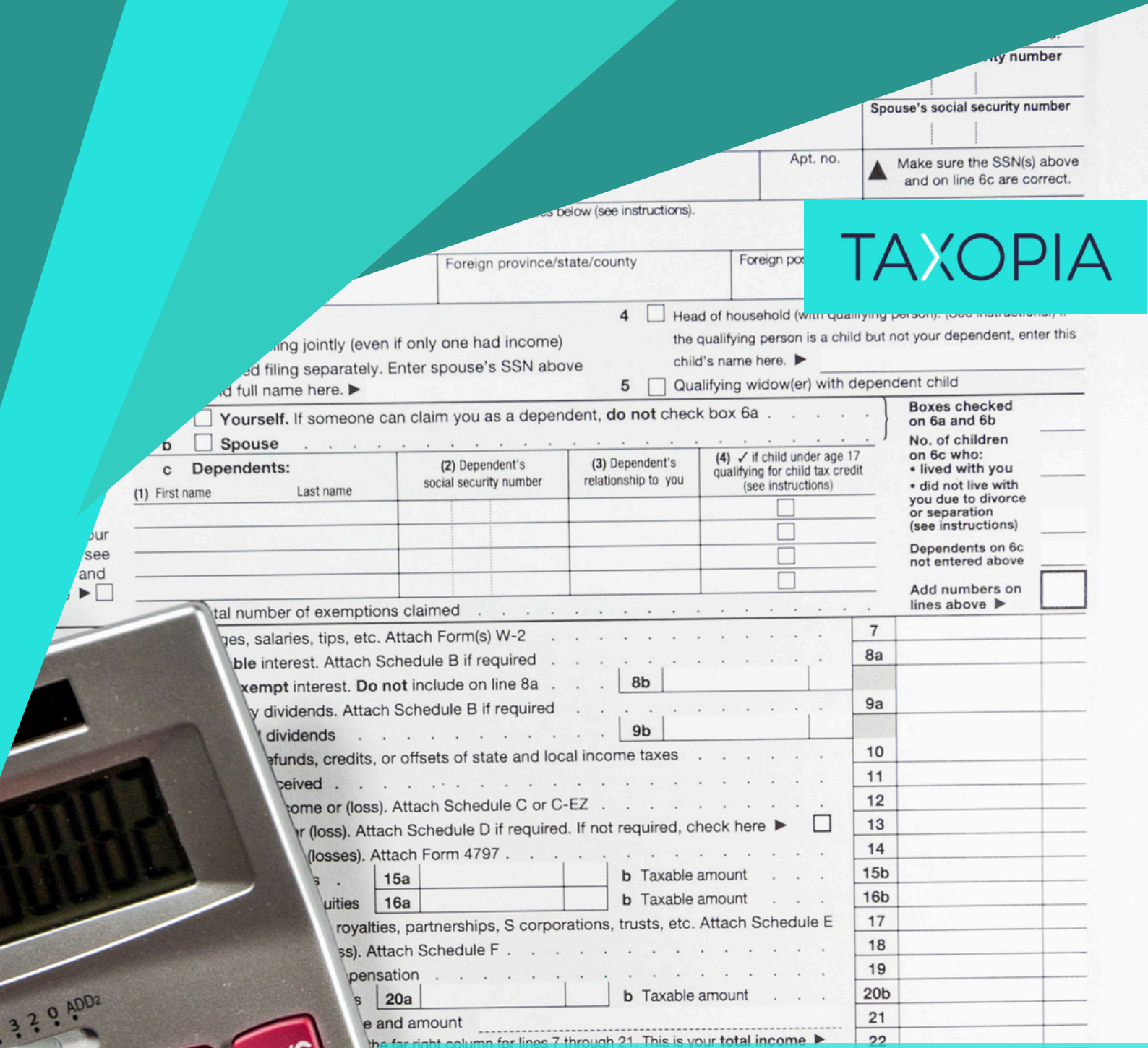


TAXOPIA

10 Smart Ways to Reduce Company Tax

A **TAXOPIA** GUIDANCE DOCUMENT

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We recommend that you seek independent advice from a qualified advisor before taking any action based on the information provided in this document.

INTRODUCTION



Paying tax means your business is earning money — and that is always a good thing. However, it makes sense to identify every viable way to reduce your tax bill so you can keep more of your revenue as profits.

At Taxopia, we bring together business and advisory experts with over 40 years of professional experience so we can offer a low-budget service to hundreds of clients. As we have built our reputation for delivering lofty standards of service and unrivalled value, the most common question we are asked is: How can I pay less tax?

This question arises because the system is complex and the rules and regulations for doing so are ever-changing, but the good news is that we can help make life easier in this area.

To get you started, this guide will walk you through the tried and trusted methods our senior accountants recommend to help business owners stay in control of finances and minimise tax.

Take a look at our list of 10 Smart, Easy Ways to Reduce Company Tax, then contact us for help with your annual tax return.



1 MAKE SURE YOU HAVE THE CORRECT TAX STRUCTURE

The experts at Taxopia often see companies, trusts and sole traders structuring their business in a way that does not align with their goals or allow for the best possible tax outcome.

Changing business structure can be complex and if done the wrong way it can trigger a capital gains event. This is why it is important to get professional advice.

When evaluating the business structure, consider:

- the profitability of the business
- the current tax position of all stakeholders
- the risk profile of the industry you operate in.

If you are thinking of starting a business, reach out to your tax agent. They can walk you through the risks and benefits of every option.

Here is a breakdown of the key business structures and their benefits:

Sole Trader
Sole traders are individuals who operate a business. When you are a sole trader, you can trade under your own name or with a registered business name. For tax purposes, the business's income is treated as part of the individual's personal income. This means any business income is taxed at the marginal tax rates for individuals.

Operating as a sole trader gives you:

- A simple business structure, as the individual owns the business.
- A low-cost option that is quick to establish
- Less paperwork and fewer governance requirements
- No legal separation between the business and the individual (this may cause difficulties once you begin to grow a team and have greater risk and liabilities)
- Ongoing control over the business operation and direction

A sole trader must register for GST if annual turnover is $75,000 or more.

Partnership

A partnership is a relationship between two or more people who carry on a business with a view to making a profit. Partnerships are governed by state government laws, and it is usual to have a formal overriding partnership agreement that outlines the way business is conducted.

When you form a partnership, you will need to have agreements around:

- Profit share arrangements.
- Arrangements of partnership salaries
- Admission of new partners
- Retirement of partners

A partnership, unlike a company, has no separate legal personality distinct from its members. Partnerships are:

- Two individuals or more carrying on a business together.
- Low cost and quick to set up.

Each partner is equally liable for the business's actions and the business is governed by the partnership agreement originally set out by each partner.

For taxation purposes, a partnership is treated as a separate entity. It must have its own tax file number and is required to lodge an annual income tax return to report its profit or loss. Each partner will then include their individual share of the partnership's net profit or loss in their individual tax returns.

Company

A company is a legal entity separate from its shareholders, who own the company. It is governed by corporations' law, which is administered by the Australian Securities and Investment Commission (ASIC).

Companies' operations are governed by their constitution. There are different forms of companies:

- Companies limited by shares – this is the most ordinary form of company.
- Companies limited by guarantee.
- No liability companies.
- Unlimited companies

For taxation purposes, a company's profits are taxed at the marginal tax rates, which are currently lower than the individual tax rates (more about this soon). As these change from time to time, it is best to refer to the ATO website for guidance on the exact rates. Companies have higher set-up costs and administration costs, but also provide some asset protection for their owners.

With that being said, directors of companies will sometimes be liable for their actions and the debts of the company. In order to direct a company in Australia, you need to apply for and secure a Director ID.

Trust

Setting up a trust can be costly, with a formal deed being required to outline how the trust will operate and yearly administrative tasks for the trustee. A trustee is legally responsible for the operation of the trust (the trustee can be an individual or a company). Profits from a trust go to the beneficiaries.

If you decide on a trust as your business structure, please note that it:

- Must have its own tax file number for lodging its annual tax return.
- Must apply for an ABN and use it for all business dealings.
- Must be registered for GST if annual turnover is $75,000 or more.
- May be liable to pay tax, depending on the wording of its deed and whether any income the trust earns is distributed to beneficiaries.
- May be able to access the small business tax concessions.
- Must pay super for any of its employees.

The income tax for a trust is determined by how the income is distributed. A trust must lodge an annual tax return the same way a business does.



When it comes to tax,

- If all trust income is distributed to adult resident beneficiaries, the trust is not liable to pay tax. This duty will fall on the beneficiaries, who must report the income on their income tax return.
- If all or part of the net trust income is distributed to non-residents or minors, the trustee is assessed on that share on behalf of the beneficiary. These beneficiaries may need to report their share of the trust's net income and claim a credit for the tax paid on behalf of the trust.
- Where the trust accumulates net trust income (does not distribute it), the trustee is assessed on that accumulated income at the highest individual tax rate.

If you have a trust structure and receive Personal Services Income, PSI rules will apply, and the net income will be treated as the trustee's individual income for tax purposes.

Not sure what will work for your business? The following will give you an overview:

(See Next Page...)

	Sole Trader	Partnership	Company	Trust
Cost	Low	Medium	Medium to high	High
Complexity of setting up	Simple	Moderate	Complex	Highly complex
Tax obligations	Low	Low	Medium	High
Legal obligations	Low	Low to medium	High	Medium
Owner	You	You and your partners	Company shareholders	Trustee
Responsibility for business decisions	You	You and your partner's share	The director(s)	Trustee
Responsibility for debts or losses	You	You and your partner's share	Generally, the company (although exceptions apply)	Trustee
Separate bank account needed	No	Yes	Yes	Yes
Extra administration and reporting	No	Yes	Yes	Yes

Before committing to a business structure, seek advice from a professional business advisor, tax agent, lawyer, or accountant. This will help you minimise tax and operate in a way that makes sense for your business model.

2 KEEP DETAILED RECORDS OF EXPENDITURE

“It’s tax deductible!”

You will hear this often when you are considering how to spend your business’s money.

The rule of thumb states that if you spend money to operate or grow your business, the expense is tax deductible. In other words, it reduces your business income and therefore you pay less tax because you earn less in profits.
Generally speaking, expenses that are tax deductible include:

-Vehicles and vehicles operating costs
-Rent for office or warehouse space.
-Purchase costs and depreciations costs of equipment such as computers, desks and chairs or machinery.
-Marketing costs
-Industry memberships and subscriptions
-Software subscriptions
-Electricity bills
-Using an accountant to help you prepare your tax return.

To claim tax deductions on your business tax return, you need records to substantiate your claim. Records are written or digital evidence of your income and expenses. While a shoebox full of receipts is one approach, these days the ATO and your accountant recommend you keep records electronically. This is because all the ATO systems are moving toward electronic reporting for tax and super obligations.

One of the easiest ways to keep track of spending is to create a business bank account and link it to a cloud-based platform such as Xero or MYOB. This way, you will have a record of every expense, when your business spent the money, who you paid it to and how much it was.

Some expenses can be claimed without records of purchase, but there is usually a cap on the amount you can include in your tax return. It is safest to be diligent, even when putting fuel in your company car, so your expenditure is noted in black and white.

Not all expenses are tax deductible but having detailed information about all the money your business spends will help your accountant to quickly prepare your tax return and ensure there is evidence to back up your claims.

3 INCOME SPLITTING – DISTRIBUTIONS

Income Splitting is a method of minimising tax that involves one spouse (the greater income earner) splitting their income to the lesser earning spouse.

Consider if you, as the Director of a company, draw a salary of $200,000, while your spouse earns no income because they are having time off to raise your children. As a household, you will pay more tax than if you both earned $100,000 because of the sliding tax scale in Australia. This situation is where income splitting can make sense as a strategy.

The most usual form of income splitting within Australia is through a trust, within the trust the income split is usually business or investment income, which the trust allocates.

Before you go down this road, it is worth noting that the ATO does watch out for individuals who employ this practice as an obvious form of tax avoidance. The ATO is generally concerned with arrangements where the compensation received by earners is artificially low. Collaborate with your accountant or tax agent to ensure your actions are legitimate.





4 USE INSTANT ASSET WRITE-OFFS, TEMPORARY FULL EXPENSING AND OTHER EXPENSE SPECIAL DEDUCTIONS RULES

Rules and regulations around tax deductions change in relation to expenses and assets but being aware of the following may help you reduce your tax bill:

INSTANT ASSET WRITE-OFFS

From time-to-time eligible businesses can claim an immediate deduction for the business portion of the cost of an asset in the year the asset is first used or installed ready for use. The rules in the space do change regularly and you need to seek specialised advice at the time.

TEMPORARY FULL EXPENSING

With temporary full expensing, your business can claim an immediate deduction for the business portion of the cost of an asset in the year it is first used or installed ready for use for a taxable purpose. You can also deduct the business portion of the costs of improvements made to assets.

Temporary full expensing was brought in to replace the instant asset write-off. Your eligibility and the amount you can claim depends on the specific rules at the time. The rules in the space do change regularly and you need to seek specialised advice at the time.

Your business can claim temporary full expensing on the cost of an eligible asset such as a vehicle, IT equipment, office equipment or tools. Primary production assets, capital works, horticultural plants and assets used for research and development purposes are not included.

A limit applies to passenger vehicles designed to carry a load of less than one tonne and fewer than nine passengers. This changes each year but is $64,741 for the 2022-2023 financial year. When you trade in a car or any other asset, the agreed price of your trade-in is usually deducted from the cost of your new asset.

Your eligibility for temporary full expensing can affect the purchasing decisions you make during the year. Work with your tax accountant to understand how this legislation may apply to your business.

SPECIAL DEDUCTION RULES

An example of another special deduction rule is the 120% tax deduction for skills training and technology costs.

If your small business has an aggregated annual turnover of less than $50 million, it will be able to deduct an additional 20 per cent of the cost incurred on business expenses and depreciating assets that support your digital adoption. This includes portable payment devices, cyber security systems or subscriptions to cloud-based services, to an annual cap of $100,000.

In addition to this, small businesses with an aggregated annual turnover of less than $50 million will be able to deduct an additional 20% of expenditure incurred on eligible training courses provided to employees until the end of the 2023-2024 financial year.

Other special deductions allow primary producers and irrigation water providers to immediately deduct the costs of water facilities. Speak to your tax accountant to find out more.



5

USE THE BASE COMPANY TAX RATE WHEN APPLICABLE

Companies are taxed at different rates, depending on their turnover.
Starting from the 2021–22 income year, companies that are classified as base rate entities in Australia can apply a 25% company tax rate. The rate was previously 27.5% from the 2017–18 to 2019–20 income years and 26% in the 2020–21 income year.

Your company is a base rate entity if:

- the aggregated turnover for that income year is less than the aggregated turnover threshold of $50 million for that income year, and
- 80% or less of your assessable income in that income year is base rate entity passive income.
-

The aggregated turnover threshold jumped from $25 million for the 2017–18 income year to $50 million from the 2018–19 income year. Being aware that your company may be eligible to pay 25% tax on income instead of the higher rate of 30% will help you to be more strategic about the way you earn money.

The passive income considered as part of this legislation includes:

- corporate distributions and franking credits on these distributions
- royalties and rent
- interest income (some exceptions apply)
- gains on qualifying securities
- net capital gain

If your business is earning money ‘passively’ due to revenue streams such as rent or net capital gains, check with your accountant to ensure it does not bump you up into the 30% tax bracket in a way that has a strong negative impact on your business’s overall profits.

6

MAXIMISE TAX-DEDUCTIBLE SUPERANNUATION CONTRIBUTIONS FOR DIRECTORS AND SHAREHOLDERS

1. Use Concessional Contributions:

- Concessional contributions include employer contributions (such as superannuation guarantee contributions) and personal contributions claimed as a tax deduction.

·Directors and shareholders can make personal concessional contributions to their superannuation fund and claim them as a tax deduction, subject to the annual concessional contributions cap.

2. Salary Sacrifice Contributions:

- Directors who receive a salary from their company can enter a salary sacrifice arrangement to make additional contributions to their superannuation fund before tax.
- Salary sacrifice contributions are generally taxed at a concessional rate of 15% within the superannuation fund, which may be lower than the individual's marginal tax rate.

3. Use the Bring-Forward Rule for Non-Concessional Contributions:

- Shareholders who have met certain eligibility criteria can utilize the bring-forward rule for non-concessional contributions, allowing them to contribute larger amounts to their superannuation fund within a three-year period.
- This strategy can be beneficial for those looking to make significant contributions to their superannuation fund and maximize tax benefits.

4. Consider Spouse Contributions:

- Directors and shareholders can consider making contributions to their spouse's superannuation fund, which may be eligible for a tax offset depending on the spouse's income.
- This strategy can help optimize tax benefits and superannuation savings for both individuals.

5. Review Contributions Caps and Limits:

- It is essential to be aware of the annual caps and limits for concessional and non-concessional contributions set by the Australian Taxation Office (ATO) and adjust contributions accordingly to avoid excess contributions tax.

6. Seek Professional Advice:

- Tax planning and superannuation strategies can be complex, so it is crucial for directors and shareholders to seek advice from qualified professionals, such as accountants or financial advisors, to tailor a strategy that aligns with their financial goals and circumstances.

By implementing these strategies and collaborating closely with professional advisors, directors and shareholders can maximize tax-deductible superannuation contributions and optimise their retirement savings while minimizing tax liabilities.

7

SMALL BUSINESS CAPITAL GAIN TAX CONCESSIONS

If your business makes money through the sale of active assets, the profits may be subject to Capital Gains Tax (CGT).
However, businesses that meet the eligibility requirements may be able to qualify for concessions/reductions to the full tax amount.

To be eligible for a CGT concession:

- your business must have an aggregated turnover of less than $2 million.
- you must not be carrying on a business (other than as a partner), but your asset is used in a connected small business (passively held assets)[1]
- a partner in a partnership that is a small business entity, and the asset is either:
  - an interest in a partnership asset (partnership assets)
  - an asset you own that is not an interest in a partnership asset (partner's assets) but is used in the business of the partnership.
- you must satisfy the maximum net asset value test.
- the asset must satisfy the active asset test.

If the asset is a share in a company or an interest in a trust, it must meet additional conditions.

CGT concessions may also apply to the disposal of an active asset if:

- the asset has been owned for more than 15 years.
- you are aged 55 years or older and retiring, or are permanently incapacitated.

If you decide to sell an asset, your tax accountant will also be able to help you figure out if you can contribute amounts to your super fund without affecting your non-concessional contributions limits.

There is also the small business rollover, which allows you to defer all, or part of a capital gain made from a CGT event happening to an active asset. Under this, you may decide to defer capital gain for twelve months when you buy a replacement asset or improve an existing active asset.

Applying CGT concessions

Being aware of CGT tax concessions and applying them correctly can have a significant impact on the money your business saves. Speak to your tax accountant about how these concessions are relevant to your business and how you can ensure you take advantage of them.



8 AVOID FRINGE BENEFITS TAX IN A GOOD WAY

Offering your employees fringe benefits such as vehicles, low-interest loans, contributing to your employee's rent or paying health insurance premiums is a way to attract and hold onto quality staff.

However, the tax on these incentives is paid by the employer rather than the employee and it is generally around 47 per cent, which can push up your business tax bill.

If you are strategic and know which steps to take, there are ways to minimise the Fringe Benefits Tax you pay.

- You may decide to purchase FBT-exempt vehicles for your team to use. As an example, if you provide private use of an electric car that meets the right criteria, your business will be exempt from paying FBT. The type of vehicles you provide your staff with and the way they are used come into play in relation to fringe benefits as well.
- Another option is to pay your staff additional salary/wages or provide an annual cash bonus instead of offering benefits which may be taxed.
- Be aware of the benefits that do not fall under the category of 'fringe benefits,' for example:
- Tools or electronic devices that are used for work.
- Items which cost less than $300 (e.g. if your Christmas party costs less than $300 per employee)
- You may also be able to avoid paying FBT if you give an employee a benefit that they would otherwise have been able to claim as an income tax deduction.

  For example, if you operate a warehouse and you send your staff to forklift training so they can be certified and boost their resumes. Even though your business covers the cost of the course, your staff could have paid and claimed the deduction. Because of this, you should be able to avoid paying FBT on this benefit.

- You can also reduce your business's fringe benefits tax by having your employees contribute to some of the costs; for example, you may offer $100 per month towards health insurance and have your employee make up the rest of the cost.

If you do offer a selection of benefits, a conversation with your tax accountant about how you can change things without your team feeling as though they are losing out can help you save at tax time.



9 NEGATIVE GEARING AND DEDUCTIBLE EXPENSES

Negative Gearing is the term used to describe a situation where expenses involved with paying for an asset are greater than the income earned from it.

If your business has purchased assets and it costs more to own them than they generate in revenue, you may be able to negative-gear the expense as a way of saving on tax. The trade-off of owning an asset that costs you money will hopefully be that it has risen in value when the time comes to sell it.

Negatively gearing an asset such as a property through your company may not be the best entity structure. Your tax accountant may recommend making the purchase through a trust instead. Speak to an expert to identify whether you can use this strategy to reduce your business's taxable income.

When it comes to deductible expenses, do not forget to share information with your accountant about your loans and repayments. You will likely find that the interest you pay can be tax deductible.

This does not apply to you as an individual; for example, the interest you pay on your home loan is not tax-deductible. Knowing this may help you prioritise your personal and business debt repayments.

The other expense to keep in mind is working from home. With so many businesses operating a 'hybrid' model these days and Directors having a home office, do not forget to speak with your accountant about what can and cannot be claimed.

Tax deductible home office expenses include:

- Electricity
- Insurance
- Gas
- Home internet and telephone
- Office furniture and IT equipment
- Rent

Mortgage interest may also be deductible but speak to your accountant about how claiming mortgage costs as part of working from home may influence CGT in the future (this is mostly applicable to sole traders).

There are so many areas such as negative gearing and working from home deductions which can be applied to reduce an overall company tax bill. When you collaborate with an accountant, they will ask all the right questions to ensure no dollar spent is ignored.

10

REPORTING YOUR TAXABLE INCOME ON CASH VS ACCRUAL METHODS

The method your company chooses to report taxable income can have a sizable impact on the result. As a small business, you do get to choose which method you adopt.

So, what is the difference between cash and accrual, and what impact does it have on taxable income?

- The cash method of reporting means income and expenses are only accessible and deductible when funds change hands.

  Generally speaking, a company is better off reporting on a cash basis where their accounts receivable (people who owe you money) are higher than your accounts payable (people you owe money to).

  For example, many trade services businesses often issue invoices to customers once work is completed and then wait 60 days (or even more) to be paid. Therefore, reporting income on a cash basis means the company will only pay tax on the income once the cash has been received.

- Under the accrual method income and expenses are assessable and deductible when incurred, for example, the date and invoices are issued.

  Your company will generally be better off reporting on an accrual method when accounts payable are higher than accounts receivable.

  For example, many retail businesses have very few accounts receivable (as customers pay before or as they receive their goods) but will often have accounts payable. Therefore, to receive a tax deduction for the accounts payable invoices as soon as possible, reporting on an accrual method is likely to be the best option.

Again, it all comes down to working with an accounting professional and knowing what is best for your business.



THANKS FOR READING

By making it to the end of this guide, you have given yourself a far deeper understanding of how to save on tax than most business owners.

What is challenging about the Australian tax system is that it changes regularly. Just when you think you understand how to minimise your tax, the rules are adjusted. This is why it makes sense to hand the task to a qualified and experienced tax accountant. If you are aware of what is possible in terms of tax deductions and able to share detailed records and receipts, your accountant can quickly guide you through your tax return and lodge it with the ATO on your behalf.

Do not forget past tax returns can be revised. If you feel you have missed out because of a rushed or unprofessional tax return, reach out to Taxopia today. One of our experienced tax agents can review your past returns and identify areas that could lead to a refund.

Want help to be fully prepared at tax time? Visit www.taxopia.com.au or call 1300 829 674 today.

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