

# TAXCONCEPTS

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## The difficulty with fighting inflation



On the 7<sup>th</sup> of November the RBA raised interest rates again. This is tough on many Australians, but taming inflation is a major challenge facing the post-pandemic world. After governments spent freely to offset the economic fallout of the Covid-19 pandemic, prices began to climb at the fastest pace in decades, and central banks embarked on the most aggressive and synchronized monetary policy tightening in 40 years.

While inflation has eased since its peak in December 2022, the fight continues because the target RBA inflation rate is 2-3% per annum, and there is the problem. Inflation was 5.6% for September, which, unfortunately, was a slight increase on previous months.

Click [here](#) to see important statistics on inflation. Also, note the chart at the top of this link where it shows inflation was over 5.8% from 1973 to 1984, peaking at 17.7%, now that's high. Variable Interest rates on mortgages reached 17% in 1989.

# What is the right structure for your business?



Choosing the right structure for your business will significantly affect its legal and operational risk, asset protection, tax obligations, legal costs and clientele. There are four common business structures to choose from:

- sole trader;
- partnership;
- company; or
- trust.

You can change structures to accommodate your business's growth, but changing legal structures can often be very complex. Therefore, it is essential to think carefully when choosing the right structure for your business to ensure it best reflects your future goals.

## Types of Different Business Structures

### Sole Trader

Sole Trader is the simplest of the available business structures. As a sole trader, you manage and operate the business under your name. Such a structure is cheap and easy to set up. However, it is not very flexible and will not accommodate a growing business. The sole trader structure is most suitable for contractors, tradies, entertainers, home businesses, online stores, websites and most small businesses. The majority of small business owners in Australia are sole traders.

### Partnership

A partnership is an association of two or more people who carry on business as a partnership. Setting up a partnership structure is simple and relatively cost-effective. However, there are several disadvantages to the structure. Like a sole trader structure, partners are jointly responsible for the debts of the business. Therefore, it is crucial to consider who you enter into a partnership with, as all partners are equally liable for the other partners' actions. A partnership should have a partnership agreement in place, which sets out how the partnership operates.



## Company

A company structure is ideal when you are looking to grow and scale your business. A company is its own legal entity. Therefore, individual shareholders are only liable for debts or liabilities that the company incurs up to the amount unpaid on their shares (which is commonly zero). This limited liability makes the company structure suitable for high-risk businesses. The ability to raise capital and grow via the issue of shares makes the company structure the most suitable for startup businesses. The Corporations Act regulates companies who must abide by their statutory obligations and Constitution or Replaceable Rules. If your company has more than one shareholder, you should have a shareholders agreement in place.



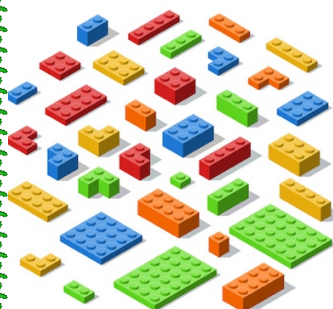
## Trust

You can use a trust to run a business. A trust will have an individual or corporate trustee who controls the trust. It is their job to distribute profits to the beneficiaries of the trust, per the trust deed. If a trust has an individual trustee, the trustee will be personally liable for the trust's debts. On the other hand, if a trust has a corporate trustee, its shareholders receive protection by the company's limited liability. A trust is not suitable if you require profits left in the business to help its scale, as a trust must distribute any income, or it will be taxed at the top marginal tax rate of 49%. Additionally, a trust may also require a unitholders agreement (if it is a unit trust) and a shareholders agreement (if it has a corporate trustee).

## Deciding on a Business Structure

When starting a business one of the first things you should consider is which structure will have the best long-term benefits and reflect your future goals. You will need to think carefully about:

- the type of business you are going to run;
- its risk profile;
- plans for growth;
- the involvement of others; and
- how to come to decisions.



Each structure has different upfront and ongoing costs. A sole trader is the cheapest to establish. Alternatively, more complicated structures, such as a trust with corporate trustees, incur higher legal set up costs and government fees.

The way that tax affects the different business structures will also factor into your decision. The profits made by sole trader businesses are considered personal income and are taxed as such. Companies pay 30% tax on their income but must keep financial records up to date and lodge annual tax returns and reports to ASIC. Using a trust structure may allow you to plan your tax, by streaming distributions to beneficiaries on lower tax rates.

## Ownership vs Control

Additionally, it is essential to consider how each structure is controlled and owned. It is best practice to engage a lawyer to ensure the documents governing each structure are appropriately executed

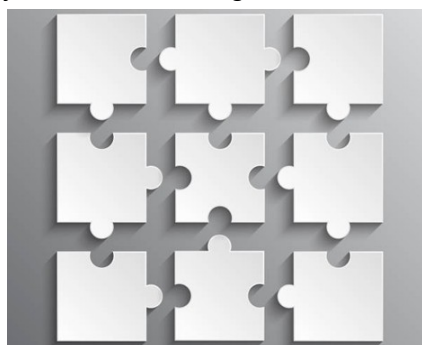
to affect control and ownership distribution amongst the parties. Consequently, choosing the right business structure will allow you to manage the level of ownership and control you desire.

Sole traders wholly own their business and operate in their own capacity. Hence, both ownership and control personally resides with them.

The default position for partnerships is that there is a unity of ownership and control; however, the partnership agreement's provisions can break this. It is crucial to consider how your partnership agreement will divide ownership and control between yourself and your partner(s).

There is a defined separation between the company's owners (shareholders) and its management (directors) in a corporate structure. Management can consist of owners, but this is not a requirement. While the management controls the business's day-to-day decision-making, the owners (shareholders) have the ultimate power to appoint and remove directors from the board. The company constitution typically governs this process; also the Shareholder's Agreement (if the company has one).

A trust structure is defined by the relationship between the beneficial owners (beneficiaries) and the legal owner (trustee). Whilst it is the trustee (legal owner) who makes the decisions concerning distribution amounts and investment strategies following the terms of the trust deed, the ultimate control of the trust resides with the appointer who has the power to replace the existing trustee with a new one.



Source: Legal Vision

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# I am making a profit but where does all the cash go?



Many small business-owners experience this feeling when they look at their books. You work hard, money comes in but it all just seems to disappear. Why?

An accountant will often say this 'problem' is hard to explain and understand, but that the answer is usually quite simple. The following seeks to set out some of the reasons why you might be suffering from this perceived problem.

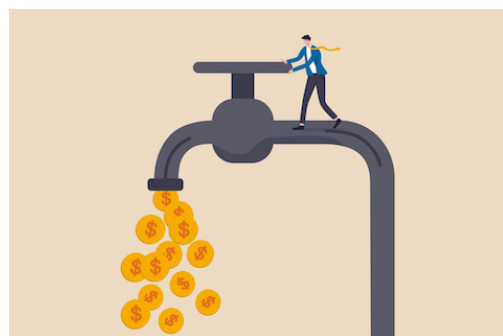
## Profit versus Cash Flow

Firstly, let's get some basics out of the way and look at what profit and cash flow actually are. It seems too many small business owners find these two confusing.

In its simplest form, profit is what is left over after subtracting your expenses from your revenue (sales). A simple Profit & Loss report in an accounting package clearly gives this information. However, comparing sales and expenses every now and again on a piece of paper can be far more confusing. Profit is usually the first number a business owner will look at to determine if all the effort they put in is worth it. It is also the number, with some adjustments, that you pay tax on.

On the other hand, cash flow refers to the balance of cash moving in and out of a business. If more cash comes in, then you have a positive cash flow and vice versa. While maybe not as eye catching as a good net profit, cash flow is just as important, if not more so. The time it takes for your clients to pay is critical to cash flow.

There may only be a subtle difference when looking at profit compared to cash flow and they can often reflect each other, but this isn't necessarily the case and high profits don't always produce positive cashflows. One isn't more important than the other, but managing both well is essential to running a successful business.



## I am making a profit but where does all the cash go?... cont.

### Why the difference?

There are some key differences between profit and cash flow that usually explains why they aren't the same. Here are some examples of where these two differ:

- Profit is usually reported when sales and expenses are accounted for, not paid.
- The accounting or tax treatment of a purchase may not reflect the cash paid for it. For example, asset purchases may be depreciated meaning only a portion of the purchase cost is deductible each year.
- Timing and payment of PAYGW, super and income tax. For example, profit may be looked at every month but BAS is paid every quarter. This situation can be misleading and frustrating when decisions such as spending are made.
- Borrowing for purchases may mean that an expense is claimed but the cost of it is paid off over a period of time. On the other hand, a business can claim the interest on business loans and that can be a big help.
- Personal capital introduced and drawings taken out aren't included in the profit but do impact the cash flow of the business. This is where a business owner has to be weary. Taking money out in drawings has to be controlled as it is quite easy to take too much cash out in this way, meaning business expenses can be harder to pay.

Having your business' funds at your fingertips can make it too easy to withdraw money out at any time to meet your personal needs. While this may sound self-explanatory, many small businesses fall into this trap. To help avoid this trap:

Separate business and personal spending. Credit cards are good for this provided they are paid off in full every month.

Set up a regular transfer to a personal account for your everyday living costs.

Taxes and Super

Knowing when your tax and employee obligations are due to be paid will allow more effective planning and budgeting for your business. With the different timings of when all these payments are due, it can be easy to lose track. To assist in managing your tax and super obligations:



Set up a savings account to transfer funds into, in preparation for making these payments and lessen the blow of a big tax bill.

Try to keep track of your possible taxable income during a financial year. This will help you manage expenses and investments, as well as keep you abreast of possible tax bills you need to pay in the future.

Excessive Debtors

Slow customers payments will negatively affect your business' cashflow. Fortunately, there are ways that this can be avoided:

If your payment terms to customers are too generous, look to reduce this period. For example, rather than allowing 30 days for payment, reduce this to 7-14 days.

Implement processes for effectively tracking and following up on outstanding debts such as monthly reconciliations or limits on accounts.

## **I am making a profit but where does all the cash go?... cont.**

Analyse your customer payments and maintain a good ratio of good pays to bad. This way you can focus on the latter or even identify those you will cease dealing with as the risk to you is too high.  
New Business and Expansion

If you are just starting a business or looking to expand, it is inevitable that you will be experiencing higher cash outgoings. This can be good in the long run but understanding and managing your cash flow during this period is extremely important.

Prepare a budget and work with it on a regular basis. Don't go blindly into anything new.

Be careful of how much you borrow and don't over-extend yourself whether borrowing from a bank or using personal funds. If you can't sustain high enough sales to meet your debt obligations issues will arise.

The differences between profit and cashflow can easily be misleading when managing the operations of your business. In brief, best practise is to plan in advance for the upcoming costs and monitoring cash flow regularly.



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## Scams by numbers - 2022–23 scam data is now available



Did you know that your clients aged between 35-44 are the most likely to pay money to a scammer?

Scams are becoming increasingly harder for the community to identify. The 2022–23 scam data results are now available and they reflect a shift in how Australians are responding to fake emails, SMS and social media messages.

During this period, there were 25,609 ATO impersonation scams reported, an increase of over 25%. Despite the spike in this number, there has been a 75% decrease in the amount of money paid to scammers.

Scammers are becoming increasingly interested in harvesting personally identifying information (PII) rather than requesting payments. Divulging PII continues to be a way for scammers to compromise another's identity, leading to difficulties with lodging tax returns and myGov logins. However, we saw a 71% decrease in people providing this information.

Please encourage your clients to stay vigilant, lock down their identity information and frequently sign into their online accounts to check for unusual changes.

(NB: Stopping scammers funds is the only way to stop them and the above shows we are learning. Keep up the good work!)



### Latest scam data

2022–23 Scams by numbers - Last financial year our data shows:

- There were 25,609 ATO impersonation scams reported to us, an increase of over 25%.
- The amount of money paid to scammers decreased by 75%.



## Scams by numbers - 2022–23 scam data is now available... cont.

- Only 28 people paid money to a scammer, a 66% decrease.
- 346 people divulged personal identifying information (PII), a decrease of 71%.
- There has been a significant shift in the way scammers are contacting people – Email has increased by 179% and SMS contact has increased by 414%.
- The shift toward SMS and email scams has seen an increase in targeted phishing scams, leading clients to fraudulent websites. In response, we have initiated 4,836 take downs of websites with AusCERT.
- 35–44-year old's are now the most likely to pay money to a scammer, this has shifted from the younger demographic of 25–34 year old's in the previous year.
- 25–34-year old's have remained the age group that divulged the most PII to scammers.



Source: ATO

## Festive work parties must dance through an FBT 'minefield'



Any business planning a lavish Christmas party must contend with an FBT minefield and a 16-year-old spending limit unless it is held on the premises, within working hours and involves only current employees.

In a festive message ahead of the party season, the ATO has reminded party planners that the FBT minor benefit exemption of \$300 applies outside a narrow range of strict conditions.

The \$300 threshold for FBT applies to current staff as soon as the party moves off-site but bust the limit for partners – or “associates” – regardless of venue and the costs quickly multiply.

H&R Block director of tax communications Mark Chapman said any businesses that tripped over the complex FBT rules could face a hefty tax bill.

“Provided the cost per head is less than \$300 there’s no FBT because that’s the minor benefits exemption,” he said.

“That exemption limit applies to each individual who comes along. However, if you spend more than \$300 than per head, then the whole lot is subject to FBT, not just the excess over \$300.”

“It can be very expensive. So the difference between spending \$290 per head and \$310 per head isn’t just \$20. You’re looking at a quite substantial tax bill if that’s the case.”



Set in 2007, the \$300 minor benefit exemption “might have been quite a tidy sum once upon a time, but these days it probably isn’t” and would keep being whittled away by inflation since legislation was required to change it.

## Festive work parties must dance through an FBT 'minefield'.... cont.

A quick calculation shows that figure would be almost \$450 if it had kept pace with CPI.

The rules get more complicated once clients, income tax deductions and GST credits are factored in, and Mr Chapman said many businesses probably tripped over the tax unawares.

"We don't really have any idea but anecdotally, it must be lots of companies given that the ATO has a real focus on this and they put the messaging out so soon.

"Because it really is a bit of a minefield in terms of will it be subject to FBT at all? Does the minor benefits exemption apply? Is FBT going to be an issue if you can bring partners or clients?

"All of these issues in total make it a bit of a minefield really. I suspect that there are lots of companies who do actually get it wrong."

He said the only surefire way to avoid FBT was to spend less than \$300 per head or hold the event on a working day and on the business premises.



In its recent reminder, the ATO advised businesses to acquaint themselves with the rules before hiring a restaurant or booking an event.

"It's important to get on top of how FBT works before you provide perks and extras, otherwise you may end up with an unexpected FBT liability," the ATO said.

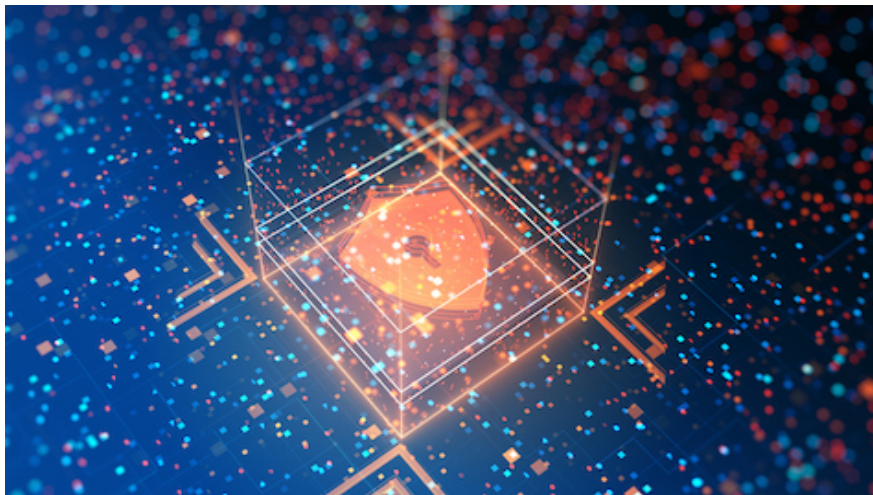
It clarified that FBT was not payable on the party costs for invited clients, but the \$300 threshold applied to "associates of employees (such as their partners)" and to gifts.

Another factor in the overall price was the potential for income tax deductions for the cost of the party, which were claimable only if FBT applied.

The ATO advised celebrating businesses – regardless of guests, venue or cost per head – to keep records of all spending for the post-Christmas tax hangover.

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## Directors on the hook for cyber security, ASIC warns



Repelling attacks is just the start – businesses must demonstrate an ability to respond or the board will be held accountable, the regulator says.

Directors are duty-bound to ensure their company has “adequate” cyber security and the ability to recover from an attack or they could face action by ASIC, the chair of the regulator says.

Joe Longo said cyber readiness meant more than trying to engineer a bulletproof system but extended to building an ability to respond.

“Cyber preparedness is not simply a question of having impregnable systems. That’s not possible,” he said. “Instead, while preparedness must include security, it must also involve resilience, meaning the ability to respond and weather a significant cyber security incident.”

“This can only be built on thorough and comprehensive planning for significant cyber security incidents, and a clearly thought-out risk management strategy.”

Recovery plans on their own were also insufficient without regular testing and never-ending risk reassessment, including within supply chains.

Speaking at the Australian Financial Review Cyber Summit yesterday, Mr Longo said last year’s attacks against Optus and Medibank were a wake-up call but surveys showed most businesses lacked confidence in their organisation’s ability to remain resilient in a “worst-case” cyber event.



One important lesson was that relying on third-party providers always involved risk.

“None of us has control over the security of a third-party provider,” he said. “If we rely solely on the security measures those providers have in place, we leave a wide opening for a data breach if those measures are compromised.”

He said the Latitude Financial breach earlier this year originated from an outside provider and because Latitude was itself a service provider, millions more than its own customers were affected.

Initial findings from an ASIC survey still in progress revealed “that one of the weakest links in cyber preparedness is third-party suppliers, vendors, and managed service providers”.

## Directors on the hook for cyber security, ASIC warns.... cont.

Supply chain risks were a related issue, with almost one in two respondents saying they did not manage third-party or supply chain risk.

Mr Longo said ASIC had uncovered disconnects in the way various parts of a business handled the digital risks between:

- Boards' oversight of cyber risk.
- Management reporting of cyber risk to boards.
- Management identification and remediation of cyber risk.
- Cyber risk assessments.
- How cyber risk controls are implemented.

"This disconnect must be addressed," he said. "Cyber security and resilience are not merely technical matters on the fringes of directors' duties. ASIC expects directors to ensure their organisation's risk management framework adequately addresses cyber security risk, and that controls are implemented to protect key assets and enhance cyber resilience."

"Failing to do so could mean failing to meet your regulatory obligations."

"Measures taken should be proportionate to the nature, scale and complexity of your organisation – and the criticality and sensitivity of the key assets held. This includes reassessment of cyber security risks on an ongoing basis, based on threat intelligence and vulnerability identification."

"For all boards, cyber security and cyber resilience have got to be top priorities. "If boards do not give cyber security and cyber resilience sufficient priority, this creates a foreseeable risk of harm to the company and thereby exposes the directors to potential enforcement action by ASIC based on the directors not acting with reasonable care and diligence."

He said boards and directors also had to consider how they would communicate with customers, regulators, and the market when things went wrong.

"Do they have a clear and comprehensive response and recovery plan? Has it been tested?"



"How will the company detect if the system has been broken, or exploited? History shows that even robust defence systems can be circumvented, and resilience demands you be prepared for that possibility."

He said two points needed to be emphasised: there was a need to act now, and third-party suppliers were a "clear vulnerability".

"If you're not evaluating your third-party cyber security risk, you're deceiving yourself. And recent events show that you will suffer for it."

"Don't put yourself in that position."

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