YEAR-END TAX BULLETIN

JUNE 2019

2019 TAX HIGHLIGHTS

FEDERAL BUDGET ANNOUNCEMENTS

The Federal Treasurer handed down the 2019 Federal Budget on 2 April 2019. As the Budget was designed as a pre-election statement by the Government, there were few tax initiatives in the Budget.

The key announcements from the 2019 Federal Budget that may have an impact for year-end tax planning include:

Tax relief for individuals

The Government announced another round of tax relief for low and middle income earners. The changes for the immediate income tax years have passed Parliament and are reflected in the offsets detailed below.

Instant asset write off

There are a number of changes to the instant asset write off to both the maximum asset value that qualifies for the immediate write off and to the turnover threshold for qualifying taxpayers.

From 1 July 2018, taxpayers with a turnover less than $10 million can write off assets costing less than $20,000. From 29 January, 2019, taxpayers with a turnover less than $10 million can write off assets costing less than $25,000. From 2 April 2019 (7.30pm), taxpayers with a turnover less than $50 million can write off assets costing less than $30,000 (to 30 June 2020). These changes have been legislated.

INDIVIDUALS TAX RATES

2018-19 Individual tax rates		
	Threshold	Rate
1st rate	$0 - $18,200	0%
2nd rate	$18,201 - $37,000	19.0%
3rd rate	$37,001 - $90,000	32.5%
4th rate	$90,001 - $180,000	37.0%
5th rate	$180,001 +	45.0%

In addition, the Medicare levy is 2% of taxable income. Therefore, the top marginal tax rate for resident individuals will be 47% (including Medicare levy).

A new Low and Middle Income Tax Offset will also be available, providing a benefit of up to $255 for individuals earning under $37,000 and up to $1,080 for individuals earning between $48,000 and $90,000. The offset reduces by 3 cents for every dollar in excess of $90,000. There is no offset for taxpayers earning in excess of $126,000.

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SMALL BUSINESS

Small Business Company Tax Rate

From 1 July 2016, the income tax rate applicable to companies carrying on a business will reduce to 27.5%. The reduction will progressively apply to companies based on their aggregated turnover in the years in question.

The 27.5% tax rate will apply to companies as follows:

Year Ended 30 June	Turnover
2017	$10 million
2018	$25 million
2019	$50 million

To qualify for the reduced income tax rate, companies must satisfy the passive income test (derive no more than 80% of their income from passive sources, as defined in the legislation).

In addition to prescribing the income tax rate applicable to companies, the turnover and base rate entity passive income test is also relevant to determining the rate at which companies can frank their dividends for an income year. It is important to note that, under the legislation, a company may have an income tax rate that is different from their franking rate.

TAX PLANNING TIP

Companies need to monitor their income tax rates as these may change from year to year. In particular, where rates are changing across years, companies may seek to time the derivation of income and/or the incurring of deductible expenses to take advantage of the changing rates (subject to prepayment rules and general anti avoidance rules).

Trapped franking credits

From a franking perspective, a company's maximum franking rate is determined according to its corporate franking tax rate. For 30 June 2019, the company will have a 27.5% corporate franking tax rate where its turnover for 30 June 2018 is less than $50 million and it satisfies the base rate entity passive income test based on its 30 June 2018 income.

If the company pays a franked dividend based on profits of a previous year where the company's tax rate was higher than the franking rate for the current year, there may be trapped franking credits e.g. previous year rate 30% and current year franking rate 27.5% then 2.5% franking credits trapped in company.

TAX PLANNING TIP

Companies need to consider which franking rate they are subject to in the 30 June 2019 year, and which rate they will be subject to next year. Where the company may move from a 30% franking company in 2019 to a 27.5% franking company in 30 June 2020, there may be advantages in paying franked dividends prior to 30 June 2019 (subject to the position of the shareholders). You should consult your BDO adviser in relation to this issue.

Higher top-up tax

Shareholders in companies that pay 27.5% franked dividends will have to pay higher top-up tax because the franking offset they receive will be lower than if the dividend was franked at 30%. Generally, this means the company tax cut is clawed back by the government when dividends are paid to resident shareholders.

For example, a company has $100 profit and pays 30% tax, and pays the $70 balance as a franked dividend to the shareholder. If the shareholder's marginal tax rate in 47%, they will pay tax on the $70 franked dividend of $17 (after franking offset) leaving the shareholder with $53 after tax.

However, if the company pays tax at 27.5% tax on the $100 income it can pay a $72.5 franked divided franked at 27.5%, in which case the shareholder pays $19.50 on the $72.50 franked dividend leaving the shareholder with the same $53 after tax.

Super guarantee

The rate for superannuation contributions by employers on behalf of their employees under the SGC for the year ended 30 June 2019 is 9.5%.

Employers must make superannuation guarantee contributions for their employees on a quarterly basis within 28 days after the end of each quarter (September, December, March and June)

TAX PLANNING TIP

Tax deductions for the superannuation contributions will only be available in the 2019 tax year if the contribution is received by the superannuation fund by 30 June 2019.

Taxable payments reporting system

Businesses in building and construction are required to record payments to contractors and report these payments to the Tax Office. From 1 July, 2018, businesses engaged in the courier or cleaning industries were also required to make these reports. From 1 July 2019, the rules will extend to businesses engaged in IT, road (freight) transport, and security industries.

The annual report is due to be lodged by 21 July 2019.

Director penalties

Company directors need to pay attention to companies' PAYG and SGC liabilities as there are strict penalties for directors of companies that fail to make outstanding PAYG and SGC payments.

Loans from private companies - Division 7A

Shareholders of private companies and associates may be assessed on a deemed dividend if the company provides them with loans, payments, loan forgiveness or private use of company assets, unless the requirements of Division 7A are satisfied.

Make sure all Division 7A loans made in the 30 June 2018 tax year have been either repaid or put under a complying Division 7A loan agreement by the lodgement date of the company's 2018 tax return.

Make sure the minimum repayment amounts have been made by 30 June 2019 for complying Division 7A loans made in the 2018 and previous years.

TAX PLANNING TIP

To ensure all future Division 7A loans are covered by a qualifying loan agreement, consider entering into a Division 7A complying facility loan agreement that will be able to cover all future loans to shareholders and/or their associates.

The Government announced in the 2019 Budget that the amendments to Division 7A have been deferred to commence from 1 July 2020. The extent of the amendments has not been announced. You should discuss these issues with your BDO adviser once the amendments have been released.

TRUSTS

Unpaid trust distributions

Distributions made by trusts to associated private companies which remain unpaid at the end of the following year may be deemed to be a loan to the trust and become subject to Division 7A.

For the 2019 tax year, unpaid distributions to a private company that arose in the 2018 tax year may be a deemed dividend to the trust for the 2019 tax year unless the trustee:

- Has put the amount in a sub-trust for exclusive benefit of the private company by the earlier of the lodgement date or due date for lodgement of the trust's 2018 tax return (usually 15 May 2019)
- Converts the amount to a Division 7A complying loan by the earlier of the lodgement date or the due date for lodgement for the 2019 company tax return, or
- Pays the amount to the company by the earlier of the lodgement date or due date for lodgement for the company's 2019 tax return.

For unpaid distributions that have been placed into a sub-trust, the annual return on the sub-trust investment must be paid to the private company by 30 June 2019.

The taxation of unpaid present entitlements under Division 7A is subject to the current review of the provisions. As noted above, the new Division 7A is scheduled to commence from 1 July 2020, although the amendments have not yet been released. We recommend you discuss your options with your BDO adviser once the new Division 7A rules are released to ensure your UPE arrangements continue to satisfy Division 7A.

Reimbursement agreements

Trustees are also reminded of the application of Section 100A of the 1936 Act, especially where a trust has made a distribution of income to a private company.

Where the Tax Office determines that Section 100A applies to an arrangement, the net income that would otherwise have been distributed by the trustee is instead assessed to the trustee at the highest marginal rate.

Section 100A will not apply to ordinary commercial or family dealings.

In a recent publication, the Tax Office considered the following arrangement, referred to as the washing machine, would attract Section 100A:

- The trustee owns all the shares in a private company
- The company is also a beneficiary of the trust and undertakes no activity but derives a small amount of bank interest on its own account
- The directors of the private company and the trustee company are the same individuals or related individuals
- The trustee resolves to make the company presently entitled to some or all of the trust income in year 1 and distributes that to the company prior to the lodgement of the trust's tax return in year 2
- The company includes the distribution in its assessable income for year 1
- Division 7A does not apply to the arrangement because the company's entitlement is paid before the lodgement of the income tax return
- The company pays a fully franked dividend in year 2 to the trustee. This forms part of the trust's income in year 2
- The trustee makes the company presently entitled to all of some of the trust income at the end of year 2
- The arrangement is repeated.

The reimbursement agreement results in the distribution benefitting a party other than the beneficiary (it instead benefits the trustee). The reimbursement agreement provides for the payment of income from the trustee to the company on the understanding (implied from the repetition in each income year and their common control) that the company would pay a dividend to the trustee of a corresponding amount (less the tax paid).

The agreement is designed to achieve a reduction in tax that would otherwise be payable had the trustee simply accumulated the income.

This agreement is not an ordinary commercial dealing because the ownership structure and, particularly, the perpetual circulation of funds, serve no commercial purpose.

There are hybrids of this scheme which involve money flowing from the company via interposed entities, ultimately ending up back in the trust. These have also been identified by the Tax Office as possibly giving rise to a Section 100A determination.

Trust distributions and resolutions

Most discretionary trust deeds require distribution determinations for 30 June year end be made before 30 June, or earlier. Trustees must make these determinations prior to 30 June or the date in the deed if earlier than 30 June.

Trust streaming

Under the streaming provisions, trustees can stream franked dividends and capital gains to specific beneficiaries, rather than distributing these amounts as part of the general distribution to beneficiaries.

The deed must not prevent the trustee from streaming these amounts to specific beneficiaries. In addition, the beneficiaries who are to receive these amounts must be specifically entitled to them, and the trustee must record the streamed distributions in the accounts or records of the trust, by 30 June 2019 for franked dividends or by 31 August 2019 for capital gains (although the trust deed will usually require the trustee's distribution determination to be made by 30 June 2019).

TAX PLANNING TIP

You and/or your tax adviser should regularly review your trust's deed to ensure you and/or your tax adviser understands how it interacts with the various tax requirements, some of which are mentioned above.

TFN trust reporting

Trustees of resident discretionary trusts, family trusts and other closely held trusts are reminded they are required to report new beneficiaries' tax file number (TFN) and certain personal information to the Tax Office. For 30 June 2019 the TFN report of new beneficiaries must generally be made to the Tax Office by 21 July 2019.

If the beneficiary has not provided their TFN to the trustee, the trustee will have to withhold tax from the trust distribution where the beneficiary becomes presently entitled to trust income or is paid an amount of trust income.

TAX PLANNING TIP

To ensure you don't miss the reporting of beneficiaries TFN's we suggest you report to the ATO the TFN's of all likely beneficiaries of the trust now, even though they may not be receiving a distribution until a future year.

ONGOING YEAR END ISSUES

Small business entities

- The small business turnover threshold has increased from $2 million to $10 million. Benefits include simplified depreciation and trading stock rules
- Thresholds for the small business CGT concessions remains at $2 million turnover or $6 million net asset test.

Timing of income derivation

- Determine whether you should use cash or accruals tax accounting
- Consider deferring receipt until after 30 June 2019
- Alternatively, if you are in a tax loss, consider accelerating the receipt of income prior to 30 June 2019.

Income received in advance

- Income received in advance is not taxed until services are provided as long as income credited to unearned income account, and released to profit when the services are provided.

Timing of expenses

- Expenses are deductible if incurred by 30 June 2019
- Provisions are generally not deductible
- Some accruals are not deductible
- Some prepayments are not deductible until future years
- Interest paid after business ceases may continue to be deductible.

Repairs

- Deduct repairs and maintenance incurred before 30 June 2019, unless they relate to initial repairs, substantial replacement or improving an asset.

Gifts

- Donate to deductible charities before 30 June 2019 - check recipient endorsed deductible gift recipient
- Gifts not deductible if some benefit is received by donor except when given at an “eligible fundraising event” (special conditions apply).

Bad debts

- Review all debts before 30 June 2019
- Write-off bad debts before year end to get deduction in that year (provision for doubtful debts not deductible).

Trading stock

- Valuation - choose cost, market value or replacement
- Identify any obsolete stock – special valuation rule
- Scrap unwanted stock by 30 June
- Small business entity taxpayers do not undertake a stock valuation if the difference between opening and closing value is less than $5,000.

Prepayments/advanced expenditure

- Prepay deductible expenditure by 30 June 2019
- Prepayment rules operate to spread deduction over more than one year
- Prepayment rules do not apply to salary, amounts required to be paid by law or a court, or expenditure under $1,000
- Small business entity taxpayers and non-business individuals are allowed prepayments in year incurred if the benefit does not extend beyond 12 months.

Director and employee entitlements

- Conduct shareholders’ meeting before 30 June 2019 to approve directors’ fees to obtain deductions for 2019
- Ensure arrangements for employee bonuses based on 2018/2019 results are in place before 30 June 2019 to get deductions for the 2019 year.

Sale of investments and businesses

- Where CGT assets can be realised for a gain, delay sale until after 30 June, unless you have losses that may be lost because of company/trust loss rules
- Crystallise capital losses to offset gains, however, losses may be disallowed in the event of wash sale where loss asset or similar asset reacquired or continues to be controlled by the taxpayer.
- If CGT assets held for less than 12 months by individuals, trusts or super funds that are eligible for the CGT discount, consider delaying sale until 12 months has passed
- For small business entities with CGT assets less than $6 million or annual turnover less than $2 million, consider small business CGT concessions and restructure rollover relief.

- Ceasing business or business sold
- Consider consequences of payments for employee entitlements, transfer of employee entitlements to a new employer and redundancy payments
- Consider if small business concessions, rollovers, or super contributions are available
- Consider whether expenses incurred after business ceases may still be deductible.

Business related costs / project costs

- Project costs are deductible over the life of the project
- Other business related costs not otherwise deductible, not included in a CGT cost base nor capital allowance cost, may be deductible over five years
- It is essential the costs relate to a business that is, was, or will be carried on for a taxable purpose.

Depreciation

- Scrap obsolete items by 30 June 2019 to claim undepreciated cost
- Increase depreciation by reassessing effective life of assets if asset's effective life is less than ATO estimates of effective life
- For items that cost less than $1,000 consider a low value pool, with diminishing value rate of 37.5%
- Assets that are subject to the asset write off (subject to threshold and cost limits) can be immediately deducted. Refer to our earlier discussion regarding qualifying assets and taxpayers
- Other small business assets may be placed in the small business depreciation pool and depreciated at 15% in the first year and 30% in subsequent years
- If not a small business, some depreciable items of less than $100 may be immediately deductible, see PSLA 2003/8 ($300 if not in business).

Imputation

- If shares not held at risk for at least 45 full days, franking offset may not be available (except individuals whose franking offset less than $5,000)
- Trusts beneficiaries lose franking offset unless beneficiaries have vested and indefeasible interest in the shares held at risk for at least 45 days or family trust election made and trustee held shares at risk for at least 45 days
- Where company pays more than one dividend in franking period, ensure all dividends franked under benchmark rate (franking percentage of first dividend).

Year end tax effective investments

- Has promoter obtained product ruling
- Ensure promoter operated the scheme in accordance with product ruling
- Check if the investment is the subject of a Taxpayer Alert
- Consider Part IVA and other integrity measures
- Warning signs include contrived or artificial arrangement, limited or non-recourse funding; low cash outlay; in-built exit strategy; prepayments; arrangement not economically viable without tax benefit; arrangement not independently assessed for viability.

Home office expenses

- Portion of interest, rent and insurance are not deductible unless you are carrying on business from home and the area is separate and distinguished from private living areas
- Converting spare room not sufficient
- Power, heating and depreciation can be claimed at a flat rate established by ATO even if room is not exclusively set aside for a home office
- If an office is provided by the employer, working from home as a convenient place to do part of the work may not be sufficient to claim home office expenses
- Be aware that the ATO has identified this as an area of concern.

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