

2020 Tax Planning Strategies For SME Business Owners

With COVID-19 having an impact on most businesses, tax planning is more important than ever this year.

Below are some practical strategies that SME business owners should consider in the lead up to 30 June to reduce this year's tax liability.

SMALL BUSINESSES

The following two strategies apply only to small businesses that have an aggregated turnover of less than \$10 million:

1. Deduction for pre-paid expenses

A small business can claim an immediate deduction for certain prepaid business expenses where the payment covers a period of 12 months or less and that period ends before the end of the next income year. The most common expenses that you should consider prepaying by 30 June 2020 include lease payments, interest, rent, business travel, insurances and business subscriptions.

Note that your business must be obligated to make the prepayment under the relevant contractual agreement to get the immediate tax deduction this financial year - you cannot simply choose to prepay the expense.

2. Other tax concessions

A small business is also entitled to the following additional tax concessions:

- Simplified trading stock rules, giving small businesses the option to avoid an end of year stocktake if the value of their stock has changed by less than \$5,000 from the previous year; and
- The option to account for GST on a cash basis and pay GST instalments as calculated by the ATO.

Expansion of instant asset write-off

Under the Government's COVID-19 stimulus package, the instant asset write-off threshold was increased from \$30,000 per asset to \$150,000 per asset, and extended to businesses with an aggregated annual turnover of less than \$500 million.

This measure applies to all purchases made from 12 March 2020 to 30 June 2020.

This tax break is not an immediate cash hand-out, but rather is a deduction that reduces taxable profit. Therefore, taxable business will only obtain the cash flow benefit when they lodge the 2020 tax return although they can vary the June 2020 quarter PAYG tax instalment to obtain an immediate cash flow benefit.

Importantly to obtain an immediate tax deduction, the asset must be used or installed ready for use by 30 June 2020. This could be an issue for imported equipment and also in the domestic context where Australian suppliers are COVID-19 impacted or transport companies are flat out.

Business investment incentive

Where asset purchases are not eligible for an immediate write-off, an additional 50% of the asset cost will be deductible in the year of purchase - existing depreciation rules would continue to apply to the balance of the asset's cost.

Business with an aggregated annual turnover of less than \$500 million can access this investment incentive for new assets acquired from 12 March 2020 to 30 June 2021 – second hand assets are excluded.

Like the instant asset write-off, this tax break is not an immediate cash hand-out and therefore can only be claimed as a deduction through the tax system.

Scrap obsolete equipment

If obsolete plant and equipment is sitting on your depreciation schedule, it should be scrapped and written off by 30 June to generate an additional tax deduction.

If your business is classified as a small business and assets were allocated to a small business pool, you can continue to claim one deduction for the pool of assets - you cannot separately write-off individual assets in the pool.

Superannuation contributions

The maximum concessional superannuation contribution limit is \$25,000 for all individuals. Note that employer super guarantee contributions and salary sacrifice contributions are included in the cap.

Where a concessional contribution is made which exceeds these amounts, the excess is taxed at your marginal rate, less a 15% tax offset for the tax already paid by the super fund on the excess contribution.

If you are making a personal superannuation contribution, ensure you obtain the relevant documentation from your superannuation fund to substantiate claiming the deduction before lodging your 2020 tax return.

In order to obtain a deduction in the 2020 financial year, the contribution must be received by your superannuation fund by 30 June 2020 - refer points (ii) and (iii) below.

Other important superannuation issues in the lead up to 30 June include:

(i) Carry-forward concessional super contributions

From 1 July 2019, you can make 'carry-forward' concessional super contributions if you have a total superannuation balance of less than \$500,000 at 30 June 2019. The unused concessional contributions caps can be used on a rolling basis for five years upon which they will expire.

For example, if a person had \$20,000 in concessional contributions made on their behalf during the 2018-19 year, the \$5,000 balance carries forward to the 2019-20 year.

This means the person can make concessional contributions of up to \$30,000 this financial year without breaching the contributions cap if their super balance was less than \$500,000 at 30 June 2019.

(ii) Super contributions made by cheque or electronic funds transfer (EFT)

Care needs to be taken where last minute contributions are made by cheque or electronic fund transfer to ensure that the deduction can be claimed in the current financial year.

Where the super contribution is made by cheque and the fund receives it by 30 June 2020, the deduction is allowed in the current financial year so long as the trustee banks the cheque within 3 business days and the cheque is not subsequently dishonoured.

Where the contribution is by EFT, it is taken to be made when the amount is “credited” to the bank account of the fund and not when the transfer is made.

Unless the contribution is made between linked accounts of the contributor and the fund (held at the same bank), the deduction may be deferred to the next financial year where the funds are not credited to the super fund account by 30 June 2020.

(iii) Super contributions made to the government’s small business superannuation clearing house (SBSCH)

To ensure a deduction can be claimed for employee super guarantee contributions in the 2019-20 year, the ATO says that due to processing time delays, payments need to be accepted by the SBSCH by 23 June 2020.

Defer income & capital gains tax

- Businesses that return income on a cash basis are assessed on income as it is received. A simple end of year tax planning strategy is to delay “receipt” of the income until after 30 June 2020.
- Businesses that return income on a non-cash basis are generally assessed on income as it is derived or invoiced. Income may be deferred in some circumstances by delaying the “issuing of invoices” until after 30 June 2020.
- Realising a capital gain after 30 June 2020 will defer tax on the gain by 12 months and can also be an effective strategy to access the 50% general discount which requires the asset to be held for at least 12 months. The date of the contract is the realisation date for capital gains tax purposes. In some cases, the capital gain can be further reduced to Nil under the small business capital gains tax concessions.

Family trust distributions

For the 2020 year, minors (i.e. children under the age of 18 at 30 June) can receive investment income (including trust distributions) of up to \$416 without paying tax. Any income earned above this amount is taxed at penalty rates.

Income received by a family trust should be allocated amongst the various beneficiaries by 30 June each year and documented by way of resolution. It is preferable that the resolution is made by 30 June 2020 to avoid any later dispute with the ATO as to whether the income was properly allocated by this date.

The exact requirements for allocating trust income are set out in the trust deed, and as each trust deed is different, it is vital that trustees are aware of the terms applying to that particular trust.

Failure to follow the terms of the trust deed and to allocate the relevant income by 30 June may result in the trustee paying tax on income of the trust at the top marginal tax rate of 49% (including 2% Medicare levy).

Note also that special rules apply to the “streaming” of capital gains and franked dividends received by family trusts to particular beneficiaries, and if you wish to stream it is critical that there are sufficient “streaming” provisions in the family trust deed which allow the trustee to do so.

Write-off slow moving or obsolete stock

All businesses have the option of valuing trading stock on 30 June 2020 at the lower of actual cost, replacement cost, or market selling value. A different valuation method may be applied for each item of trading stock.

For example, where the market selling price of stock items at year-end is below the actual cost price, your business can generate a tax deduction by simply valuing the stock at market selling value for tax purposes.

Also, in situations where stock has become obsolete at year-end (e.g. fashion clothing), your business may elect to adopt a lower value than actual cost, replacement cost, or market selling value, provided the value adopted is reasonable.

Claim deductions for expenses not paid at year end

All businesses are entitled to an immediate deduction for certain expenses that have been “incurred” but not paid by 30 June 2020 including:

Salary and wages. A tax deduction can be claimed for the number of days that employees have worked up to 30 June 2020, but have not been paid until the new financial year.

Directors fees. A company can claim a tax deduction for directors fees if it is “definitely committed” to at 30 June 2020 and has passed an appropriate resolution to approve the payment. The director is not required to include the fees in their taxation return until the 2020-21 year when the amount is actually received.

Staff bonuses and commissions. A business can claim a tax deduction for staff bonuses and commissions that are owed and unpaid at 30 June 2020 where it is “definitely committed” to the expense.

Repairs and maintenance. A deduction can be claimed for repairs undertaken and billed by 30 June 2020 but not paid until the next income year.

Write-off bad debts

If your business accounts for income on a non-cash basis and has previously included the amount in assessable income, a deduction for a bad debt can be claimed in 2019-20 so long as the debt is declared bad by 30 June 2020.

Your business will need to show that it has made a genuine attempt to recover the debt by 30 June to prove that the debt is bad. It's preferable that this decision is made in writing (e.g. a company directors minute).

Your business can also claim back the GST paid on debts that have been written off as bad, or where not written off as bad, the debt has been outstanding for 12 months or more.

Personal services income rules

If you conduct a business through a trust or company structure that relies on your personal effort and skill to generate the income, there are different rules that apply to the diversion of some or all of that personal services income.

For example, if your company earns personal services income, the ATO can treat the income as having been earned by the individual rather than the entity that earns the income, unless certain tests can be satisfied. The personal service income regime also denies particular types of deductions which would otherwise be available to a business