,000 per individual).

Deductions

A taxpayer can only claim a general deduction for losses or outgoings that are incurred in that year, where the purpose is to earn assessable income or in carrying on a business of earning assessable income.

An expense is "incurred" if there is a presently existing liability for the payment, *even if the payment is not actually physically made.*

Year-End Planning Considerations

- All expenses and payments during the year should be reviewed to determine whether you may be able to claim a deduction for the expense.
- Review all liabilities that are pending but not paid to determine if they can be taken up as a tax deduction in the current year.
- Keep documentation so that you can prove that you have in fact incurred the expenses before year-end.
- Review your Debtors, If you have doubtful debts, you can possibly bring forward deductions if you are able to write those amounts off as bad debts for tax purposes before 30 June 2016
- Where you hold trading stock, you can choose to value trading stock at year-end at cost, market selling value, replacement value or obsolete stock value. This can have the effect of either bringing forward deductions or shifting the amounts to the following year

Prepayments

Where a taxpayer prepays expenditure, such expenditure is generally not deductible upfront (unless the amount is regarded as "excluded expenditure"). Instead, prepaid expenditure is apportioned over the shorter of the eligible service period or 10 years.

Where amounts are incurred by an individual or small business entity (SBE), such amounts may still be deductible upfront if the eligible service period is essentially less than 12 months or does not end later than 12 months after year-end.

Year-End Planning Considerations

Consider whether a prepayment of the next 12 months of expenses, such as interest before year end, will help to effectively reduce your taxable income for the current year.

Depreciation

A taxpayer can claim a deduction for the decline in value of an asset it holds if that asset is a depreciating asset that is installed ready for use or already used for any taxable purpose over the effective life of the asset

Special depreciation concessions apply to an entity that is considered a small business entity(SBE). Generally, this is defined as a business with aggregated turnover of less than $2 million.

Year-End Planning Considerations

- If an SBE, you can claim immediate tax deduction for depreciable assets (whether new or second-hand) costing less than $20,000 which are acquired and installed ready for use between 12 May 2015 and 30 June 2017.
- Prior year-long life pooled assets can be pooled and depreciated at a rate of 30%..
- Ensure that depreciation schedules are reviewed and consideration given to writing off obsolete and scrapped items by 30 June.
- Consider self-assessing the effective life of depreciating assets Note that taxpayers are able to use a 200% multiple of the straight line depreciation rate for assets by electing to use the diminishing value rate.
- Consider delaying disposal of items for a profit until after 30 June and bringing forward disposal of items for a loss to before 1 July

Bad Debt Deductions

A taxpayer can only claim a deduction for bad debts if the debts: (i) are written off as bad before year-end; and (ii) have previously been included in the taxpayer's assessable income

Service and Management Fees

Service Fees and Management Fees can be an effective way to split/divert income from high marginal tax rate taxpayers to low marginal tax taxpayers.

Car Log Book Reminder

From 1 July 2015 individuals are only able to use the cents per kilometre method or log book method for claiming car expense deductions.

Taxpayers wanting to use the log book method need to ensure that their car usage is recorded for a minimum continuous period of 12 weeks.

This means that if you are planning to use the log book method for the 2016 income year, you may want to consider starting a log book soon if you have not already done so.

However, such payments may be the subject of ATO scrutiny and may be deemed to be non-deductible if:-

- The fees may be considered excessive.
- The service entity has not performed the services independently of the taxpayer.
- The arrangements may make no commercial business *sense.*
- The services may not have been actually delivered.
- There is no documentation of a management or service agreement.
- The documents or arrangements are put in place after year-end.

Year-End Planning Considerations

Before year-end, taxpayers should review all inter-group service and management fees. They should ensure that appropriate arrangements and documentation are in place and that they are commercially justifiable

YEAR-END BUSINESS REVIEW

As well as conducting a Tax Planning Review of your business, now may also be an opportune time to critically review the financial performance and operational structure of your business.

The starting point of the review will be an examination your business Profit & Loss Statement and Balance Sheet. Some of the areas of enquiry in reviewing the performance of the business include:-

Profit & Loss Statement

Revenues

- Did you meet your budgets / targets as set out in your business plan?

- Was revenue concentrated to a small number of customers?
- Where did revenue come from? Did you lose any customers or revenue sources during the year?
- What opportunities are there for increased revenues during the next 12 months from new and existing clients?

Costs

Vigilance in managing revenue and particularly costs is key to ensuring profitability.

- Did gross profit meet the targets set by your business plan?
- Were there cost overruns during the year?
- Are you using your buying power to your maximum advantage?
- Are suppliers giving you the best value?
- Do you have any 'lazy' costs that can be eliminated?

Balance Sheet

A thorough analysis of the Balance Sheet is critical to understanding the revenue and cost drivers of your business.

Stock

- Review the valuation of and the turn rate of stock
- Are you carrying excessive or obsolete stock?

Debtors

- Review the quality, concentration and particularly the turn rate of your debtors
- Do you have appropriate terms of trade and retention of title in place?

Work in progress

- Are your inventory levels appropriate for your business?
- Can you source other suppliers to achieve cost savings and reliability of supply?
- Is your work in progress operating at acceptable levels of efficiency?
- How quickly can you adjust your output to take advantage of improved conditions and conversely a decline in conditions?
- Do you have adequate working capital?

Non Current Assets

- Is your plant and equipment up to date?
- Is your plant and equipment being used at its optimal efficiency?
- Do you have any assets that are surplus to requirements?

Current Liabilities

- Are you making the most of creditor terms available to you?
- Are you meeting both short term and long term banking covenant obligations?
- Do you know your immediate, short term and mid term borrowing requirements?
- Do you have adequate facilities in place to meet these needs?

Non Current Liabilities

- Can you manage your long term debt obligations and meet banking covenants?
- What plans do you have for reducing long term debt?
- Are you getting the best pricing possible from your bankers? Understanding the financial position of your business is critical to determining the level and mix of capital required.

The above points are not an exhaustive check list of the financial aspects of your business. They are however, often the key areas that are overlooked.

ARE YOU READY FOR SUPERSTREAM?

The requirement for employers to make super contributions on behalf of their employees by submitting payments electronically in a SuperStream compliant format (EFT or BPAY) becomes mandatory for small employers (19 or fewer employees) on 30 June, 2016.

With 30 June almost upon us, businesses need to be SuperStream ready. This will typically include:-

- Choosing a system. Options, include using payroll software, online payment system, or a clearing house, like the ATO's Small Business Superannuation Clearing House, and
- Collection of the necessary employee identification data and enter it into the system ready to pay contributions electronically..

Please do not hesitate to contact us if assistance is required.

Disclaimer:-
The News Bulletin is distributed by Kaias Phillips to provide information of general interest to their clients. The content of this newsletter does not constitute specific advice. Readers are encouraged to consult their tax adviser for advice on specific matters.