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TAX TIME

Tax tips for your small business

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It's that time of year when small businesses can benefit by considering strategies to minimise tax burden. In this second article of our three-part series for year-end tax tips we look at accelerating deductions and how small businesses can reduce their tax for 2017.

Clearly a modest budget ahead of an election year with virtually no spending cuts.

With the individual tax rate set to reduce by 2% for those in the top bracket, a tax deduction is worth a little bit more in 2017 than 2018. The mere deferral of a tax liability for one year can provide some welcome cash flow relief when it comes time to paying your tax. Indeed you never know what the future will bring, so a tax deduction taken in a year when you know tax will arise is like a mid-year gift.

Incur necessary expenses including prepayments

A business deduction does not necessarily need to be paid in order to be claimed. You often just need to have been issued an invoice. So for all those expenses (excluding inventory) you know you will need to outlay for, it may be better to order it this financial year. Suppliers who offer generous terms of settlement are ideal but even paying the cash before year-end can also be a good idea. Repairs and maintenance is a good example. Simply ensuring all invoices received have been accounted for is also something that can sometimes be neglected.

Small Businesses have the advantage of not having to spread out a deduction into a future year for prepayments where the service period is less than 12 months. Prepayments do not necessarily need to be "paid" however it is often necessary to trigger the deduction in the first place. Prepaying rent and interest are obvious big ticket items that can provide an early deduction.

Depreciable Assets

We raised the $20,000 Instant Asset Write-off in the last edition, which means depreciable assets are usually limited for small business for old and expensive assets. Even these assets can be added to a "pool" providing a

30% depreciation rate (15% in the first year). But for those who have not pooled, it can pay to have a look at your depreciable assets prior to year-end to determine if any assets are no longer being used. These can be written off and their remaining depreciable balance claimed as an immediate tax deduction if they have been “scrapped”.

Bad debts

To get a deduction for a bad debt in the current year it needs to be “written off” in the ledger, before year end. There also needs to have been reasonable attempts to recover the debt and an argument can be made that there is limited likelihood of the debt being recovered. It can pay to review your debtors list and identify defiant customers.

Pay super

While super for the final quarter is not payable until 28 July, it will not be deductible in the current year if not paid before year end. So you might as well pay it. Also be wary of paying after 28 July, you will not receive a deduction at all.

For both staff and owners, additional concessional contributions into super should be considered both to take advantage of the cap ($30k or $35k if 49 years of age or over in 2017 then reducing to $25k next year) and to reduce taxable income.

Bonuses

In order to claim a deduction for bonuses the amount needs to have been determined before year-end and documentation should exist to prove that the decision to pay it was made, usually by way of a minute or communication with the recipient.

Analyse inventory

The value of closing stock is usually added back to taxable income and therefore the lower the value the better. An exception is where the simplified trading stock regime is chosen which avoids the need to make an adjustment if the movement in value is reasonably estimated to be less than $5,000. Either way it can be beneficial to carry out a detailed stocktake. The value of trading stock is reduced where stock can be argued to be obsolete or damaged, so the nature of the stock and trading history for each item can be relevant in minimising taxable income.

Owner remuneration

Income of family members from a business depends on the ownership structure (e.g. sole trader, partnership, trust or company). Wages, dividends or profit share may, in certain circumstances, have different tax outcomes to the recipients. It is therefore worthwhile to ensure you are aware of what your personal tax position is likely to be and plan appropriately.

Where wages or other forms of income are being paid to other family members, it’s worthwhile considering if a minor under 18 years can commence a full-time occupation prior to 30 June as this can provide them with the lower adult tax rates.

Owners should also consider repayment of any “Division 7A” loans (these are borrowings from a company) prior to year-end. Repayment this year can avoid a dividend (and resultant personal tax) that is usually required under the relevant rules. And if you have a discretionary trust involved, distribution resolutions should be completed prior to year-end.

Income deferral

Income deferral could be as simple as delaying the issue of invoices, however it is often necessary to review customer contract terms to determine when income becomes assessable. The general rule is that income becomes assessable when it is “derived”, typically meaning non-refundable or a present debt exists.

Despite being derived, income may also be non-assessable if it is not “properly referrable” to an income year. In practice this usually means that where services have been paid for but are yet to be performed they can be considered non-assessable “unearned income”.
Such amounts should be accounted for in a separate balance sheet account, which can be made as an adjustment after year end but they need to be identified. This can include a proportion of a receipt where a service is only partially performed. So, if you receive 20% of a contract up front but will not start work on it until July, that amount will be excluded from this year’s taxable income.

Income from the sale of goods is generally not assessable until the goods are delivered.

Be careful however when dealing with an associate. Schemes designed to provide an immediate deduction to one party but defers income to another may result in the deduction being denied.

Certain businesses may want to consider if they can use a cash accounting method for determining income, this may be possible for micro-businesses providing services relating to professional skill and personal work that does not rely on capital items such as plant and machinery.

Other areas to consider

Many businesses have multiple entities with transactions occurring between them. End of year is a time when you should ensure the appropriate invoices and other paperwork has been prepared. It is good practice to get a handle on what taxable profits are being made in each entity to ensure you don’t end up with, for example, profits in one entity and losses in another.

In terms of non-business investments, any term deposits may want to be commenced in early July if on an annual maturity cycle. Any investments sitting in a loss may want to be sold before year-end if other capital gains exist. Avoid repurchasing the same asset as anti-avoidance provisions may apply. Similarly, the sale of investments with an underlying capital gain may want to be deferred until July so the tax payable is effectively delayed for a year. The same principals can apply to depreciable assets if you are not using a small business pool method.

Finally, if you are expecting a refund, get your affairs in order and lodge your returns early. Your accountant will also love you for it!

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