



# BUSINESS ISSUES

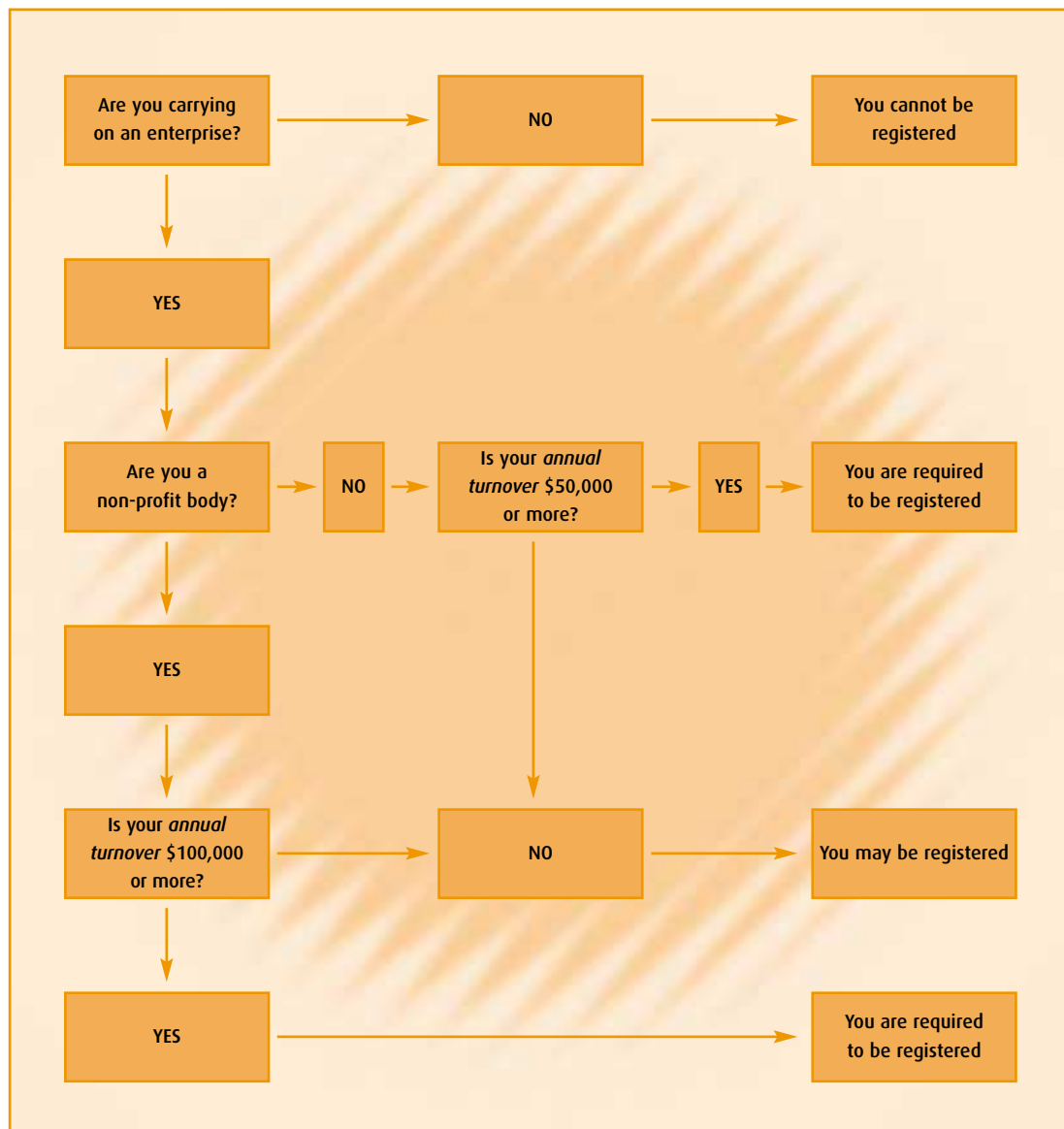
## Basic Registration Issues

Registering for an Australian Business Number and registering for GST are two separate issues.

Even though you may not be required to register for GST and choose not to register, you may still be required to have an ABN.

If you do not have or provide an ABN for goods and services you supply after 1 July 2000, all payments made to you may be subject to the new withholding tax of 48.5%. (Note that this applies to commercial businesses making supplies to other businesses. Accordingly, it does not apply to organisations whose income is exempt from income tax activities, or activities being undertaken as a hobby, private recreational pursuit or where there is no reasonable expectation of profit.)

You do not have to be registered for GST to get an ABN, however you **MUST** have an ABN to register for GST.



Annual turnover of \$50,000 or more it is **compulsory** for you to register.

Annual turnover of less than \$50,000 you may register **voluntarily**.

**If you are a non-profit organisation:**

Annual turnover of \$100,000 or more it is **compulsory** for you to register.

Annual turnover of less than \$100,000 you may register **voluntarily**.

## The concept of “annual turnover”

The concept of annual turnover for GST purposes will include all amounts payable to your business on its own account, that is, gross income as opposed to net income (this excludes GST). To this extent, *annual turnover* will not include amounts payable to your business where these are held “as agent” on behalf of someone else. It also includes the GST exclusive market value of goods and services provided to you in return for supplies you have made in the course of your business.

Your *annual turnover* calculation should also exclude income derived from *input taxed supplies* and supplies made for no consideration, private sales or gifts/donations received.

### EXAMPLE

Maree runs a small commercial art gallery buying and selling works of art and crafts. Her annual turnover is \$75,000. Maree does not have a choice whether to register or not, she **MUST** register. *Registration is determined by annual turnover in this instance.* Assume Maree simply charges a fee for arranging the sale of the artworks as an agent from artists direct to consumers. Maree receives \$60,000 from consumers which is passed on directly to the artists and \$15,000 in commission on those sales which she processes through her accounts. Maree’s annual turnover would now be \$15,000 as the \$60,000 was merely held on behalf of the artists. She can **CHOOSE** whether she registers for GST or not.

When estimating your annual turnover for GST purposes, you will need to assess your twelve month turnover using both of the following methods:

1. the current month plus the past 11 months turnover (your “current annual turnover”)
2. the current month plus the next 11 months estimated turnover (your “projected annual turnover”)

In estimating your future annual turnover you exclude any anticipated transfers of capital assets. Refer to the following table to see when you are required to register and when it is optional.

## Considering Turnover Threshold

Current Annual Turnover (CAT) <sup>Δ</sup>	Projected Annual Turnover (PAT) <sup>†</sup>	REGISTRATION
Over	Over	Compulsory
Over	Under	Optional
Under	Over	Compulsory
Under	Under	Optional

### Why register for GST?

If your *annual turnover* is below the threshold amounts (\$50,000, or \$100,000 for non-profit organisations), you may choose to register. There are various factors to take into account when considering whether or not to register.

Where you choose not to register, you will be unable to claim any input tax credits for GST paid on purchases and cannot charge GST on supplies you make.

In some cases, the value of your supplies, i.e. the amount you charge for your supplies excluding GST, may have to be increased to take account of GST paid on your purchases which cannot be recovered via an input tax credit.

That is, to enable you to retain the same dollar margin, you might have to increase your prices as GST will be a real extra cost to you.

Therefore, there are a number of factors to consider in the registration decision process, which include:

- > how price competitive, and therefore sensitive, is the market place and will the addition of GST cause customer loss to non-registered competitors?
- > will registration possibly enable a better financial return through your ability to reclaim GST on its input costs while maintaining previous turnover (net of GST) levels?
- > are your customers, sponsors and suppliers predominantly businesses who will be required to register? If so, those businesses may actively persuade you to register in order that in-house GST documentation and administration procedures can be developed with a minimum of exceptions
- > are your customers, sponsors or suppliers mainly unregistered persons, i.e. end consumers? If you are unregistered, customer demand is more likely to be based purely on price, ie they are not influenced by your decision to register or not, rather than by the end price of the goods and services

<sup>Δ</sup> Current Annual Turnover - equals turnover for the current month plus the previous 11 months.

<sup>†</sup> Projected Annual Turnover - equals turnover for the current month plus the next 11 months.

## Dealing with registered or unregistered suppliers

We can illustrate the consequences of dealing with registered or unregistered suppliers by reference to the following table:

	Registered Supplier	Unregistered Supplier
Cost of inputs	100	100
GST paid	10	10
Input tax credit	(10)	0
True cost of inputs	100	110
Margin	100	100
	200 <sup>+</sup>	210
GST charged	20	0
Price to customer	220 <sup>Δ</sup>	210 <sup>†</sup>

<sup>+</sup> shows the true cost of the supply where the recipient can claim an input tax credit of \$20

<sup>Δ</sup> shows the true cost of the supply where the recipient is unable to claim an input tax credit of \$20

<sup>†</sup> shows the true cost of the supply for any recipient where the supplier is not registered and no GST is charged by the supplier

Therefore, all other things being equal, the example shows that a recipient of supplies who couldn't claim input tax credits may prefer to deal with an unregistered supplier as the cost of the supply would be \$210, rather than \$220 from a registered supplier.

However, it is important to note that this does not mean that customers who are unable to claim input tax credits should always deal with unregistered suppliers. Depending on the mix of inputs, labour and the profit margins, it would be possible to show examples where the cost of a supply from an unregistered supplier would be more than from a registered supplier.

### Not registering when you should

Not registering when you should is a very serious matter. The ATO can back-date your registration to when you could 'reasonably have been expected to realise' that your turnover was over the \$100,000 limit.

If you fail to register, you could face:

- > being fined for not registering
- > your registration being back-dated to a date determined by the Commissioner
- > having to make back-dated GST payments for taxable supplies you made from the backdated date of your registration (when it's too late to collect GST from your clients or claim input tax credits to offset this)

- > difficulty in substantiating input tax credits for GST that you paid on acquisitions after the backdated registration date, because you may not have been focused on obtaining tax invoices

**Remember:**

- > **the liability to pay GST to the ATO falls on the business that makes the supply, not the customer**
- > **the liability to GST is 1/11 of the price you sold the item for, whether you adjusted your prices to include GST or not**

## Options for GST registration

Non-profit organisations have several options for GST registration:

- > defining the organisation as a single entity, and registering or choosing not to register as the registration rules allow
- > registering with other entities as a group
- > registering as a parent entity with branches
- > under special flexible registration arrangements, available only to charities and certain non-profit organisations, units of a GST-registered entity can be treated as separate entities, these are called sub-entities

## Grouping

Non-profit entities which:

- > operate together in providing services
- > are members of the same non-profit association (note: some or all of the members of the association can join the GST group)
- > are registered, have the same tax periods, and account on the same basis (cash-based or accruals)
- > are not members of another GST group
- > can apply to the Commissioner of Taxation to be treated as a GST group.

Grouping brings administrative advantages, since it can reduce administrative and compliance costs because:

- > one entity (called the 'representative member') manages GST affairs for the group and lodges one Business Activity Statement (BAS) on behalf of all group members
- > transactions between entities within the group are not treated as taxable supplies (ie no GST is payable and no input tax credits can be claimed on transactions between members)

**This method would only be advantageous where each of the entities was registered.**

## Branching

A GST registered entity which operates through a branch structure can choose to register each branch (or branches) separately for GST. If it does this it becomes known as the 'parent entity' and the process is called branching. Branching is only possible if the branch carries on an enterprise and the parent entity is not a member of a GST group.

Branching means that each registered branch operates as a distinct entity for GST purposes:

- > each branch must report separately to the ATO
- > GST is payable on transactions between the GST branches and the parent entity, and between branches

Having branches and other activities treated as 'sub-entities' (see below) is a special option for charities.

Sub-entities - flexible registration arrangements for non-profit organisations.

A non-profit organisation which is registered for GST can choose to have units of its operation treated as sub-entities for GST. Each unit must have its own accounting records and be identifiable by distinct activities or location. For example:

- > branches (local offices)
- > individual properties or projects
- > groups of properties under separate funding programs
- > support services funded by different funding programs
- > special projects
- > fee for service arrangements
- > tenant groups
- > individual fundraising activities etc

If a non-profit organisation opts for this form of registration, each unit will be treated as a separate entity.

That means that a unit must register as a separate entity if its turnover is greater than \$100,000.

Once the ATO has given approval for a charity to treat its operations as separate units, the decision cannot be changed for 12 months.

## When to pay and claim GST

### Reporting GST to the ATO

GST registered businesses must choose the appropriate:

- > tax period: quarterly or monthly
- > accounting system: you can account for GST using cash or accruals-based accounting
- > lodgment method: your return can be made to the ATO electronically or manually

### Tax Period

Choosing the right *tax period* is yet another decision that will impact on your business operations. The GST tax reporting periods are monthly or quarterly depending on the *annual turnover* of the enterprise.

GST registered businesses (with a turnover less than \$20m) must pay their GST liability to the ATO *at least* every three months.

You can choose to pay every month, if that helps manage your cash flow (for example, if you usually get refunds, or if you want to avoid spending GST you owe to the ATO).

You must have your GST report, the Business Activity Statement (BAS), in to the ATO within 21 days of the end of each tax period.

If your overall tax liability is a payment by your organisation to the ATO, you must make that payments within 21 days of the end of the GST period.

If your overall tax liability is a refund to your organisation, you will receive this refund from the ATO within 14 days of lodging your BAS. If not the ATO will pay interest for the period of the delay.

#### Option 1: Lodging your Business Activity Statement every 3 months

For the tax period	GST payments are due no later than	Refund is due
June to September	21 October	4 November
October to December	21 January	4 February
January to March	21 April	5 May
April to June	21 July	4 August

## Option 2: Lodging your Business Activity Statement every month

For the tax month	GST payments are due no later than	Refund is due
June	21 July	4 August
July	21 August	4 September
August	21 September	5 October
September	21 October	4 November
etc	etc	etc

## What Tax Period should you choose?

If you are in a position to be able to choose your tax period, then you should base this decision on the following factors:

- > the time, effort and cost involved in preparing returns
- > the volume of transactions of your business
- > the timing of the transactions of your business
- > the method of accounting you are using
- > your cash flow position
- > whether you collect the GST or it is still in your uncollected debtors

When considering cash flow costs versus administrative costs you should bear in mind that the opportunity cost (ie lost or extra interest) on cash flow may not be that great over a three-monthly period, although this needs to be weighed against whether you will actually have the cash needed.

### Monthly tax periods may be preferable where:

- > you purchase business inputs regularly throughout the year and/or their cost is substantial
- > your sales are either of GST-free goods, or, if taxable, they are infrequent
- > you have the time and capacity to prepare the GST returns at little cost
- > where you predominantly issue invoices for your supplies but pay cash for your expenses

**Quarterly tax periods may be preferable where:**

- > you purchase business inputs irregularly and/or their cost is not substantial
- > your sales are either GST-free, or, if taxable, they are regular
- > the preparation of GST returns is costly to you
- > where you predominantly receive cash for your supplier but pay for expenses on invoice (where you account on an accrual basis)

Cash flow implications are an important area of business and risk management and must be considered in detail.

**Cash v Accruals Method of Accounting****What accounting system will you use for GST?**

There are two ways to account for GST - cash-based GST accounting or accruals-based GST accounting.

- > If you are a registered charity, you can use either basis, regardless of your annual turnover.
- > If you are not a registered charity, the GST accounting system you must use depends on your annual turnover:
  - more than \$1,000,000** - you must use accruals accounting or get special approval to use cash-based accounting. (You will be entitled to account for GST on a cash basis where you lodge income tax returns on a cash basis.)
  - less than \$1,000,000** - you can choose to use either cash or accruals-based accounting

Your decision is not limited by your organisation's current accounting method. You can choose the GST accounting basis that is best for your organisation. However, it will obviously be additional administrative work for you to account for GST on an accruals basis if you are accounting for income tax on a cash basis.

**Cash-based GST accounting**

With cash-based GST accounting you deal with GST when money changes hands. This is simple and has little impact on your cash flow.

Cash-based GST accounting means that you:

- > have to pay GST on taxable supplies according to when you receive payment **or part payment** from your clients and customers
- > can claim input tax credits only when you have paid the bill from your suppliers (and you hold a valid tax invoice)

For example: If you draw on your grant cheque in July 2000, you must pay GST on it for the period ending in July 2000.

If you pay your stationery supplier in October 2000, you claim back input tax credits in the period that includes October 2000, even if you receive the stationery supplies earlier or later.

## Accruals-based GST accounting

With accruals-based accounts you deal with GST in the tax period the transaction happened, even if no money changed hands. This may be more complicated and has a greater impact on your cash flow.

Accruals-based GST accounting means that you:

- > where you predominantly receive cash for your supplier but pay for expenses on have to pay GST in the tax period when you issue an invoice or when payment or part payment is received from your customer, whichever is earlier - you may have to pay GST on supplies you have not been paid for yet
- > can claim input tax credits in the tax period when you receive an invoice from your supplier, or when you pay the bill, whichever is earlier - if you have a valid tax invoice, you may be in a position to claim input tax credits before you have paid for

For example, if your grant cheque goes into your bank account in July 2000, or you have invoiced the funding body in July 2000 but not yet received the grant cheque, you have to pay GST in the tax period ending in July 2000, even if the grant is for services you will provide from July to September 2000.

If you sell in September, you must pay GST for the tax period ending September, even if you don't get paid until November.

If you are invoiced for stationery purchases in August, you can claim input tax credits during the tax period including August, even if you don't pay your supplier until October.

While there are arguments for and against the use of either the cash or accruals method, the decision will usually depend on the specifics of your business. Some guidelines are provided below:

**The accruals method and purchases on credit:** the accruals basis can be more favourable where a business makes the majority of its purchases on credit. As the entitlement to claim an input tax credit under the accruals method arises on invoice, there may be a potential cash flow benefit where those input tax credits are claimed from the ATO, prior to payment being made for the supply, as long as you hold a tax invoice.

**The accruals method and lengthy debtor terms:** conversely, where a business has long delays in debtor payments, cash flow problems may arise as you may be required to remit GST to the ATO prior to receiving payment from debtors. In such cases, it may well be preferable to account for GST on a cash basis.

**Changing from cash to accruals:** Provided your annual turnover is less than \$1,000,000, you can change accounting methods from accruals to cash accounting and vice versa. If your annual turnover is \$1,000,000 or more and you do not use the receipts method for income tax purposes, then you must use accruals accounting (unless you get the ATO's permission).

If you are using cash accounting and your annual turnover increases to \$1,000,000 or above, then you must change to accruals accounting from the beginning of your next tax period unless you are using the receipts method for income tax purposes.

**Action Decisions:**

- > in order to alleviate potential cash flow issues where you are using the accruals basis, you should ensure that your collection methods are effective - this is much more important in a GST environment.
- > you will need to negotiate your trading terms with suppliers and customers and be aware that your suppliers too will want to bring forward your payment terms.

You are currently using cash accounting and quarterly tax periods. Your annual turnover is \$200,000. In the month of August 2001, you decide that you wish to change your method of accounting. Your GST return for the quarter ended 30 September 2001 should be done on the basis of cash accounting. You can change to accruals accounting from the quarter beginning 1 October 2001.

You are currently using accruals accounting for both income tax and GST purposes and monthly tax periods. Your annual turnover is \$1,600,000. You have a good compliance record with the ATO and use a financial year ended 30 June. You decide that you would prefer to change to cash accounting and quarterly tax periods. You cannot change your accounting method without the ATO's permission because your turnover is above the threshold of \$1,000,000. However, you can change your tax period from monthly to quarterly.

You are currently using cash accounting and monthly tax periods. In the month of May 2001 it becomes apparent that your projected annual turnover will be \$2,000,000. Your GST return for the month ended 31 May 2001 will be on a cash basis. From 1 June 2001 you will be required to change to accruals accounting for GST purposes unless you are using the cash method for income tax.

### What happens if you do change methods?

Some care is required in changing methods to make sure that all transactions are brought to account only once for GST purposes. There are special transitional rules that apply in these circumstances.

If you change from cash accounting to accruals accounting, supplies that were invoiced before but not paid until after the change would be overlooked if the normal rules applied. Conversely, changing from accruals accounting to cash accounting would result in GST input tax credits or liability being reported twice if the normal rules applied. Therefore, when changing from cash accounting to accruals accounting the transitional rule is that:

- > if a supply was not included (either in full or in part) in a tax period before the change, but would have been included if the change had been made earlier, then the supply (in full or the part remaining) must be brought to account in the first tax period that the change takes place

You buy goods on account and are invoiced in June 2001. You pay the account in August 2001. For the tax period ended 30 June 2001 you were using accruals accounting. You change to cash accounting from 1 July 2001.

The GST input tax credit is brought to account in the period ended 30 June, as this is when the tax invoice was received. You do not also claim a GST credit for the same transaction when you pay the account in the next period. Each transaction is brought to account only once.

You are using cash accounting as at the quarter ended 30 June 2001 and you change to accruals accounting from 1 July 2001. You receive a tax invoice in June for the supply of art materials, including GST paid of \$200. The invoice is not paid until 30 July. As you were using cash accounting in the June quarter when you received the invoice, you did not claim the GST input tax credit at that time. When you change to accruals accounting in the next tax period, you must claim the credit in that period, even though the invoice was received in the earlier period. You can only claim the credit once.

When changing from accruals accounting to cash accounting the transitional rule is that:

- > the GST effect of any transaction is brought to account once only. Where it has not been brought to account when the change takes place, it will be brought to account in the next tax period.

## Adjustments

In the course of doing business, certain events occur which will give rise to an adjustment (or correction) being made to the accounts. As GST is based on transactions, where an adjustment occurs in the accounts it may have potential GST implications.

The ATO Industry Booklets provide a simple summary of events likely to result in an adjustment. These are outlined below:

- > all or part of a supply or purchase is cancelled
- > the *price* for a purchase or supply is altered (such as when you provide or become entitled to a volume discount or early payment discount)
- > a supply becomes *taxable* or a purchase becomes creditable
- > a supply stops being *taxable* or a purchase stops being creditable
- > the purpose of your purchase changes
- > you have bad debts or you fail to pay a debt

Increasing adjustments will occur where the GST amount has been understated (so there is more GST to pay).

Conversely, decreasing adjustments will occur where the GST amount has been overstated (so there is less GST to pay). For instance, if there is a change in the *consideration* you receive or are entitled to receive for a supply, you will need to make either an increasing or decreasing adjustment to adjust the GST.

Where the *price* decreases, the amount of GST payable will decrease, conversely, where the *price* increases, the amount of GST will increase. Where an increasing or decreasing adjustment is necessary, the supplier must issue an *adjustment note* within 28 days of either a recipient's request to do so, or becoming aware that the recipient has an increasing or decreasing adjustment. The *adjustment note* will have to contain similar details to the *tax invoice*.

### EXAMPLE

Julie's Art 'n' Craft sells works to Alessio for \$110 (\$100 + \$10 GST) on credit in August 2000. Julie's payment terms include a 5% discount for payments received within 30 days. Alessio (a keen businessman) remits \$104.50 (\$95 + \$9.50 GST, or 95% of \$110) to Julie in September but before the discount period expires.

When Julie sells the works, she remits \$10 GST to the ATO in her August return. (Julie is a monthly lodger.) However, as the GST on the sale is now only \$9.50, Julie will need to make a decreasing adjustment in her next return to ensure that she claims back the 50c which is now an overpayment of GST. Julie will also be required to issue an adjustment note to Alessio.

A draft ruling from the ATO regarding information requirements for adjustment notes was released in December 1999.

## Bad debts

As discussed above, an adjustment may be required where an enterprise writes off a debt as bad or recovers amounts previously written off. Currently, a bad debt may be written off either when you know that the debt is bad and write it off for accounting purposes, or after a period of 12 months has elapsed. An adjustment would need to be made in the tax period that the debt is written off to account for GST appropriately.

A draft ruling from the ATO regarding the treatment of adjustments and the write-off of bad debts was released in December 1999.

### EXAMPLE

James, an art consultant, provided advice to New Form Gym in the fit-out of new premises. New Form Gym was invoiced for the amount of \$1,100 but has not paid for the goods one year later. Although James has commenced legal action, no recovery of monies occurred or is reasonably likely to occur. James does not account on a cash basis and writes off the \$1,100 as a bad debt.

GST of \$100 has already been remitted to the ATO. However, when the total amount of \$1,100 is written off, an adjustment is required. The adjustment of \$100 ( $\$1,100 \times 1/11$ th) reduces James's net amount of GST to be accounted for in the tax period in which the amount is written off (i.e. the \$100 GST originally paid is a "decreasing adjustment" which James shows as a credit on his next BAS).

## Changes in creditable purpose

The treatment of adjustments for a change in creditable purpose is different from the normal *adjustment events* above. Where the actual use of an acquisition changes from a creditable purpose to a non-creditable purpose (for example, from a business to *personal use*), an adjustment must be made. An adjustment is also required where the extent of the creditable purpose of the asset has changed.

### EXAMPLE

Noel buys a computer in July for his business. He estimates the business use to be 95%. He claims an input tax credit equivalent to 95% of the GST included in the price of the computer.

During the next 12 months, Noel uses the computer 20% of the time for games. He is required to reduce the amount of credit he has claimed from 95% to 80% of the GST included in the price of the computer.

Unlike other adjustments, these must be calculated at the end of an '*adjustment period*' (a 12 month period ending on 30 June) and the use must be monitored for further *adjustment periods* depending on the value of the good e.g. for goods costing \$1,000 to \$5,000, two *adjustment periods* will be required.

The computer that Noel purchased cost him \$4,000. He is required to monitor his private use of the computer for two adjustment periods, ie over two periods of 12 months ending on 30 June.

Noel does that and finds that he has used the computer for business use for 100% of the time during the second year. That brings his total business use for the computer to 90% over the two year period. That means Noel is entitled to an adjustment to increase the *input tax credit* that he has claimed for the computer from 80% to 90%.

It will be necessary to keep records of the actual application of the goods or service acquired (eg business or *personal use*) to be able to perform the relevant calculations required. Note: anyone in business will not be required to keep any records for this process other than those already required for Income Tax purposes.

#### **Adjustment periods required for a change in creditable purpose**

GST-exclusive amount of consideration for the acquisition	Number of adjustment periods
\$1,000 or less	None
\$1,001 to \$5,000	Two
\$5,001 to \$499,999	Five
\$500,000 or more	Ten

Source: ATO Bulletin - "Travel and Tourism & The New Tax System" page 45

There are different rules about the number of adjustment periods for purchases used in making financial supplies. The ATO released a ruling on 22 December 1999 on this issue.

### **Mixed supplies**

In some cases, you will be selling or purchasing mixed supplies, that is, a mixture of different types of supplies (for example, GST-free and taxable supplies). Where this occurs (and it may be common), it will be necessary to separately identify those types of supplies and ensure that they are treated in the appropriate manner.

#### **EXAMPLE**

Theresa runs a restaurant in an arts centre and is registered for GST. Theresa purchases both fruit and pastry to prepare one of her sumptuous desserts. Fruit is a GST-free supply, however, pastry is a taxable supply.

Theresa must ensure that she records the purchase of these supplies correctly in her books so that she claims the appropriate input tax credits.

The dessert that Theresa sells will be subject to GST.

In an effort to reduce accounting costs, the ATO has proposed a simplified method of accounting for GST for small retailers of food who will have an annual turnover of up to \$1,000,000. The proposed method will allow eligible businesses to calculate the percentage of annual turnover which relates to taxable sales, and, then calculate the GST based on that percentage. Further details of this simplified method have been released by the ATO and are available on the web or by phoning 132478.

## Classifying and capturing transactions

The ability to classify and capture all transactions appropriately is a key for survival in a GST environment. As discussed, GST is a tax based on transactions, it is essential that **all** of your business transactions are accurately recorded. Where transactions are not classified or captured correctly, your business could stand to lose valuable *input tax credits*, or fail to remit the appropriate amount of GST, which could lead to fines and penalties being incurred.

The first step to ensure that your business will comply is to classify your transactions. This means re-classifying your transactions to establish the appropriate GST treatment of each transaction, (that is, *taxable*, *GST-free*, *input taxed*, or out of scope). A simple method of going about this classification is to use a table similar to the one presented below to analyse each transaction your business makes and to ascertain where that transaction fits in to the GST regime.

### Cafe run by Art Gallery

The Yirra Art Gallery runs a cafe and is registered for GST. The Art Cafe purchases both fruit and pastry to prepare one of their sumptuous desserts. Fruit is a GST-free supply, however, the pastry is a taxable supply.

The Art Cafe must ensure that they record the purchases of these supplies correctly in their books so the Cafe can claim the appropriate input tax credits.

The dessert that the Art Cafe sells will be subject to GST.

Transaction	Taxable	GST-Free	Input Tax	Out of Scope
Fruit/Vegetable purchases		X		
Sale of restaurant meals	X			
Payment of Chef's Salary				X
Mortgage Interest			X	

## Internal recording and reporting

Record keeping processes and documentation will need to change with the advent of the GST. Accounting systems will also need to change to some extent. One of the most important aspects of the new GST regime is the use of tax invoices.

### Tax invoices

A *tax invoice* is a document that records the supply of goods or services and is the key mechanism to claiming *input tax credits* for goods or services *valued* at more than \$50 (\$55 inclusive of GST). **If you don't have a valid tax invoice, then you cannot claim the input tax credits.**

The *tax invoice* must record:

- > the GST-inclusive *price* of the goods or services supplied
- > a brief description of the supply
- > the Australian Business Number (*ABN*) of the supplier
- > any other information required by the Tax Office (see below); and
- > in a format approved by the Tax Office

A *tax invoice* may be separate from, or incorporated with, a regular sales invoice. While it is not necessary to show the **amount** of GST on the invoice, it may be beneficial for you (as well as for the purchaser) if GST is shown separately. It is important to note though, that a credit card slip alone will not constitute a *tax invoice*.

GST registered businesses must:

- > **provide a tax invoice** to a purchaser within 28 days of the purchaser requesting a tax invoice

For example: when an arts organisation receives their grant from a funding body, they must provide the funding body with a tax invoice within 28 days of a request for a tax invoice (unless the funding body issues a 'recipient created tax invoice')

- > **check that invoices they receive** from their GST-registered suppliers are in the format required by the ATO for claiming input tax credits. For example: that the invoice includes the ABN of the supplier and specifies the price and GST is included in the price

- > **store all tax invoices** so they can be easily used when recording GST payments

For example: While a supplier does not have to give you a tax invoice until 28 days after you request one, you don't have to pay the bill until you have a valid tax invoice, and then store the tax invoice with your cheque requisitions.

- > **withhold part of the invoice amount if there is no ABN** - the 'withholding tax' amount is currently 48.5% of the invoice price and this must be sent to the ATO. (Withholding only applies where the transaction is between two businesses and the supplier does not quote an ABN.)

Consider the other possibilities:

**Business to Business** - For example: if your handyman gives you a handwritten bill for \$100 with just his name, the work done and the amount to be paid, you can only pay him \$51.50. You have to 'withhold' 48.5% of the bill (in this case \$48.50) and send this \$48.50 to the ATO.

**Business to Private** - Distinguish between the handyman who is in business doing this for you at home, that is, you are a consumer, i.e. there is no ABN withholding tax.

**Business to Non-Business** - Also note that if the work is being done for your business, but the handyman is only carrying on a hobby, then there is no ABN withholding. If the handyman carries on a business you must deduct if no ABN is quoted.

Note: The Australia Council is working on the simplest possible practice for its clients and will be advising them directly.

The ATO has produced *tax invoice* regulations that specify additional information requirements for three types of *tax invoices*:

- > supplies (excluding GST) of \$1,000 or more
- > supplies of less than \$1,000
- > recipient created *tax invoices*

It may be prudent to choose a tax invoice format that reflects the requirement for the highest *priced* goods or services that you may supply, ie if you supply goods *valued* at between \$50 and \$50,000 you would probably wish to simplify your system by issuing one type of *tax invoice*. To do so, it would be necessary to ensure that it complies with the requirements of a *tax invoice* over \$1,000.

If you deal entirely with consumers you may never need to issue a tax invoice. In these cases your cash register docket will be sufficient as a receipt. However, you need to remember that you will need to be able to issue a tax invoice if you are requested to do so.

We have included below examples of tax invoices where the taxable supply is less than \$1,000, and where the taxable supply is more than \$1,000. Although it is generally advisable to use one standard form of invoicing, for the purposes of illustration, in the first example, the GST component of the price is not separately identified, whereas in the second example it is.

The fundamental differences between tax invoices for supplies less than \$1,000 and tax invoices for supplies of \$1,000 or more are identified in the tax invoice requirements table below.

The tax invoice for supplies of \$1,000 or more includes the following additional requirements:

- > name of recipient
- > address or ABN of the recipient
- > the quantity or volume of what was supplied

**Tax Invoices for supplies of \$1,000 or more:****MUST INCLUDE:**

- > The words "Tax Invoice"
- > Name/Trading Name of Supplier
- > Issuer's ABN
- > Date of Issue of Invoice
- > Brief description of each thing supplied
- > GST-inclusive price for supply

**TAX INVOICE**

**Spring Productions** #:121/2K

**ABN:** 123 456 789 10

**Date:** 7 August 2000

**To:** Emry & Old

Description:	Price (A\$)
--------------	-------------

Flyer Printing	\$880.00
----------------	----------

<b>Total GST Inclusive Price</b>	<b>\$880.00</b>
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**Tax Invoices for supplies of \$1,000 or more:****MUST INCLUDE:**

- > The words "Tax Invoice"
- > Name/Trading Name of Supplier
- > Issuer's ABN
- > Date of Issue of Invoice
- > Name of Recipient
- > Address or ABN of Recipient
- > Brief description of each thing supplied
- > Quantity/volume of thing supplied
- > GST-inclusive price for supply

**TAX INVOICE**

**Locatelli Consultants** #:120/2K

**ABN:** 123 456 789 10

**Date:** 10 August 2000

**To:** Hennessy Brothers

**Recipient:** Andrew Hennessy

**of supply:** Hennessy Brothers  
 ABN: 10 987 654 321  
 9 Park Street  
 Outtaway NSW 0000

Description:	Price (A\$)
--------------	-------------

Consultant Fees for month of July 2000:	\$33,000.00
---	-------------

GST:	\$3,300.00
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<b>Total GST Inclusive Price</b>	<b>\$36,300.00</b>
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Requirement	> \$1,000	> \$1,000 where GST is 1/11th of the price	> \$1,000 where GST is less than 1/11th of the price	> \$1,000 and mixed supplies	< \$1,000, same as >\$1,000 scenarios EXCLUDING	additional requirements where recipient created
ABN of supplier						
the GST-inclusive price of taxable supply	×	×	×	×		
the words "tax invoice"	×	×	×	×		
date of issue	×	×	×	×		
name, or trading name of the supplier	×	×	×	×		
name of the recipient	×	×	×	×	×	
address or ABN of the recipient	×	×	×	×	×	
brief description of each thing supplied	×	×	×	×		
quantity or volume of what was supplied	×	×	×	×	×	
the words "the total price includes GST for supply" or The GST-exclusive value and the amount of GST.		×				
GST-exclusive value and the amount GST			×			
Identify each taxable supply and show: - the GST-exclusive amount of supply - the amount of GST payable; and - the total amount payable				×		
the words "recipient created invoice"						×
the words "the GST shown is payable by the supplier"						×

### Pre-GST tax invoices and input tax credits

ATO Tax Reform Bulletins outline procedures for the issue of *'tax invoices'* prior to 1 July 2000 for supplies to be made after this date where the amount charged includes an amount for GST. The ATO has also released a draft Ruling (GSTR 1999/D2) which allows a business to claim an *input tax credit* without the need to hold a *tax invoice*.

Essentially the Ruling recognises that amounts of GST are being charged for portions of a supply which relate to the period after 1 July 2000, eg: annual membership to an association or a magazine subscription. At the same time, while there is this requirement to charge GST, businesses affected may not as yet have received an *ABN*.

In order to comply with the Australian Competition and Consumer Commission (ACCC) requirements, GST should be identified on the invoice from your supplier. In these cases you would be entitled to claim an *input tax credit* for this GST in your first return after 1 July 2000.

If you obtain an invoice prior to 1 July 2000 which meets the requirements set out in the Ruling (when finalised) you should be able to use that invoice to claim an *input tax credit* after 1 July 2000 for the GST you are being charged now.

### **Recommendation for pre-1 July 2000 invoices**

Because Tax Invoices will not actually exist until 1 July 2000, the Tax Commissioner will allow Input Tax Credits to be claimed in relation to amounts paid for GST prior to 1 July 2000, where the following details are available on a document to show that the amount has been paid.

### **Invoices for supplies before 1 July 2000**

A document issued before 1 July 2000 for a supply post 1 July 2000 needs to show:

- > your name or trading name
- > your address
- > date of issue
- > the price of the taxable supply (ie that part of the supply relating to post 1 July 2000)
- > the amount of GST included in the price of the taxable supply (or a statement that the "price of taxable supply includes GST")

Where you have (or will) pay for subscriptions, memberships etc which span 1 July 2000, you should set these aside. You will then need to determine which of these invoices do not meet the requirements set out in the ATO Ruling for pre-1 July 2000 invoices and seek to obtain a compliant invoice in the interim, or request that a tax invoice be provided during the first tax period.

To avoid this additional administrative requirement you may consider withholding any payment of the proportion attributable to GST unless an invoice can be provided which will allow you to claim an input tax credit.

### **Supplies of goods or services that span 1 July 2000**

The intention of the legislation is to ensure that any transactions which span 1 July 2000 should fall either under the Wholesale Sales Tax regime, or under the GST system, not both. You should note that where you have stock on hand as at July 1, 2000 you will be entitled to a special credit for the amount of sales tax included in the rest of that stock. You:

- > can claim the credit in any BAS lodged prior to 22 January, 2000
- > MUST be requested as at 1 July, 2000 to qualify for the special credit
- > MUST do a stock take as at 30 June, 2000 and calculate the sales tax based on that stock take

The following table explains the treatment of certain transactions across numerous scenarios such as where:

- > an invoice is issued and consideration received prior to 1 July 2000. Delivery takes place on or after 1 July 2000 - GST liability arises
- > an invoice is issued prior to 1 July 2000. Delivery takes place and consideration is received on or after 1 July 2000 - GST liability arises
- > delivery takes place prior to 1 July 2000. An invoice is issued and consideration is received on or after 1 July 2000 - NO GST liability
- > delivery takes place and an invoice is issued prior to 1 July 2000. Consideration is received on or after 1 July 2000 - NO GST liability
- > supplies are made on a progressive or periodic basis spanning 1 July 2000. Consideration is received in advance; and GST arises according to the proportion of services provided after 1 July 2000
- > supplies are made on a progressive or periodic basis spanning 1 July 2000. Consideration is made on a progressive basis. Cash accounting: record as cash received. Accruals: apportion services to each tax period.

A few examples may serve to clarify the different rules which apply under the ANTS (Goods and Services Tax Transition) Act 1999.

Commonly, payments (consideration) for goods and services will not occur until after either delivery of the goods, or at least receipt of an invoice.

#### **EXAMPLE**

In late May 2000, Bagryana orders brochures to be printed for her arts and crafts store. The brochures are delivered within a week with an invoice stating that Bagryana has 90 days to pay.

**Result:** As delivery has taken place before 1 July 2000, the supply of the goods will not give rise to GST liability. It does not matter whether Bagryana pays for the brochures before or after 1 July 2000.

Generally speaking, supplies that are paid for prior to 1 July 2000 may be deemed to have been made on or after 1 July 2000 if the actual supply takes place on or after that date.

**EXAMPLE**

On 29 June 2000, Warren decides to order 10 new seats for his theatre company. An invoice is issued, and Warren pays for the seats on that day, however he arranges to have the chairs delivered to the theatre on Sunday 2 July.

Under the GST regime, as the invoice was issued and consideration received prior to 1 July 2000, but the supply of the goods was to take place after 1 July 2000, the payment made prior to 1 July 2000 will be subject to GST.

Result: the full amount of consideration received for the supply will be subject to GST. This amount of GST will be included in the supplier's GST return for the tax period starting 1 July 2000. Warren can claim an input tax credit for 1/11th of the price.

**What does your accounting system need to do?**

A GST-compliant accounting system will need to enable some or all of the following:

- > identification and isolation of both GST to be accounted for (often referred to as the "output tax") and *input tax credits* as separate line items, to be netted off at the end of the relevant *tax period* (note that the *Business Activity Statement* does not require these to be identified in the accounting system but instead requires details of gross revenues and expenses)
- > attribution of output tax and *input tax credits* to the relevant *tax period*
- > recognition of the GST status of supplies made or received (that is, *taxable*, *GST-free*, *input taxed*) and separate compilation of transactions of each type. It may also be necessary, for example, for different types of *GST-free* supplies to be identified
- > adjustments for increases and decreases in output tax and *input tax credits* respectively in later *tax periods*. (Note that the *Business Activity Statement* requires the amounts of *consideration* for discounts, etc where they are granted by suppliers in a period subsequent to the original supply)
- > adjustment of *input tax credits* based on 'changes in use' of acquisitions over time

In this regard, while it is assumed that a computer based system will probably be used, it should be noted that this is not absolutely essential. Many countries in Europe, amongst others, implemented a GST/Value Added Tax system long before the use of computers became widespread. As will be noted from the review of the basic accounting concepts below, it is entirely feasible to achieve the required result without using a computer program. However, as a minimum you should probably ensure that you are running a cash payments and cash receipts book

## Accounting on an accruals basis

Despite the fact that most of the GST-related transactions will be computer-based, it is important that those responsible for administration understand the accounting mechanics - *the debits and credits* - underlying GST recording in order to have a true understanding of what it is all about.

Double-entry bookkeeping is founded on the financial equation:

<b>Assets - Liabilities = Owners Equity</b>
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*GST payable* is a liability (the amount collected from customers).

An *input tax credit* is an asset (or receivable), being the amount paid to suppliers for business inputs and recoverable from the ATO where such an entitlement arises.

In order to ensure ease of completion of the *Business Activity Statement* four basic GST balance sheet clearing accounts are recommended:

- > **GST payable clearing account** - this account should be used to record the entity's GST liability to the ATO (this account has a CR<sup>Δ</sup> nature)
- > **GST receivable clearing account** - this account should be used to record the entity's input tax credit entitlement (this account has a DR<sup>†</sup> nature)
- > **GST payable adjustment clearing account** - this account should be used to record the reduction in the entity's GST liability where the related GST liability arose in a *prior tax period* (this account has a DR nature)
- > **GST receivable adjustment clearing account** - this account should be used to record a reduction in the entity's input tax credit entitlement where the related input tax credit entitlement arose in a *prior tax period* (this account has a CR nature)

Some common journal entries for a GST registered business accounting on an accruals basis have been summarised in the examples below. These are only suggested entries as the treatment of GST in the accounts is currently under investigation by the Urgent Issues Group of the Australian Accounting Research Foundation, and some businesses may have a preferred method of accounting for GST.

Note: The following example journal entries are for accruals-based accounting only and assume that all the transactions occur in the same tax period unless otherwise stated.

Δ Credit (CR): Accounting term used to generally describe the situation where a business records income or a liability in their accounting records. For example, a business will "credit" their income account when they make a sale and they will "credit" a liability account when they take out a loan. Therefore, a GST liability account is a credit account as it represents money owed to the tax office.

† Debit (DR): Accounting term used to generally describe the situation where a business records an expense or an asset in their accounting records. For example, a business will "debit" an expense account when they purchase stationery and they will "debit" an asset account when they purchase a motor vehicle. Therefore, an input tax credit ("GST receivable") will be a debit account as it represents money owed to you (and as such represents an asset).

**Example 1: GST sale with discount given for early payment in the same period**

If there is a sale of goods on credit for \$110 inclusive of GST, the journal entry for this transaction would be as follows:

**JOURNAL 1A**

SALE			
Accounts Receivable	Dr	\$110	
Sales Revenue	Cr		\$100
GST Payable Clearing account	Cr		\$10

Assuming that you give a 10% discount if the payment is made within 14 days, and the purchaser pays within 14 days, they will then be entitled to the 10% discount and this will result in a reduction of the GST inclusive sale price by \$11 to \$99.

**JOURNAL 1B**

10% SALE DISCOUNT			
Cash at Bank	Dr	\$99	
Discount Allowed	Dr	\$10	
GST Payable Clearing account	Dr	\$1	
Accounts Receivable	Cr		\$110

Therefore, the GST payable will be reduced to \$9 (that is, the GST Payable Clearing account CR of \$10 less the GST Payable Clearing account DR of \$1)

**Example 2: GST sale where item is returned in the same period as the related sale**

Again, assume a sale is made for \$110 as in Journal 1A above, and the customer returns the goods because they are faulty. The entry to reverse the sale is shown below:

**JOURNAL 2**

SALE RETURN			
Sales Returns	Dr	\$100	
GST Payable Clearing account	Dr	\$10	
Accounts Receivable	Cr		\$110

**Example 3: GST sale on credit which is subsequently written off as a bad debt**

Assume there is a sale on credit as per Journal 1A and you make the decision to write off the debt in a subsequent GST period. (Note: You can only write off the debt for GST purposes if it has been outstanding for more than 12 months.) The entry to reverse the original entry is shown below:

**JOURNAL 3**

BAD DEBT WRITTEN OFF			
GST Payable Adjustment Clearing Account	Dr	\$10	
Bad Debt Expense/ Provision for Doubtful Debts	Dr	\$100	
Accounts Receivable	Cr		\$110

**Example 4: Purchase with discount received for early payment in the same period**

If you purchased goods on credit for \$110 inclusive of GST, the journal entry for this transaction would be as follows:

**JOURNAL 4A**

PURCHASE			
Purchases	Dr	\$100	
GST Receivable Clearing account	Dr	\$10	
Accounts Payable	Cr		\$110

Assuming that the supplier gives you a 10% discount if the payment is made within 14 days, and you pay within 14 days, you will then be entitled to the 10% discount and this will result in a reduction of the GST inclusive sale price by \$11 to \$99.

**JOURNAL 4B**

10% PURCHASE DISCOUNT			
Accounts Payable	Dr	\$110	
GST Receivable Clearing account	Cr		\$1
Discount Received	Cr		\$100
Cash at Bank	Cr		\$99

Therefore, the net GST payable by you and hence your GST Receivable Clearing account will be reduced to \$9 (that is, the GST Receivable Clearing account DR of \$10 less the GST Receivable Clearing account CR of \$1).

**Example 5: Purchase where the item is returned within the same period as the related purchase**

If you purchased goods on credit, then found that the goods were faulty and returned them to your supplier, the entry to reverse the purchase would be as follows:

**JOURNAL 5**

PURCHASE RETURN			
Accounts Payable	Dr	\$110	
GST Receivable Clearing account	Cr		\$10
Stock	Cr		\$100

Note that when transactions occur that relate to the events that occurred in a prior tax period, (for example, sales returns or purchases returns occurring this period but the original sale or purchase occurred in a prior tax period), you will be required to account for the adjustment in the GST Payable Adjustment account or GST Receivable Adjustment account. That is, you must not net off the adjustment against the current period's GST Payable Clearing account and the GST Receivable Clearing account.

If you are unclear regarding the procedure required, you should consult further with your accountant.

## Dealings with the Australian Taxation Office (ATO)

This section will cover the procedures and forms for dealing with the ATO.

### The Australian Business Number (ABN)

The Australian Business Number or *ABN* is a new 11 digit identifier which will not replace your Tax File Number (TFN) but will eventually be used for all your dealings with the ATO and for future dealings with government departments and agencies at all levels

To apply for an ABN, you must be either a company or an entity carrying on an enterprise. Employees, hobbyists and individuals who are conducting activities without a reasonable expectation of profit cannot register for an ABN. This means that the ATO can determine whether people are really independent contractors when they apply for the ABN.

You will be required to display the ABN on various stationery you use in carrying out your business, including specifically, your *tax invoice*, and other items which will be outlined by the ATO when decided.

You may like to consider as a transitional measure, printing your next order of stationery with both your ACN and ABN so that you will not have to destroy stationery on 1 July 2000.

### ATO endorsement of organisations having tax deductible and tax exempt status

Legislation enacted by the Federal Government as part of The New Tax System includes the Registration of Deductible Gift Recipients and Income Tax Exempt Charities (ROGATE).

A deductible gift recipient is an entity to which gifts are deductible to the donor. A tax exempt charity is one that is exempt from income tax.

### Deductible Gift Recipients (DGR)

On 1 July 2000, the tax deductibility status of organisations will lapse unless they are mentioned by name in the *Income Tax Assessment Act 1997* or are endorsed by the ATO as a deductible gift recipient.

To be a deductible gift recipient, an organisation will be required to:

- > have an Australian Business Number
- > have a gift fund for its principal purpose. All gifts to the organisation for that purpose must be placed in that fund as well as any money received by the organisation resulting from the gifts. No other money or property must be placed in the fund
- > use the gift fund only for its principal purpose
- > the instrument establishing the organisation or rules governing its activities must state that any surplus assets of the gift fund are to be transferred to another tax deductible recipient if the gift fund is wound up or if the organisation ceases to be endorsed by the ATO as being a tax deductible recipient

## Tax exempt status

Similar provisions also apply in relation to the endorsement of tax exempt charities. To be endorsed, organisations must have an ABN and be able to satisfy the existing criteria for tax exempt status.

### How to apply

The application form for an Australian Business Number includes a section asking whether you are a gift deductible recipient or tax exempt. If you answer yes, the Australian Tax Office will forward to you the additional forms to be completed for your application for gift deductible or tax exempt status.

## Charitable Institutions

A charitable institution is exempt from income tax.

An 'institution' has been described as an establishment, organisation or association, instituted for the promotion of some object, especially one of the public utility, that is religious, charitable, educational

The word 'charitable' has a technical legal meaning. 'Charitable' does not simply mean that a person is generous or one is kind or lenient in one's attitude towards others.

An organisation will be considered 'charitable' only if its main purpose falls within one of the following:

- > the relief of poverty
- > the advancement of education
- > the advancement of religion
- > other purposes beneficial to the community

### Relief of poverty

The main object of the organisation must be to provide relief of poverty, sickness, destitution or helplessness. Examples of relief include providing food directly to the needy and providing food, clothing or money to victims of a natural disaster.

- > St Vincent de Paul/Smith Family/Meals on Wheels
- > Meals on Wheels
- > hospitals and auxiliaries
- > disaster relief organisations
- > overseas aid organisations
- > refugee welfare centres
- > refuge and crisis centres
- > drug education or rehabilitation centres

### **The advancement of education**

As well as the examples given under public educational institutions above, charitable institutions for the advancement of education include:

- > Parents & Citizens or Parents & Friends associations
- > Scouts, Cubs, Girl Guides, Brownies and similar organisations

Examples of non-exempt institutions include:

- > associations of former pupils of a particular school

### **The advancement of religion**

As well as the examples given under religious institutions above, charitable institutions for the advancement of religion include:

- > organisations established to build or maintain a building of worship
- > organisations established to provide stipends to the clergy

### **Other purposes beneficial to the community**

The main object of such organisations must be for the benefit of the community. It includes a wide range of activities such as:

- > providing public facilities eg. libraries, swimming pools, museums
- > providing public utilities eg. roads, bridges

Examples of exempt institutions include:

- > public art galleries, museums and libraries
- > bodies which protect animals or preserve historic buildings
- > rescue organisations, such as bush fire brigades and surf life saving clubs
- > organisations which promote the health of women
- > organisations which educate the public about a particular disease
- > organisations which provide community or neighbourhood facilities

Examples of organisations which are not charitable institutions for other purposes beneficial to the community include:

- > development corporations
- > resident groups
- > social and cultural clubs
- > progress associations which conduct significant political or lobbying activities

## The Business Activity Statement (BAS)

The ATO has introduced a new reporting form called the *Business Activity Statement* or BAS. The BAS will allow you to report not only your GST but other tax obligations and entitlements.

The BAS will ultimately record the net amount payable to the ATO or refunded to you or offset against any other obligation you may have. The BAS will report your business tax entitlements and obligations, including the amount of GST you have paid and the amount of GST you have collected. It will reduce the number of times artists to report your business tax obligations to the ATO for many arts administration and artists.

The **BAS is the single form** you fill in and return to the ATO as a tax return on:

- > GST
- > income tax withheld
- > income tax instalments
- > deferred company income tax instalments
- > FBT
- > Wine Equalisation Tax
- > Luxury Car Tax

The structure of the BAS allows any GST amounts payable or refundable to be offset against other non-GST taxation liabilities recorded in the BAS for the same period. This would tend to minimise the cash flow consequences of having to wait up to 14 days for the payment of any refund from the ATO.

**In order to calculate the GST component for your BAS** (the GST you have to pay and how much input tax credit you are entitled to), you will need to record the following:

- > total sales and income and other supplies made
- > export sales
- > other *GST-free* supplies made
- > *input taxed supplies*
- > acquisitions and importations
- > acquisitions for making *input taxed* sales and income and other supplies
- > estimated private use of acquisitions and importations

Briefly, **the records you need to keep** (you need to keep these for 5 years) to help you to fill in the BAS include:

- > cash register tapes (if you do daily summaries you only have to keep these for a month - see the ATO's record keeping booklet)
- > records of cash sales
- > invoices issued and obtained
- > investment distributions
- > creditors and debtors lists
- > details of payments to other entities from which you are required to withhold tax
- > details of goods for own use

In addition to the above, you may need to keep records of the **change in use of assets** if they are used for making *taxable or GST-free* supplies on the one hand and *input taxed supplies* on the other hand.

## Lodging your BAS

The BAS must be lodged no later than the twenty-first day of the month following the end of your *tax period*. The first lodgement dates will be 21 August 2000 for a monthly lodger or 21 October 2000 for a quarterly lodger.

There is scope for you to change the end of a *tax period* to align with your current accounting practices by ending your *tax period* either seven days earlier or later than when your *tax period* would otherwise end. It should be noted, however that this does not change the requirement for you to lodge your BAS return by the 21st of the month following.

All registered entities may choose to lodge returns and make payments electronically.

However, registered entities with an *annual turnover* of \$20 million or more are required to lodge all returns and make all payments electronically, unless it is accepted that it is not practical to do so.

All refunds paid by the ATO will be done electronically. Accordingly when filling out the ABN application form, applicants will be asked to provide bank account details.

## ATO ruling agenda

As may have already been apparent, there are various areas of the GST legislation which remain unclear or require a degree of fine-tuning. To this end, the ATO has provided a ruling agenda in order to give an indication of when they will be in a position to provide the 'answers'. A copy of this is available on the ATO's tax reform website: [www.taxreform.ato.gov.au](http://www.taxreform.ato.gov.au).

There are a significant number of rulings yet to be finalised some of which include:

- > adjustment events
- > interaction between FBT and GST
- > treatment of appropriations and grants by governments

A copy of the current rulings program is shown at the end of this workbook. Also included is a list of rulings or draft rulings which have been or will be released. A number of these were released on 22 and 24 December 1999, including:

- > recipient created invoices
- > the margin scheme for suppliers of real property held prior to 1 July 2000
- > attributing GST payable, input tax credits and adjustments

Businesses will also be able to seek private rulings from the ATO. GST ruling GSTR 1999/1 outlines the operation of the GST ruling system.

## Contracts and transitional arrangements

All businesses should be aware that entering into any dealings that span the introduction of GST may produce GST consequences. Essentially, the tax legislation prescribes certain rules to apply where any contracts or ongoing supplies involve the receipt or delivery of a particular good or service on or after 1 July 2000.

As a general rule, the intention is that any dealings that span the implementation date should fall either under the existing indirect tax system or under the GST system.

Relevant Dates	
<b>2 DECEMBER 1998</b>	the date that the legislation was introduced into Parliament
<b>8 JULY 1999</b>	the date that the legislation received Royal Assent
<b>29 JULY 1999</b>	the date for a reduction in the WST on certain items from 32% to 22%
<b>1 JULY 2000</b>	the date from which the GST will become operative and WST will be abolished
<b>1 JULY 2005</b>	the date from which the transitional provisions will cease, affecting reviewable contracts with no prior review opportunity and non-reviewable contracts signed prior to 8 July 1999

Royal Assent (the date on which the Governor General passed the law) occurred on 8 July 1999. As a result, any party entering into a contract after that date will be deemed to have intended the GST consequences.

**Therefore, if the contract is silent in relation to GST, the pricing in the contract is taken to be GST-inclusive.**

As the obligation to account for GST rests with the supplier, the supplier could end up out of pocket with no ability to recover the GST paid from the purchaser. GST only needs to be accounted for in relation to most supplies of goods or services made after 1 July 2000.

### EXAMPLE

Your current fee for a particular service is \$100.00

If you supply the service after 1 July 2000 and do not include GST in your charge after 1 July 2000, rather than receiving \$100.00, you will receive \$100.00 from the client but you will be liable to GST of 1/11th, i.e. \$9.09. For example:

Current Price	\$100.00
GST content	\$9.09
<b>Net result</b>	<b>\$90.91</b>

To include GST, you would need to invoice your customer for \$110.00 and remit \$10.00 to the ATO. This would result in the same net return to your business of \$100.00.

To avoid unintended consequences and perhaps substantial losses to your business, it is advisable to collate all of your contracts into a Contracts Register, distinguishing between contracts that were signed:

- > before 2 December 1998
- > between 2 December 1998 and Royal Assent (8 July 1999)
- > after Royal Assent (8 July 1999)

Businesses should have all long-term contracts reviewed to determine any exposure to unforeseen, and in some cases, unrecoverable, GST on present and forthcoming transactions. If you are in any doubt, it is essential that you consult with a competent GST adviser.

You will probably find that your business will have costs, such as rent and insurance, which are supplied on a progressive basis, and span a period which straddles 1 July 2000.

Your business will be entitled to an input tax credit for the GST portion of the payment which relates to the period from 1 July 2000 if you obtain a *tax invoice* from the supplier (see earlier comments on the form of the *tax invoice*).

As you are only entitled to claim *input tax credits* where you have a proper *tax invoice*, it is imperative that you request one from your suppliers before you claim the *input tax credit*. The supplier must provide a tax invoice within 28 days of receiving your request.

## Policy for new contracts and arrangements

Any contract or arrangement entered into after 8 July 1999 will have GST implications where that contract or arrangement operates after 1 July 2000. Where a supply is to be made after 1 July 2000, you will need to take steps to ensure that GST is appropriately provided for in these arrangements. This will include inserting an appropriate GST clause in the documents evidencing these contracts and arrangements.

The risk of having to account for GST, should nothing be done to address the issue, lies with the vendor (or supplier) of the goods or services forming the subject of the contract. If the vendor does not provide itself with the ability to recover the GST from the purchaser, for every \$100 increment under a current contract, the vendor will have to account for \$9.09 to the ATO and will only receive the net amount of \$90.91.

Where contracts and arrangements include clauses under which remuneration, commission or *consideration* is based on sales turnover, these contracts will need to identify whether or not that turnover figure is the GST-inclusive or GST-exclusive amount. (An important area to note here is royalties. Contracts will need to be clear as to whether the royalty payment or receipt based on sales revenue is based on the GST inclusive sales figure or GST exclusive.)

This seemingly minor calculation can have enormous profitability consequences if not addressed appropriately. Put simply, a contract which calculates a commission based on turnover figures, may provide the recipient with an increased amount if the turnover figure is GST inclusive. Where both parties are registered for GST purposes, a royalty based on GST inclusive sales would mean an increased receipt by the payee (who would then be liable to GST on the receipt) and on increased payment by the payer (who

would then be entitled to an Input Tax Credit on the payment). The net effect in this case would be NIL.

#### EXAMPLE

**Pre-GST:** Juan is entitled to a royalty of 25% on ticket sales for his play. The Vagabond Theatre sells \$1,000 worth of tickets. Juan is entitled to \$250.

**Post-GST:** Juan is entitled to a royalty of 25% on ticket sales for his play. The Vagabond Theatre sells \$1,100 worth of tickets. Juan is paid \$275 (being 25% of \$1,100). Juan is liable for \$25 GST (being 1/11th of \$275) leaving him with \$250 in the hand. The Theatre is registered for GST and is liable for GST of \$100, less \$25 in GST paid to Juan. The Theatre is left with \$1,000 "in the hand".

#### Motor vehicles - input tax credit (ITCs) issues

It has been suggested that the *price* of a new car is expected to drop due to the introduction of GST.

Prior to GST, most new cars attracted sales tax at the rate of 22% on the wholesale value of the car (equivalent to a tax on the retail value of about 17%). The same principles apply to trucks, detachable trailers for prime movers, and specialised truck bodies.

The GST will be applied to the retail value of the car at a rate of 10%, therefore providing a reduction in *price* of approximately 7%.

Used cars, purchased through private transactions and not through a registered dealer, are outside the scope of the GST regime, as such a sale would not comply with all of the requirements for it to be a *taxable* supply. However, if the purchase is made from a dealer who is registered or required to be registered, the car will be subject to GST and the dealer will be entitled to a notional *input tax credit* on the price paid for any second hand cars.

If purchased from a business that has used the vehicle in its business, they will be liable to GST on the sale and can therefore be expected to include GST in their sale price.

There are special *transitional provisions* relating to the purchase of new cars to dissuade businesses from deferring motor vehicle purchases. Due to these provisions, businesses will not be entitled to an *input tax credit* on a new motor vehicle purchased before 1 July 2001. Further, businesses will be only entitled to 50% of the *input tax credit* on a new motor vehicle purchased on or after 1 July 2001 and before 1 July 2002.

The restrictions on obtaining *input tax credits* on new motor vehicles falls away with effect from 1 July 2002. Thereafter, only the normal rules governing the availability of *input tax credits* will apply.

These provisions do not apply to businesses which were previously entitled to purchase vehicles exempt from sales tax. These businesses will be entitled to a full *input tax credit* on the purchase of any new motor vehicles acquired on or after 1 July 2000.

**EXAMPLE**

Leon runs a gallery. On 30 November 2000, he purchases a new vehicle for \$33,000 for use in the gallery business. The GST included in the cost of the vehicle is \$3,000. Leon is not entitled to an input tax credit for the \$3,000 GST as he purchased the vehicle between 1 July 2000 and 30 June 2001.

On 20 September 2001, Leon expands his business and purchases another vehicle for \$33,000. The GST included in the cost of the vehicle is \$3,000. Leon is entitled to an input tax credit for 50% of the GST included in the price, that is, \$1,500, because he purchased the vehicle between 1 July 2001 and 30 June 2002.

If the car is used for non-business/ private purposes, the input tax credit must be reduced to take that proportion into account.

**Leases and hire purchase agreements**

This is a complex area and still subject to some uncertainty as to the precise treatment as the law is in the process of clarification.

Generally payments made by way of a hire fee or a lease will be subject to GST. Accordingly a car lease will attract GST. However, for a hire purchase arrangement, GST will be charged according to the value of the vehicle, but not on the finance charge.

**Wholesale sales tax on trading stock**

The ATO has released a Draft GST Ruling on the *special credit* available for wholesale sales tax (WST) paid on trading stock on hand as at 1 July 2000 (GSTR 1999/D3).

Essentially an enterprise is entitled to the *special credit* if it is registered at 1 July 2000 and has on hand goods that have been acquired or imported and held for the purposes of sale or exchange in the ordinary course of business, ie it applies to what would normally be regarded as trading stock.

**To be eligible for the special credit an entity MUST BE REGISTERED AS AT 1 July 2000**

The *special credit* does **not** apply to:

- > secondhand goods (generally), that is, goods that are not new or have been previously used such as demonstration goods or used plant and equipment
- > certain alcoholic beverages
- > consumable goods such as office stationery or cleaning rags as they are not generally held for the purposes of exchange and are not stock on hand
- > goods on consignment

The basis for the *special credit* must be lodged in a BAS/GST return before 22 January 2001, ie a return covering a *tax period* not later than the one ending on 31 December 2000.

There are two ways of ascertaining the amount of the *special credit*:

- > identifying the amount of WST borne on the quantity of goods from stock records or other source documents
- > calculating the amount of WST by identifying the WST inclusive cost of the goods purchased in Australia or the WST and *customs duty* inclusive cost of the goods imported into Australia and knowing the rate of WST applicable to these goods

It should be noted that, in ascertaining the WST inclusive cost price, any costs upon which WST was not charged should not be taken into account. Any adjustments to WST due to discounts, rebates and returns should be taken into account and an amended GST return lodged if necessary.

It is clear that in order to calculate the *special credit* as described above, businesses will need to keep sufficient records to identify the quantity of stock on hand at the start of 1 July 2000 and the WST borne on those goods. These records and any calculations or other documentation supporting the method of calculation for the *special credit* must be kept for a period of at least five years. If sufficient records have not been kept, or if the amount of WST borne in respect of goods otherwise cannot be readily ascertained, the following methods of calculation may be used:

- > **where the business acquires goods from a retailer and the invoice does not show the amount of WST**, the enterprise can calculate the WST included in the purchase price by estimating the taxable value on which tax would have been charged as being 50% of the total purchase price
- > **where an enterprise operates a mixed retail business with a turnover of less than \$5 million and with a wide range of stock items**, the enterprise can calculate a percentage of the total value of purchases made over a 13 week period that has borne WST at different WST rates. These percentages are then applied to the total value of stock on hand at the start of 1 July 2000

## Pricing

With the introduction of GST, it will be necessary for your arts business to ensure that your major stakeholder groups (suppliers, customers, contractors etc) are kept fully informed of how you intend to deal with the introduction of the GST and the processes you will be using to deal with any required changes. Of course the same goes for businesses dealing with you agents, material suppliers,

Under the GST:

- > there will be no sales taxes charged to customers or suppliers
- > cost reductions may be passed on by suppliers because they will save on sales tax and other indirect taxes
- > you will pay GST on goods and services supplied to you and you will seek to charge GST in your *prices*

## Dealing with suppliers

It is very important for the ongoing success of your arts business that you pay the correct amount for your supplies and are able to claim back the correct amount of GST (*input tax credits*) from the ATO.

When buying supplies for your arts business, you need to sort all transactions into taxable supplies and *GST-free* or *input taxed supplies* in order to:

- > identify the items that have GST included in the *price* so that you can claim *input tax credits*
- > monitor prices on items where GST is not paid

You will notice that after the introduction of the GST, many of the *prices* you pay for supplies should change. This is one of the reasons why you need to be aware of which of your supplies should include an amount for GST, so that you pay a fair *price* and do not pay any GST on *non-taxable* items.

You must also ensure that you receive the correct documentation from your supplier so that you can claim the correct amount of *input tax credits*. The main source document you will need will be the *tax invoices* which you must obtain from your suppliers.

*Tax invoices* can only be given by registered businesses.

If any of your suppliers are not registered, you will not be able to claim any *input tax credits* for supplies you buy from them (they will not have charged you any GST, but would not have received input tax credits for GST charged to them). Therefore, you may find that obtaining your supplies from that particular supplier becomes relatively more expensive. Your options are to either:

- > ask them to register so that they can charge you GST (and you can claim input tax credits on their business purchases) and then give you *tax invoices*
- > choose another supplier who is registered and negotiate a *price* for your items with them

When you are considering whether or not to deal with an unregistered supplier you may need to consider the impact that the PAYG provisions may have. Where a supplier cannot quote an ABN you may need to withhold amounts from your payment to them. This will create further administrative costs for your business.

Before negotiating prices with your suppliers, it is important to know how the prices of your supplies are being adjusted taking into account not just the GST, but the other tax reforms such as the removal of wholesale sales tax. It is possible that your suppliers' costs will go down (after allowing for any input tax credits) and those savings should be passed on to you.

You may wish to send a letter to your suppliers to place them on notice of the fact that you will require appropriate documentation from them, and you understand that they should be making savings which they should be passing on to you. In the arts sector these sort of letters can help to make more aware of the need to get ready for GST!

This information on the degree to which savings may become available, may be obtained from the body that represents the industry you work in, the professional who prepares your accounts or does your legal work, or through other publications that list expected price increases or decreases.

## Dealing with customers and pricing decisions

Once you identify and group your transactions into the three basic types of supplies - *taxable*, *input taxed* and *GST-free* - you can work out where GST will apply. The next step is to analyse your business transactions in order to determine your *prices*. GST is not as simple as merely adding 10% to your current prices.

You will still need to analyse your costs, review your margins and consider any other market forces or pressures. While you may require your suppliers to identify how they will be sourcing and passing savings on to you, you may well find that your customers engage in a similar process with you.

If you are in a market where consumers will not tolerate a price increase and the cost of your inputs go up, you may have to take a decrease in your margin, alternatively, you may have to be prepared to explain to your customers how your prices are being set.

Your customers will be affected differently by GST and it is important that you are aware of how GST will affect them so you can anticipate how demands may change during the transition to GST.

Your customers who are registered for GST purposes may be able to claim as *input tax credits* the GST component of the *price* charged by you.

Unregistered customers will not be able to claim *input tax credits*. Therefore different pricing strategies may be necessary depending on who makes up your customer base.

When you supply goods and services to other GST-registered businesses, you will need to provide a *tax invoice* to support the transaction. Without a *tax invoice*, your registered customer will not be able to claim back the GST built into your *price*.

To maintain client relationships, arts businesses would be well advised to:

- > ensure all of your brochures, publications and price lists (including on Internet sites) are updated to show a GST inclusive price, (for ACCC purposes you must advise the final price). You should advise your clients that you are registered and the price includes GST
- > take a proactive stance in educating your customers - do not wait for them to go to a competitor. If your business client does not understand that they can claim a credit for the GST you have included in the price, they may make decisions which will adversely affect you
- > share unique aspects of the GST for your sector of the arts industry with your customers; and
- > ensure your staff are trained to understand and handle any GST issues or inquiries which may arise, especially those staff who are responsible for entering into contracts, or otherwise dealing with customers. This may be as simple as ensuring that staff get a tax invoice for any expenses over \$55 (GST inclusive) they incur and for which you reimburse them

The value of some goods and services is expected to change as a result of the GST and the New Tax System. Therefore, credit limits and trading terms that you currently have in place with both your customers and suppliers will need reviewing to represent both the price changes and the addition of GST. The main steps involve:

- > analysing costs, you may get some Input Tax Credits - an apparent increase in costs may end up being a decrease
- > reviewing margins, the ACCC will let you maintain, but not increase your net dollar value
- > considering market pressures ie, how your customers will react to changes in your selling prices

You are required by law to review your cost base for the goods and services you supply, taking into account the abolition of wholesale sales tax.

On that reviewed cost base, you will be adding your current dollar, NOT percentage, dollar mark-up, and to that new value for your goods and services you will be adding the 10% GST. **Your cost base to which you add 10% GST does not include the GST included in the price you paid for acquisitions or inputs.**

#### EXAMPLE

You are a local theatre group and are registered for GST. Pre-GST, the price charged by you for a theatre ticket was \$20. The \$20 was made up of \$15 production costs, with a \$5 mark-up to go towards maintenance of the theatre and other costs of the theatre group.

Post-GST, production costs are \$14, due to the savings after the abolition of wholesale sales tax. You do not include GST on production costs in your calculations, as that GST you pay will give you an input tax credit for the same amount, so is not actually a cost to you.

To generate the same cash in hand at the end of the production, the dollar mark-up of \$5 is added to the new production costs with a new total of \$19. You add GST of 10%, and your new ticket price is \$20.90

If registered for GST, you will have to include GST in your published prices, although the GST component need not be separately identified. For example, the cost of a ticket may be described as \$66 includes GST of \$6, or simply as \$66 includes GST.

## What if you are not registered for the GST?

### EXAMPLE

You are a local theatre group and are not registered for the GST. Pre-GST, the price charged by you for a theatre ticket was \$20. The \$20 was made up of \$15 production costs, with a \$5 mark-up to go towards maintenance of the theatre and other costs of the theatre group.

Post-GST, production costs are \$14, due to the abolition of wholesale sales tax. However, you will be paying 10% GST on these costs. As you are not registered, you do not receive input tax credits for this GST, and your total production costs become \$15.40. You add your dollar mark up of \$5, and your new ticket price is \$20.40. You do not add any GST to this price. You are not registered.

NOTE: These examples are fictitious, and give no real indication of what costs are likely to be for any given organisation whether they register for GST or not. These examples do give you the process through which you must work in order to assess the real implications for your practice or organisation.

## Compliance with ACCC guidelines

The intent of the ACCC pricing guidelines is to ensure that consumers gain the full benefits of tax reform. To do this, the ACCC will monitor prices both before and after the introduction of the GST to provide information on price movements.

The ACCC guidelines generally require that there must be no unnecessary price increases and that the benefits of tax reform are to be passed on to consumers as they occur. If your prices need to increase, any rises should be no greater than necessary to maintain your margin.

The ACCC will be vigilant against "price exploitation", that is, a price for a supply which they consider to be unreasonably high having regard to the changes brought about by The New Tax System. At their website, you can find further guidelines on these matters: [www.accc.gov.au](http://www.accc.gov.au)

The ACCC can impose significant fines on a business that takes unfair advantage of the transition to GST. Anyone engaged in the offence of 'price exploitation' during the three year transitional period commencing 1 July 1999 will be liable to penalties up to \$10 million for corporations and \$500,000 for individuals.

It is very important for all businesses to give due consideration to the effect of GST and other tax reforms on current prices. **A wise practice would be to begin keeping written records detailing your pricing decisions and the reasoning behind them in order to be able to justify these to the ACCC, if ever required to do so.** If you work on an annual subscription then you will only have to record this once a year.

**A brief summary of what the ACCC expects is that you:**

- > make price reductions as soon as you identify savings and pass on the
- > full benefit of indirect tax reductions to consumers
- > must take full account of indirect tax reductions when increasing (GST inclusive) prices
- > do not put any mark-up on GST component of prices
- > reflect only actual tax increases in prices
- > do not use the move to GST to increase net dollar margins

While bearing in mind the role that the ACCC is taking, one should be clear that they are not trying to prevent you enhancing your profitability as part of the normal business process. They are merely tasked with ensuring that margins are not increased by businesses using GST as an excuse to do so unfairly.

## Employee-related expenses

This section deals with employee related expenses, allowances and reimbursements.

### Employees

Salary and wages are not subject to GST. Therefore, there is no GST liability or input tax credit entitlement arising from the payment of salaries and wages.

Salary and wage earners are not carrying on an enterprise under The New Tax System. Therefore, if you are an employee, you are not eligible for an ABN or registration for the GST for activities for which you receive a salary or wage.

#### EXAMPLE

Dom is a lighting designer employed part time by Arcadia Opera. At the same time, Dom undertakes casual lighting work with other companies. Dom is both an employee, of Arcadia Opera, and an individual carrying on an enterprise, with the other companies. With respect to his work with Arcadia Opera, Dom is not eligible to apply for an ABN or to register for GST, and there are no GST obligations or entitlements. However, in his work for other companies, Dom is an individual carrying on an enterprise. For his non-salaried or contract work, Dom is entitled to receive an ABN and to register for GST.

### Contractors

If you contract artists and other people who are registered for GST to perform work for you, they will include GST in their contract price, and will issue you with a tax invoice. You will be entitled to input tax credits for GST they have included in the price for their services.

#### EXAMPLE

The Winery Jazz Festival contracts a jazz band to provide services at its festival. The band charges the festival \$660, including \$60 GST, per day. The band gives the festival a tax invoice for \$1,980 for the three days. GST of \$180 is payable by the band to the ATO. The festival can claim input tax credits for the \$180 GST included in the price of the band hire.

NOTE: In order to provide a tax invoice, either the band as a partnership is registered for the GST, or one band member may be registered. He or she then is the only one contracting with the festival, but then separately contracts with his or her unregistered fellow band members. Musicians need to give careful consideration as to how they are going to manage their contractual relationships under The New Tax System, particularly in relation to their liability in respect of any work undertaken by them as a member of a group, and in relation to potential impacts on their current income tax arrangements.

## Reimbursements

You are entitled to input tax credits for GST included in reimbursements you make to employees for expenses they incur that are directly related to their activities as your employees. The employee must obtain a tax invoice when the goods and services are purchased and give it to you so you are entitled to the input tax credit.

Note: A tax invoice is not required where the GST inclusive price of supplies is less than \$55. However, you should retain documents as required to validate the expense, for example, petty cash vouchers and bank statements.

The employee is not entitled to the input tax credit, as the GST was paid by him or her in the course of employment, and GST and entitlement to register does not apply to activities for which salary or wages are paid.

But what happens if you are reimbursing the costs of someone who is not an employee?

### EXAMPLE

The River Blues Festival has been supported for years by the volunteer work of a dedicated local, Rhonda. Rhonda has always coordinated staging, accommodation, catering, builders, and many of the other housekeeping tasks essential to the Festival's success. For years, the Festival has always made a payment to Rhonda as a contribution to her costs. The payment has never been specifically allocated to costs incurred by Rhonda personally, and is unlikely to actually cover the total of those costs in any event.

Rhonda is not on the books as an employee of the River Blues Festival.

If Rhonda is a contractor, then the payment made by the Festival, even though merely as reimbursement for costs, and even if these costs were formally substantiated, would be a payment to a contractor and would be subject to PAYG withholding unless Rhonda provided the Festival with her ABN.

However, it may be that Rhonda has in fact been acting as an agent of the Festival. The best option may be to give Rhonda the formal authority to act as an agent on behalf of the Festival with respect to the tasks and contracts she has always carried out. All invoices she receives and expenses incurred within the extent of that agency would be expenses incurred by the Festival. As Rhonda does not receive payment for her services, the PAYG withholding would not apply.

The Festival may consider making Rhonda an employee, but in that case there would be legal requirements in relation to salary, worker's compensation and superannuation at least that would need to be addressed.

NOTE: The ATO is considering the position relating to the reimbursement of volunteers rather than agents or employees.

## Pay As You Go (PAYG)

From 1 July 2000, a new Pay As You Go (PAYG) system will replace the Pay as You Earn (PAYE) system and other withholding tax arrangements. The objective of the PAYG system is to reduce business tax compliance costs by:

- > aligning payment dates for the various taxes that business pay
- > allowing business taxpayers to make just one tax payment per quarter
- > combining the existing tax withholding systems into a single system

The new PAYG system is comprised of:

- > a **PAYG withholding system**, which will replace the existing Prescribed Payments System (PPS) and Reportable Payments System (RPS) as well as other withholding arrangements, (for example, non-resident withholding, TFN withholding)
- > a **PAYG instalments system**, which will replace the current provisional tax and company instalments systems
- > running balance accounts as a method of determining taxes owing so that taxpayers can receive a single statement which tallies their net tax paying, or tax refund, position in respect of their entire taxation liabilities

## PAYG Withholding system

The PAYG Withholding system brings all the previous withholding tax requirements together under the one system.

This includes replacing the existing PPS, RPS systems and PAYE systems.

Under PAYG, the situations where tax must be withheld are generally the same as those under the existing systems, however, in addition to these, there are 3 new situations where withholding is required:

- > a contract worker, who has an ABN, enters into a voluntary agreement with another entity, whereby payments made to the worker will be subject to withholding; as if the payments were salary and wages
- > a payment is made to a worker from a labour hire firm for the worked performed directly for a client of a labour hire firm
- > payments of an invoice where no ABN is quoted on the invoice. (Note the withholding tax for this situation is set at 48.5%)

Payments made to entities who have an income tax exempt status, that is, the income they receive will be exempt from income tax, are not required to quote an ABN and will therefore not be subject to the 48.5% withholding.

The following examples demonstrate the serious impact of the new PAYG regime impact on art practitioners who go from job to job. These examples are based on people who are carrying on a business but do not have an ABN:

- > You are a dramaturg with a theatre company and you have invoiced them for your fee of \$1,000. If you don't supply an ABN, the theatre company is required to withhold \$485 PAYG tax from your fee.
- > You are a writer or composer who has entered into a publishing agreement where you are entitled to \$100 royalties. If you do not supply an ABN the publisher will be required to withhold \$48.50 from the payment.
- > You are a multimedia artist who has succeeded in obtaining government funding of \$100,000 for a project. Without an ABN, the funder is required to withhold tax of \$48,500.
- > You are a band performing at a local venue for a fee of \$500. Unless the band provides an ABN number, 48.5% must be withheld by the venue operator.
- > You are an artist, successfully selling out your first solo show for a total of \$6,000. The Gallery will deduct its usual commission of 30-40% of sales, and then, because you don't have an ABN, withhold a further 48.5% of the gross payment leaving a total of \$1,200 or less.

## PAYG Instalments system

Individuals and entities with business or investment income will pay PAYG either quarterly or annual instalments. The PAYG system will mean businesses will pay tax on income in the tax period that they earn it. The amount of tax you will have to pay each PAYG instalment will be ordinary income you have derived in the quarter multiplied by your instalment rate.

$$\text{Your income for quarter X Instalment Rate supplied by Commissioner} \\ = \text{Instalment payable}$$

The instalment rate given by the ATO will be calculated by dividing your tax payable last year by your gross income last year (both adjusted for items such as capital gains and tax losses). The business income will be your ordinary income for the quarter such as gross sales, gross interest, gross rent etc, but will not include any capital gains.

### EXAMPLE

John operates as an arts consultant and earned \$70,000 business income in 1999/2000 income year. Based on this income he paid \$25,000 tax to the ATO in 1999-00. For the first quarter of the 2000-01 income year, John earns \$20,000 business income.

The ATO has calculated John's instalment rate as 35.7143% - this is determined by dividing \$25,000 tax from last year by \$70,000 income from last year. To calculate John's business tax liability at the end of the first quarter in 2000-01, the following calculation is required: \$20,000 business income for the quarter multiplied by 35.7143% instalment rate = \$7,142.86.

You can use your own instalment rate instead of the one given by the ATO but you may be liable for penalties if the rate is underestimated.

Note: The ATO has stated in its PAYG Factsheets that if you do not receive an instalment rate, you will not have to pay PAYG instalments.

PAYG instalments will be paid quarterly (21 October, 21 January, 21 April and 21 July), except where an election is made to pay annually. The first three payments have been extended by three, two and one weeks respectively.

The **only circumstances** in which **quarterly instalments** are **not required** are if you:

- > are not registered or required to be registered for GST (and are not in a partnership that is registered or required to be registered for GST)
- > your most recent notional tax as notified by the ATO is less than \$8,000

If you are excluded from compulsory quarterly instalments you can choose to pay one annual instalment on 21 October following the income year end (or you can still pay quarterly if you wish). An equivalent time is allowed if you or your company has a substituted accounting period.

## Calculation of Annual Instalments

If you only have to pay annually, the instalment is based on last year's income. From the 2002-2003 year, the due date for this payment will be 21 October after the end of the financial year. Until then, the dates that currently apply of no earlier than 1 April within the income year (for existing provisional tax) and 15 December after year end (for existing company tax) will continue to apply.

## Calculation of Quarterly Instalments

If you have to pay your own tax quarterly, the new system includes a fundamental change in the way in which your income tax instalments will be calculated compared to the current system.

Instalments will generally no longer be based on the previous year's income tax or the use of uplift factors. Nevertheless, an option exists in certain limited circumstances to apply a system based on past tax uplifted according to gross domestic product (GDP) changes.

Instalments will be calculated by multiplying your "instalment income" for the relevant quarter by either:

- > an ATO advised instalment rate calculated according to a prescribed method. You will not be liable to pay quarterly instalments unless you have received a written notice from the ATO advising you of your instalment rate
- > an instalment rate that you determine. However, to use your own instalment rate you must notify the ATO of the rate in an approved form. Penalties apply if your instalment rate is less than 85% of the benchmark rate that should otherwise have been used

Your 'instalment income' is the gross ordinary income you actually derive during a quarter to the extent that it would be assessable in the income year in respect of which the instalment is paid. This basically means your income according to ordinary concepts such as your sales income (regardless of whether the sales were subject to GST or not, but excluding any GST amount) and any interest, dividend or rental income you derive. The ATO will normally determine your instalment rate by the ratio of your notional tax (see above) to your instalment income for the most recent income year.

You will be able to vary your instalments in certain circumstances on a self-assessment basis in the same way that you can currently vary provisional tax instalments. For example, if your business circumstances change significantly so that the ratio of tax to sales for the most recent income year would not be an appropriate measure of your current liability, or you incur significant one-off or non-recurring expenditure, that means the normal tax ratio may be too high. However, penalties will apply if you are too far out in your estimate.

### Company payments under the new system

The new instalments regime applies to the 2000-2001 and later income years. However, transitional rules exist for companies to phase-in the new system and bring forward the timing of payment under the existing company instalment system to ensure that the 1999-2000 income year is the last year for which that system applies.

For a company that qualifies as a "small"<sup>1</sup> company, income tax will be paid on average nine months earlier than under the current system. To phase this change in, one full year's tax, due under the existing system on 15 December 2000, will be deferred so that it is paid in interest-free instalments over five years.

For a company that qualifies as a "medium"<sup>2</sup> company, tax will be paid eight months earlier than under the current system. Without phasing-in, the company's 1999-2000 tax would have to be paid at the same time as its 2000-2001 tax instalments. To phase this change in and prevent cash flow problems, the 3rd and 4th instalments for the 1999-2000 income year, and part of any outstanding balance, will be deferred so that they are payable in interest-free instalments over five years.

For a company that qualifies as a "large"<sup>3</sup> company, tax will be paid five months earlier than under the current system. Without phasing-in, one instalment would still be due under the existing system after the first payment is made under the new PAYG system. To phase this change in and prevent the company having to pay tax for the current year and the previous year at the same time, the 4th instalment for the 1999-2000 income year (but not including any outstanding balance) will be deferred so that it is payable in interest-free instalments over two and a half years.

<sup>1</sup> "Small" company means income tax payable for the last year is less than \$25,000.

<sup>2</sup> "Medium" company means income tax payable for the last year is between \$25,000 and \$1 million.

<sup>3</sup> "Large" company means income tax payable for the last year is greater than \$1 million.

## Fringe Benefits Tax (FBT)

The Federal Government has announced its intention to ensure neutrality of treatment between fringe benefits and cash salary following the introduction of GST.

The major change to the FBT system as a result of GST will be the increment to the gross up factor. The new gross up factor includes GST and has been set by the ATO at 2.129189 (compared with 1.941748 prior to GST).

In order to avoid allowing GST input tax credits for goods and services purchased by employers for the private use of employees, a new GST-inclusive gross up will be introduced. The new gross up will effectively recover the input tax credit that was obtained by an employer in providing a fringe benefit.

The new gross up factor does not apply in all situations. Businesses should refer to the following table to determine which FBT gross up factor should, in most cases, be used.

Existing FBT gross up factor (1.94178)	New GST-inclusive FBT gross up factor (2.129189)
To be used where input tax credits are not available for the items purchased	To be used where input tax credits are available for the items purchased

### EXAMPLE

Joe is employed by a company that makes only taxable supplies. As such, assets that it acquires will be subject to GST, but it will get a full input tax credit. Joe's company car is to be replaced in September 2002, his employer gets the input tax credit if it purchases the car.

The FBT gross up factor to be used is 2.129189.

## Cash flow: implications associated with the introduction of GST

### Remitting GST to the ATO and claiming input tax credits

Cash management is an important issue for all businesses. There are varying levels of understanding of the impact of the introduction of GST, particularly with respect to cash flow and timing issues associated with providing remittances to the ATO. These are critical issues that require understanding of the implications particularly with respect to the points listed below.

#### Cash flow is affected because:

Debtors increase by GST / Creditors increase by GST:

- > Debtor collections earlier than the GST payment boost cash flow
- > Debtor collections after the GST payment deplete cash flow
- > Creditor payments earlier than the GST payment deplete cash flow
- > Creditor payments after the GST payment boost cash flow. Where the business is registered to account for GST on a "cash" basis, the cash flow implications of the introduction of GST are not as significant

#### Care needed on 'accruals accounting basis':

If your business operates on a tight cash flow, particularly where you use loan capital to provide your working capital requirements, and you account for GST on an invoice (accrual) basis rather than on a cash basis, you will need to be particularly wary of the impact of GST on your cash flow.

This impact in regard to cash flow can arise in one of two ways:

- > If your business sells its goods or services for **cash**, while having creditors for the supply of the goods and services you buy, you will benefit by the additional cash flow provided by the GST you are required to collect. This is because you will be holding (GST) cash on supplies made for a period of time before you will be required to remit it to the ATO.  
On the purchase side, you may be in a position that you can claim the GST input tax credit from the ATO before you have paid the GST to your creditors.
- > If, however, you sell goods or services on credit terms, which extend beyond the date upon which you are required to account for GST, but you purchase goods or services for cash, or on short creditor days, your cash flow could be negatively impacted by the imposition of the GST. This is caused by having to pass on the net GST to the ATO before much of it is collected from your debtors.

**Choice of 'tax period' can give savings:**

If your annual turnover is less than \$20 million, it may be preferable to adopt the three-month GST period at the point of registration. If your business is likely to be cash flow positive as a result of the GST, this will create an opportunity for you to temporarily reduce your bank overdraft or increase cash funds.

Exporters and other significant suppliers of GST-free goods and services who are likely to be regular net GST refund receivers, on the other hand, may prefer to opt for the monthly GST period in order to access those refunds from the ATO as quickly and as frequently as possible.

Many importers could receive a cash flow boost at the start of the GST as goods importation costs affected by high WST rates will benefit from the abolition of the WST and replacement by the GST, which can be recovered as an *input tax credit*.

**Risk of using GST cash:**

In a number of overseas countries, many smaller businesses succumbed to the temptation of accessing any additional available cash arising from the GST output tax (to be remitted to the ATO) being temporarily held in their cash reserves.

If these cash funds are committed to long term capital expenditure or used for some other purpose, the business may be exposed to cash availability problems at the next due date for GST return filing and payment remittance. This is particularly likely to occur with small businesses that rely heavily on the state of their bank balance to give them an indication of their financial status.

A particular risk arises where subscriptions, season tickets or memberships are sold before 30 June 2000 and GST is collected in the payment for the whole period, but is not required to be remitted until 21 October 2000 (for a quarterly BAS lodger).

Policies should be instituted in your arts business to ensure that this type of cash management practice does not occur. Businesses, which work from the basis of their bank balance to determine their funds available, are more likely to fall into this trap and should be particularly wary.

**Working with credit cards:**

An important part of your cash management procedure is going to be dealing with the debit and credit card organisations. This is because of the lapse between when a transaction is entered into and payment is made by way of credit card, and when payment is actually received from the credit card organisation.

If you do not plan for this, you may be accounting for GST long before it is actually received. This being the case, it is important that you consider the option of offering discounts for cash.

It is essential that you establish what effect the introduction of GST will have on your cash flow and plan your response accordingly.

**Cash flow implications under an accruals accounting regime:**

- > consider tax planning strategies
- > undertake financial modelling
- > review cash flow forecasting techniques
- > renegotiate payment terms
- > systems must report financial results on a timely basis
- > discuss with your banker if you are using loan finance for working capital

**Information technology system requirements**

All businesses will need to ensure that their accounting systems and computer systems are GST compliant and will be ready by 1 July 2000.

The system used will need to be able to apply GST to the income streams, which are subject to GST, and capture the information required to claim *input tax credits* on purchases and expenditure. This will require the capability to flag and differentiate between *input taxed*, *GST-free* (and within this, *GST-free exports*) and *taxable* supplies.

It should be noted that unlike the Y2K programs where 'fixes' can be implemented with immediate effect, and then left in the system, most changes required by GST will necessitate that they only 'go live' with effect from 1 July 2000. This is further complicated by the requirement that adequate records need to be kept in the lead up to 1 July 2000 for transactions which span 1 July 2000 and, therefore, attract the operation of the *transitional provisions*.

In addition, all computer systems must be upgraded (where necessary) to include fields such as the Australian Business Number, and changes to invoicing and receipting forms and procedures.

For entities with a turnover of less than \$10m, a full write-off of the cost of upgrading computer systems is available where the upgrade was for the purposes of being GST-ready and the expenditure was incurred before 1 July 2000. For all businesses though, a \$200 voucher will be provided when you register for GST. This is available for use in upgrading computer equipment or obtaining GST advice.

## Information systems analysis

For each type of transaction or process affected by GST, the following questions need to be answered to obtain a satisfactory knowledge base for planning and managing changes to information systems. Given the limited time remaining to amend IT systems, such a review is of primary importance. Factors for you to consider include:

- > what process steps are undertaken to enable this type of financial transaction, what is the sequence, and what types of data flows between the steps?
- > what information systems are used to enable these process steps and what is the role of each system in each step?
- > what additional data needs to be captured during the overall process to satisfy GST accounting and reporting requirements (external and internal reporting) and at what step(s) in the process should this data be captured?
- > what decisions need to be made with respect to the technical risks, skills availability, costs, required timing, and change management implications associated with changing existing systems versus building new systems?
- > what protocols and formatting standards need to be observed for the transfer of information from IT systems to the ATO?
- > what test plans, scripts and data will be required to adequately test the efficacy of the changed and new IT systems, as well as the communication channels between the various systems (both internal and external systems)?
- > are training version(s) of the affected IT systems required, to enable effective training of planned users of the systems prior to "going live"?

## Training

As part of the ongoing implementation of GST, internal staff will require training tailored to their individual business functions and operational needs. For example, certain people will need to be trained in invoicing and pricing procedures to ensure consistency of recording for GST purposes, whereas others will need a more in depth knowledge of the workings of the GST if they are required to negotiate contracts with suppliers and customers.

Due to the dynamic nature of the GST and other tax legislation and the fact that it is likely to undergo further changes over at least the next six months, (as well as being subject to a variety of new Regulations and Rulings), there will need to be a process in place for the continuous education of managerial, operational and support staff in the new GST environment.

Such training will be necessary not only in the period leading up to 1 July 2000, but also on an ongoing basis after this initial startup date, and when new staff are engaged. It is advisable to organise training for all staff who are involved in the processing of statements, issuing letters of settlement, accepting invoices and quotations for work, purchase orders and other instruments of business correspondence. It is vital that staff thoroughly understand the GST compliance requirements of documentation of the business, its suppliers, clients and intermediaries.