



Why Tax Plan?

Tax planning is the process of organizing the affairs of a taxpayer so that, as far as legally or commercially possible, the liability of the taxpayer to income and other taxes is minimized.

Tax planning is important and beneficial to most businesses and individuals, and is best done before 30 June 2004 in respect of the 2004 tax year. A small amount of time spent on tax planning, could result in a significantly lower tax bill!

Some common tax planning strategies are:

- Reduce assessable income
- Increase deductible expenses
- Increase tax offsets
- Divert income to an individual with little taxable income

The implementation of these strategies differs from taxpayer to taxpayer depending on many variables. Tax planning should address each strategy and identify whether they are appropriate to each taxpayer undergoing the planning process.

Federal Budget 2004/05

The changes to the individual tax brackets proposed in the recent budget provide some tax planning opportunities in the remaining weeks of the 2004 income tax year. By delaying the point at which income is derived, a permanent advantage may be achieved due to the changes proposed for the 2005 and 2006 tax years. Where deductions can be brought forward into the current tax year, a permanent benefit will be gained as the value of those deductions in the next year will drop due to the changes.

This strategy can be applied in many cases including:

- Repairs & maintenance and other running expenses relating to rental properties;
- Purchasing business consumables before year end;
- Making prepayments of up to 12 months worth of interest for investment properties or geared share portfolios;
- Taxpayers under the Simplified Tax System can make prepayments of business expenses for up to 12 months.



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Capital Gains

Before 30 June 2004 each taxpayer who has realized capital gains should review their unrealized position to determine whether any losses should be realized. For example, if a taxpayer has realized a gain it may be appropriate to sell a loss making investment to set the loss off against the gain and reduce taxable income.

It is important to note that a gain or loss arises at the **date of contract** and **not** at the **date of settlement**. Therefore, you should plan accordingly.

Accelerating Deductions

One of the simplest methods of reducing one's taxable income is to bring forward the recognition of losses or expenses. This strategy involves recognizing deductions when the liability has been incurred. There is an entitlement to a deduction as soon as the taxpayer is definitely committed to the liability and it is capable of being reasonably estimated.

The strategy can also be used by taxpayers that have elected to be part of the Simplified Tax System, although they need to have made the payments by 30 June to benefit from the deduction.

Obsolete stock

Year end planning should include a review of all stock and a determination of the most appropriate valuations to be used. If for special reasons, including obsolescence, the value of stock is less than cost, the taxpayer can bring that stock to account at the market value. The stock could even be valued at the scrap value. Taxpayers can choose different methods for valuing stock from year to year and different methods can be selected for each item of stock.

Simplified Tax System ("STS")

If you are an eligible small business taxpayer, you may realize significant cash flow benefits by electing to join the Simplified Tax System.

Eligibility:

- Must have carried on a business;
- Average turnover less than \$1 million excluding GST (including related businesses);
- Adjusted depreciable value of assets is less than \$3 million (including related businesses but excluding land & buildings).



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Benefits:

- The entity is taxed based on **cash received** rather than on an accrual basis i.e. taxable income is recognized when income is received and expenses are deductible when actually paid;
- Low cost capital items (under \$1000) are **immediately deductible** in full and do not have to be depreciated;
- Accelerated depreciation on most other depreciable assets;
- If opening and closing inventory values vary by less than \$5,000, then they can be recorded as the same for tax purposes and no stock take is required to accurately determine a closing inventory value;
- Prepayments are fully deductible (limited to a 12 month prepayment).

“Income Splitting”

It is tax efficient to ensure that investments are held in the name of the taxpayer with the lowest taxable income. This ensures that income from investments is taxed at the lowest marginal tax rate.

A taxpayer with extensive investments may consider setting up a family trust to own the investments. This structure allows certain flexibility as to distributions. The trustee of the trust is given discretion to distribute income amongst the nominated beneficiaries. Each beneficiary is then taxed based on his or her personal situation. **The first \$7,382 (including the low income tax offset) of taxable income received by a resident is tax free** (except for minors under 18 years of age as at 30 June where the tax free amount is only \$772).

Often a corporate beneficiary is included as part of the family trust structure. Any distributions to this entity from the family trust will be taxed at a flat rate of 30%. This plan is more a deferral strategy. Dividends could be declared at a later date when the shareholders marginal rates are lower.

Topics raised above have been compiled to assist business and individual taxpayers in identifying issues that may be important to their circumstances when planning for the year ending 30 June 2004. The topics covered are by no means exhaustive but should be a valuable prompt in managing your tax affairs. The above topics may not apply to every situation and we recommend seeking advice on your situation. SME Business Solutions can advise you on a range of business and individual tax planning tips. For more information, contact Stuart Boyers or Jared Balkin on (02) 9411-2644.



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