Top 5 Tax Planning Strategies

For 2020-21

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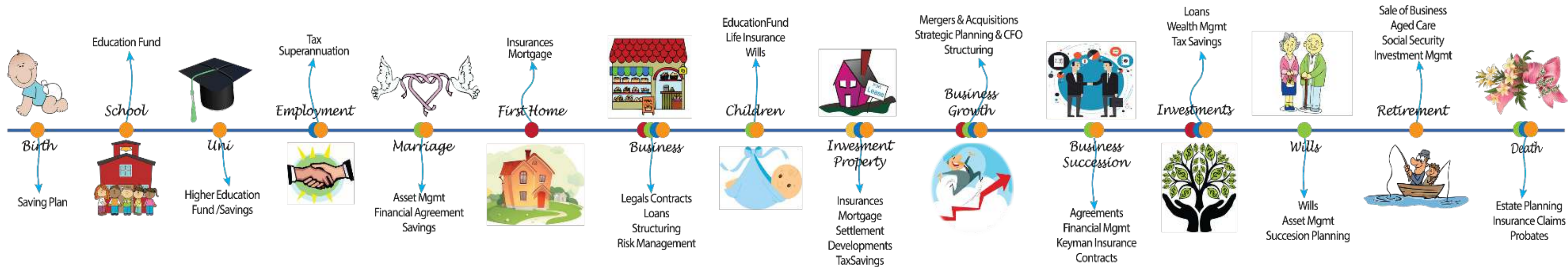

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Tax Planning

What is Tax Planning?

- Legitimate method to bring tax efficiency
- Through legal and morally acceptable strategies
- It is NOT Tax Avoidance or Tax Evasion. These are unlawful.

Why is it important?

- In Australia – Higher your Income; Higher Tax you pay
- But minimizing your income isn't something you want
- Leads to lower taxes; leaves more wealth in your hands
- A good strategy covers many aspects viz, investments, wealth/ cash flow maximization, retirement etc

Strategy 1

Instant asset write off; Temporary full expensing of depreciating assets; Accelerated depreciation

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Strategy 1

Instant Asset Write-off of $150,000

- Means you can claim an immediate deduction for the business portion of the cost of an asset up to $150,000 ex GST

- Instant asset write-off can be used for:
  - ✓ Multiple assets as long as cost of each individual asset is less than $150,000
  - ✓ New and second-hand assets
  - ✓ Certain assets are excluded such as
    - assets allocated to low value pool before using the simplified depreciation rules,
    - horticultural plants including grapevines,
    - software allocated to software development pool and
    - capital works deductions.

- Eligibility:
  - ✓ Asset must be purchased, first used or installed ready for use between 12th March 2020 and 30th June 2021, and purchased by 31 Dec 2020
  - ✓ Assets purchased prior to 12th March 2020 will still have write off threshold of $30,000
  - ✓ Aggregated turnover of up to $500 million

From 7.30pm AEDT on 6 October 2020 until 30 June 2023, temporary full expensing allows uncapped deduction

Strategy 1

Temporary Full Expensing

Eligible Businesses

- Entities with aggregated turnover less than $5b
- Aggregated turnover calculated same way as for small business entity concessions

Eligible Assets

- New or second hand (in case of second-hand asset, aggregated turnover to be below $50m)
- First held by you at or after 7.30 pm AEDT on 6 Oct 2020
- First used or installed ready for use by you for a taxable purpose (business purpose) between 7.30 pm AEDT on 6 Oct 2020 and 30 June 2022 (extended to 30 June 2023 in recent budget)

Exclusions

- assets allocated to a low-value pool or a software development pool
- certain primary production assets (water facilities, fencing, horticultural plants or fodder storage assets), unless you are a small business entity who chooses to use the simplified depreciation rules to these assets
- buildings and other capital works for which you can deduct amounts under Division 43
- assets that either
    - will never be located in Australia
    - will not be used principally in Australia for the principal purpose of carrying on a business.

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Strategy 1

Temporary Full Expensing

Improvements

- You can claim an immediate deduction for the business portion of the cost of improvements to existing assets
- Existing assets are assets that would be eligible assets except that you held them before 7.30 pm AEDT on 6 Oct 2020
- You cannot claim the acquisition cost of existing assets; however, you can claim an immediate deduction for the cost of improvements incurred between 7.30 pm AEDT on 6 Oct 2020 and 30 June 2023

If your business has an aggregated turnover of $50 million or more, you can immediately deduct the business portion of the cost of improvements to an asset that would otherwise be excluded because it is either:

- a second-hand asset
- an asset you entered into a commitment to hold, construct or use before 7.30pm AEDT on 6 October 2020.

Opting Out

- You can make a choice to opt-out of temporary full expensing for an income year on an asset-by-asset basis if you are not using the simplified depreciation rules.
- However, you must notify us in an approved form
- The choice is unchangeable, and you must notify us by the day you lodge your income tax return for the income year to which the choice relates

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LUXURY CAR LIMIT STILL APPLIES

E.g.

You buy a car for $100,000 (ex GST) before 6 Oct 2020. The delivery of the vehicle has been taken before 30th June 2021 and hence, the car is eligible for instant asset write-off

- Assume the car has been purchased in the name of a company or trust
- It is being used 100% for business use.
- Since the value of the car is above the luxury car limit, the deduction will be restricted to the luxury car limit.

Total deduction available in FY 2020-21 is as under:

Price of Car	: $100,000
Luxury Car limit	: $ 59,136
Total deduction	: $ 59,136
Balance	: $40,864 (depreciation not available on this amount)

- If there is a private use element of the car, FBT adjustment has to be done based on either statutory method or log book method
- Assume the car has been purchased as a sole trader and assume you have 40% private use, deduction available will be 60% of the luxury car limit of $59,136 which is $35,482

If the value of the car was above $150,000, it won't be eligible under instant asset w/off rules. However, if purchased after 6 Oct 2020, it will still be eligible under Temporary full expensing subject to same luxury car limit.

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Strategy 1

Backing Business investment - accelerated depreciation

- ✓ Used where cost of asset is more than $150,000
- ✓ Entity's aggregated turnover is up to $500 million for FY 2019-20 and 2020-21
- ✓ There is no limit on the number of eligible assets unless
  - Passenger vehicle designed to carry a load of less than one tonne or fewer than 9 passengers

- Eligibility:
  - ✓ Asset must be new and not previously held by another entity as trading stock
  - ✓ First used or installed ready for use on or after 12th March 2020 and 30th June 2021
  - ✓ Must not be an asset to which an entity had applied for instant asset write-off rules or temporary full expensing
  - ✓ Excludes:
    - Second-hand assets
    - Some specific Div 40 assets subject to low value and software development pools
    - Certain primary production assets
    - Building and other capital works (under Div 43)
    - Excess cost of car above the luxury car limit under any other depreciations rules

- Opting out – You can make a choice to opt-out on an asset-by-asset basis if you are not using the simplified depreciation rules

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Strategy 1

- What it means for Small business entities:
  - ✓ If you are a small business with an aggregated turnover of less than $10 million, and you use the simplified depreciation rules, those assets over the instant asset threshold which are eligible for the accelerated depreciation and not eligible for temporary full expensing, are added to the general small business pool.
  - ✓ You can deduct an amount equal to 57.5% (rather than 15%) of the business portion of a new depreciating asset in the year you add it to the pool. In later years the asset will be depreciated under the general small business pool rules.

E.g.

You buy a equipment for $200,000 (ex GST) before 30th June 2021. No instant asset write-off is applicable (However you may be eligible for full w/off under Temporary full expensing if purchased after 6 Oct 2020)

Total deduction available in FY 2020-21 is as under:

Accelerated Depreciation@ 50% : $100,000
General Pool Depreciation @ 15% on remaining balance : $ 15,000
Total deduction : $115,000

Balance c/f to next year as part of the pool : $85,000 (depreciated at 30%)

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Strategy 1

SUMMARY TABLE

Date of Acquisition	Amount	Eligible under
From 1 July 2020 to 7.30 pm on 6 Oct 2020	Up to $150,000 ex GST	Instant Asset w/off
From 1 July 2020 to 7.30 pm on 6 Oct 2020	More than $150,000 ex GST	Accelerated Depreciation
After 7.30 pm on 6 Oct 2020 to 30 June 2021	No limit on amount	Temporary full expensing

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Strategy 2

Contribution into your Superannuation Fund

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Strategy 2

- Concessional Contribution is before tax contributions ; non-concessional contribution is from after-tax income

- Concessional contributions include
  - ✓ compulsory employer contributions
  - ✓ any additional concessional contributions your employer makes
  - ✓ salary sacrifice payments made to your super fund
  - ✓ Direct voluntary contributions paid by you to the superfund

- For taxpayers wishing to claim deductions for concessional superannuation contributions, ensure that the payment is made (and received by the fund) by 30th June 2021.

- Concessional contributions are capped at $25,000 per taxpayer (increased to $27,500 for 2021-22). Going over means paying more tax.

- Therefore, consider deferring any contribution above the cap (unless you use Contribution Reserving Strategy)

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Strategy 2

- You don't need to salary sacrifice to top up your concessional contribution if you are in employment. You can make a lump sum contribution before 30th June to claim the tax deduction. This is helpful in situations where you have a certain capital gain on sale of asset before the financial year ending and you could not plan the salary sacrifice in advance
- Ensure super contributions for employees are paid and cleared by 30th June 2020. Late payment can not be claimed for deduction
- Contributions made to Superfund are taxed in Superfund at 15%
- If company is in profit, making a concessional contribution to associated persons will mean saving of tax at 27.5% for the company and paying only 15% in the Superfund giving a Net benefit of 12.5%
- Consider your individual marginal tax rate when you decide about making concessional contribution; the higher the marginal tax rate – the tax outcome is better

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Strategy 2

- If your super balance is less than $500,000 and you've made concessional contributions of less than $25,000, you can make additional concessional contributions in subsequent financial years for any unused amounts. Unused cap amounts can be carried forward for up to five years. The 2019/20 fiscal year is the first year you can use any remaining cap amounts.

- If you earn less than $54,837 p.a., you could be eligible for the government co-contribution. Means that the government will contribute 50% of after-tax contributions you make up to a maximum of $500.

- The full benefit is available for income earners under $38,564 and phases out where adjusted taxable income is between $39,837 and $54,837.

Strategy 3

Prepay your Expenses and Move Incomes between Financial Years legitimately

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Strategy 3

- It is legal to claim a tax deduction on interest expense as much as 1 year ahead provided it is paid for before 30th June 2021

- A common strategy that people use toward the end of the financial year is to pre-pay interest to a lender. Most lenders that allow you to pre-pay interest also give a discount on the interest for doing so, so not only do you save tax, you also pay less interest. Be mindful of giving enough notice to the bank before year end to achieve this. You will not be allowed to pre-pay interest on your fixed rate loans

- This results in bringing forward tax deductions that would otherwise be incurred in the next financial year (but since the dividends/ other investment income hasn't been received they won't add to assessable income until next year).

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Strategy 3

- The pre-payment rules could also be used to pay other business expenses like rent, insurances etc. To do so, however, you may need to have available cashflow. Certain prepayments are excluded like wages

- In case you have losses, there is no benefit in applying this strategy in FY 2020-21 as cash boosts given by the Australian Tax Office will absorb the losses

- Subject to cash flow considerations and anti-avoidance rules, consider deferring income to the following year, particularly if:
  - ✓ income for that year is likely to be lower; or
  - ✓ tax rates for that year are expected to be lower

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Strategy 3

- If you have issued an invoice just to receive an advance/ deposit from a customer but goods/ services have not been delivered, this should not be considered as part of Sales Revenue; rather coded to Liabilities as Unearned Revenue in the Balance Sheet
- This could also be true for assets trading at a capital gain. If you are working now but will likely not be working in a few years, then you may defer the sale of any such an assets until the later years
- Try to time the sale of assets like property/ shares in a way that you can net off the losses of one against the gains from another. So you are better off selling the asset with a loss first if you can't time the sale of both within the same financial year

Strategy 4

Bad Debts and Trading Stock

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Strategy 4

- Consider whether a change of stock valuation method is appropriate. For example, changing from cost to market valuation method at the end of the financial year may be beneficial depending on the profit of the business

- Trading stock in transit at year's end may have to be taken into account in calculating the value of stock on hand at the end of the year. For example, if you have purchased stock and made a payment but have not received a delivery, you need to either exclude that from your cost of sales if you are not considering that as part of the closing stock.

- For obsolete stock, or in other special circumstances, consider whether to adopt a special lower valuation or write off

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Strategy 4

- Take a close look at your Accounts Receivable list, identify the potential bad debts and write them off during the year. This will reduce your taxable profit

- In the event that you recover the money from your debtor in subsequent years, it can be added to the taxable income of that year

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Strategy 5

Optimise Tax Rate while operating under different structures – Companies, Trusts & Partnerships

Strategy 5

How to optimise the tax rate

Scenario 1: If you are operating as a Company

- Make sure you evaluate the amount of wages or dividends to be paid to the owners keeping in mind the individual marginal tax rates
- If payment of higher wages and dividends pushes the individual to a higher marginal tax rate, you may consider retaining the extra profits within the company to be taxed at 26% (or 30% in case of investment companies / non small business entity)
- If you need to draw more cash than the allocated wages/ dividends, consider taking temporary director/ share holder's loan

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Strategy 5

Scenario 2: If you are operating as a Trust

- Consider all adult beneficiaries in the family to whom the profits can be distributed for tax purposes. This could include adult children with no / low other income.
- Since you cannot retain taxable profits in a trust (as the trustee will have to pay maximum marginal tax rate), you have to distribute all the taxable profits by 30th June 2021 (it does not mean you have to actually distribute the cash)
- If you have optimised all the adult beneficiaries in your profit distribution, you may consider distributing the profits to a company under your control. The company will only pay 26% (or 30% where applicable) which may still give a better outcome than the individual paying taxes at a higher marginal tax rate

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Strategy 5

Scenario 3: If you are operating as a Partnership

- There is a very limited options of optimising the profit distribution in a partnership as generally the share of the partners are already defined unless operating as a family partnership

- If you are operating as a family partnership (like husband and wife business), you can always provide one of the partners a salary to change the allocation of over all profits amongst the partners. This will be useful if one of the partners is earning income from elsewhere such as a salary/ dividends etc

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General Updates

Marginal income brackets

The 2021 upper limit of some marginal income brackets for individuals have increased, with:

- The 19% tax band increasing from $37,000 in 2020 to $45,000; and
- The 32.5% tax band increasing from $90,000 in 2020 to $120,000

Loss carry-back measures

2021 is the first year the new loss carry-back measures can be used to provide a refund to companies when they lodge their 2021 tax returns.

Companies with an aggregated turnover of less than $5 billion can choose to carry back their:

- 2020 tax losses and offset it against their 2019 income tax liability; or
- 2021 tax losses and offset it against their 2019 and 2020 income tax liability, noting the amount of refund/offset is limited to the lesser of the amount of tax paid previously or the surplus in the franking account at 30 June 2021.

If no choice is made to use the loss carry-back measures, the loss is carried forward and can be offset against future profits provided either the continuity of ownership or similar business tests are met.

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General Updates

Immediate tax deduction for start-up expenses

2021 is the first year that medium sized businesses with an aggregated turnover of $10-50 million will be able to claim an immediate tax deduction for:

- Start-up expenses such as legal or accounting advice to set up a new business.
- Prepaid expenditure on a service that will be provided within 12 months.

Previously, these concessions were only available for small business entities with an aggregated turnover of less than $10 million.

From the 2022 income tax year, medium sized businesses will also qualify for:

- Simplified trading stock rules (i.e. they may sometimes not be required to do a stock-take at the end of the year) and quarterly calculations of PAYG instalments by the ATO;
- A simplified accounting method for GST purposes;
- A possible two-year amendment period for income tax returns; and
- The ability to settle excise duty and excise equivalent customs duty on eligible goods monthly.

Superannuation

From 2022, the superannuation general transfer balance cap will increase from $1.6 million for 2021 to $1.7 million. The non-concessional contributions cap will increase from $100,000 for 2021 to $110,000 and the concessional contributions cap will increase from $25,000 for 2021 to $27,500.

Reach out to us…

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