

20 July 2018

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To whom it may concern

**Re: Review of Small Business Tax Concessions**

Crowe Horwath, representing over 250,000 clients across Australia and New Zealand, appreciates the opportunity to provide a submission to the Review of Small Business Tax Concessions. As the leading accounting firm advising small and medium enterprises in Australia, we are well placed to provide real time feedback from our clients' experiences.

This submission provides the following:

- Tax issues of particular concern for small business;
- Our assessment of the various small business tax concessions;
- Improvements for existing small business tax concessions;
- Prioritisation of reform principles;
- The objective of small businesses using a particular legal structure;
- Different small business tax concessions for different sectors;
- The impact of small business eligibility criteria on a business' growth;
- Changing the definition of small business for tax purposes;
- Role of technology in meeting tax obligations; and
- Recommendations.

Please contact us should you have any questions, or wish to seek clarification on any of our comments.

Yours sincerely

**Crowe Horwath (Aust) Pty Ltd**



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## Tax issues of particular concern for small business

In our experience, the tax issue of particular concern for small businesses is simply complying with the complicated and often changing tax rules we have in Australia. All clients want to do the right thing but feel they have no idea what the right thing is. Sometimes clients can be so worried about doing the wrong thing that they miss out on benefits that they would otherwise have been entitled to, or just do nothing at all.

At times, especially post the global financial crisis, where stimulatory tax measures were introduced to encourage spending, taxpayers became accustomed to the existence of certain tax incentives and measures. However, many of these measures were temporary. This leads to a system where a small business taxpayer will become accustomed to a tax measure only for it to be unwound in future years. This again leads to uncertainty in the business community about tax obligations and entitlements.

Furthermore, the inherent uncertain nature of tax measures at times are also concerning. This is particularly the case when announcements are made, effective from the date of the announcement. When the legislation is finally released it has a far wider reach than the announcement ever signified. This makes small business owners quite nervous, and between announcement date and when the legislation is finally passed, in limbo as to how the law will work for their particular circumstances.

## Our assessment of the various small business concessions

### **Lower corporate tax rate**

With the wide range of business related taxes and imposts they are required to pay (including income tax, GST, payroll tax, PAYGW amounts, workers compensation premiums and superannuation contribution obligations), small business owners often feel as though they are in business simply to pay tax.

The recent lowering of the corporate tax rate from 30% to 27.5% was therefore a welcome measure to relieve some of the tax burden being experienced by these businesses. In addition, the increase in the turnover threshold to \$25 million in the 2017/18 year and to \$50 million for the 2018/19 year onwards will also allow a greater number of medium sized businesses to benefit, allowing them to focus more on growing their business. This measure is highly valued by small to medium enterprises as it is easily accessible with no additional paperwork required.

### **Capital gains tax concessions**

The capital gains tax (CGT) concessions are widely valued by the small business community. These concessions provide a welcome reward for business owners who are able to build a business of value and then sell it on. The small business community often feel they pay enough taxes throughout their journey to building a successful business; the availability of the CGT concessions upon the ultimate sale of the business in the end therefore justifying the means.

### **Instant asset write off and simplified depreciation rules**

The instant asset write off and simplified depreciation rules are well regarded by the small business community. The availability of an increased instant asset write off has been of great value for small business, as it has further simplified the bookwork required to be undertaken by small businesses. In addition, the simplified depreciation rules turn what would otherwise be a complicated depreciation

process for small business into something more manageable which is easier for them to understand and manage as most assets will either be written off immediately or pooled together.

#### **Refundable R&D tax offset**

The R&D tax offset goes a long way to encouraging businesses of all sizes to innovate. Whilst many businesses might otherwise choose to innovate irrespective of any Government incentive, knowing that the R&D tax offset is available provides further encouragement to conduct R&D. The availability of the refundable R&D tax offset for small and medium businesses carrying out R&D activities also makes them feel that the Government supports them in their endeavours. The additional cash injection they receive from the R&D tax offset is always reinvested straight back into the business and, in many cases, further R&D.

#### **Immediate deduction for start-up professional expenses**

The immediate deduction available for certain professional and government expenses relating to the proposed structure and operation of a business goes a long way to assisting new businesses with their cashflow in the early days of operation. The professional costs incurred when initially setting up a business are an unavoidable and necessary expense. However, the immediate deduction in relation to these expenses goes some way to mitigating the impact these costs have for a new business enabling the benefit to be reinvested back in to growing the business.

#### **Small business restructure roll over relief**

The introduction of the restructure roll over relief provisions from 1 July 2016 has been welcomed by the small business community. Whilst the small business owners themselves may not know that their operating structure might not be serving them as well it could, at times we as professional advisors have felt bound by legacy structures already in place. These are business structures that either could never have anticipated the ultimate trajectory of the business, or were the result of incorrect advice when setting up the business, which can now be restructured without necessarily triggering a tax liability. To be able to move a taxpayer into a more appropriate structure for their particular circumstances without triggering a tax liability has been greatly appreciated. In turn, when having the conversation with clients that there is an opportunity to restructure their business with no tax liability together with the advantages explained, the client has been grateful they can make the necessary changes.

#### **Two year amendment period**

The two year amendment period provides certainty to small business taxpayers with their affairs and taxation obligations. On the whole, small business taxpayers are genuinely trying to do their best to meet their taxation obligations. However, given the complexities of our tax system, most taxpayers always have a niggling feeling at the back of their mind that they may have inadvertently missed something. That the amendment period closes after two years provides taxpayers with some comfort regarding their tax affairs in the knowledge that they won't be asked to dig up material from many years ago or be subject to an unexpected large tax liability.

#### **Small business superannuation clearing house**

The small business superannuation clearing house removes some of the administrative burden for small businesses and is well regarded. For micro businesses, where the business owner typically is responsible for the administrative tasks as well, it can save that individual significant time, which can then be devoted to running the business.

### **FBT concessions**

The introduction of FBT concessions for small businesses for employee car parking and multiple portable electronic devices has been well received. The availability of these concessions to small business operators allows them to provide their employees with the necessary tools to do their jobs whilst allowing the owner to focus on growing the business.

## **Improvements for existing small business concessions**

### **Simplified trading stock rules**

As the simplified trading stock rules expect the taxpayer to have a reasonable estimate of the value of their stock on hand, it really does not provide much benefit. To reasonably rely upon this measure easily it requires the taxpayer to track their stock ins and outs. For the majority of small businesses, the cost of doing this outweighs the benefits, and so they tend to complete a once a year stocktake to determine their actual stock levels. A threshold of \$50,000 would improve the effectiveness of this measure.

### **Instant asset write off**

It would be highly valued by small businesses if the increased instant asset write off threshold was maintained. This has been a welcome simplification for small business, with the added benefit of an immediate impact on their tax position in the year they incur the outlay to purchase the asset. For some small businesses it has now removed the need to keep an asset register at all.

## **Prioritisation of the reform principles**

Overall, the small business concessions as they operate day-to-day should not prioritise one principle over the other.

However, taking into account the concessions as they stand and looking at the areas in which they are lacking, core principle 1 should be one of the top core principles for the approach to reform, being that the concessions are designed with the small business life cycle in mind. Per the Australian Bureau of Statistics, 60% of new small businesses will fail/close within the first three years of business. Although concessions have some gearing towards assisting with cash-flow, these concessions only come in to effect once the business has profits against which it can utilise the concessions. For many small businesses, especially those that require significant initial cash injection and/or that are cash-hungry, the small business concessions essentially become irrelevant for them in the first few years as they cannot be utilised.

In many ways, the small business concessions only benefit those small businesses who have cash to spend and/or who are making profits. This directly links to core principle 2, which looks at cash flow and notes that businesses in the early life-cycle phases and/or suffering setbacks can only utilise the concessions where there are profits.

## **The objective of small businesses using a particular legal structure**

The main objectives businesses have when structuring is to set up their business in a structure that works best for their circumstances. They want a structure that protects them and their family, whilst

ensuring they don't have to pay more tax than they ought. But the key for small businesses is that they are in a structure where they understand how it works for them.

Small business owners are not typically being set up in complicated structures for the sole purpose of reducing their tax liabilities. However, when determining their structure, the expected taxation implications are a consideration – as they should be for any prudent business person. In assessing whether to start a business, no one wants to work for less than they would currently be earning as an employee, and so tax is a factor.

Additionally, you don't want to have been in business for a period of time, only to find out your tax liability would have been reduced if you were structured differently. Whilst we do not think reducing tax liabilities is a focus of small business, ensuring they're not paying more tax than necessary is a focus, in the same way all businesses try to ensure they're not paying more than necessary for any services.

### **Different small business concessions for different sectors**

In our opinion, tax concessions should not apply differently across different sectors. Although some industries require more capital and outgoings than others, if the concessions are based on the correct factors, then those businesses with higher outgoings/capital receive a higher benefit from the same concessions, thus essentially equalising the sectors.

### **The impact of small business eligibility criteria on a business' growth**

The small business eligibility criteria do not necessarily influence our clients to not want to grow their business. But they do see the \$2 million turnover threshold, and the subsequent loss of access to the small business CGT concessions, as a punishment for their business performing well. Especially as \$2 million turnover doesn't generate a significant profit. Depending on the industry the business operates in, the profit can be less than what they pay their employees.

One alternative to the current \$2 million hard cut-off would be to increase it to \$10 million. In our opinion this would be enthusiastically welcomed by the business community as a change such as this would allow a larger proportion of small business operators to utilise the concessions. Raising the threshold to \$10 million would also align the CGT concession threshold with the thresholds for other small business measures and aid in simplifying the system.

Alternatively, turnover could be assessed over a period of time (for example average turnover for the past 5 years) to arrive at an average turnover that could then be measured against the relevant turnover threshold. This would then allow businesses still in the growth phase to retain their entitlement to the concessions.

The introduction of a 'soft' or staged turnover threshold with an associated phasing out of concessions could also be introduced. However, such a measure would need to be implemented in a simple manner as it could instead merely add another layer of complexity for small business in understanding their entitlements and obligations.

## Changing the definition of small business for tax purposes

In our submission, the definition of small business for tax purposes should be changed although care should be taken that it is not made more complex than it is now. The current \$2 million turnover threshold has been in place since inception in July 2007. Had this value been increased over time in line with increases in relevant measures such as CPI, business earnings and real property prices, the threshold today would be much higher. For simplicity and consistency with other small business measures, we submit that a \$10 million turnover threshold should be introduced. This would give small business owners greater certainty as to their eligibility for the various concessions and allow for a more streamlined tax administration process for all involved.

As indicated above, a more relevant measure of a business' 'small business' status might be to consider the average turnover for the past five years.

In addition, the definition could have more than one facet or step; e.g. test 1 could be turnover under \$2.5 million. If that test is failed, an alternate test could be turnover under \$4 million but less than 10 employees. These are just examples but a test hierarchy such as this would at least capture those business with high-value/turnover goods/services but who are in fact still small operations.

## Role of technology in meeting tax obligations

Technology only makes it easier to comply with tax obligations and access concessions if the technology itself is simple, accessible and reliable. Many clients struggle to find the time to learn the required information or software and rely heavily on their tax agents/accountants to interpret, analyse and disseminate the relevant information to them. Furthermore, older clients struggle to engage with and understand technology, which restricts the ability of their tax agents/accountants to introduce technology to their interactions with that client.

## Recommendations

Our recommendations can be summarised as follows:

- Increase the turnover threshold of a small business entity to \$10 million for all small business concessions
- Maintain the \$20,000 threshold for the instant asset write off
- Increase the simplified trading stock threshold to \$50,000