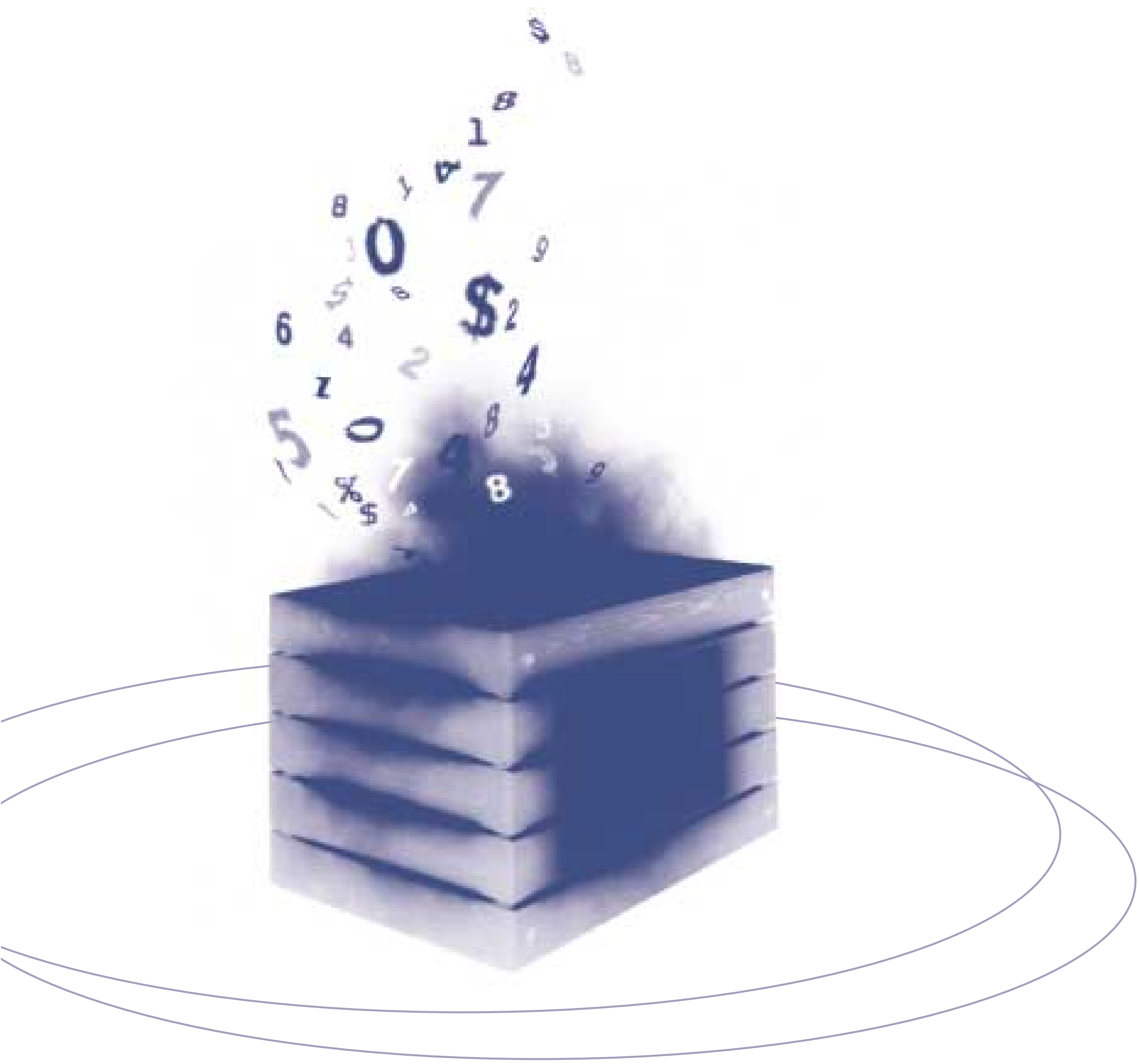
Australia Council for the Arts

case studies



GST Start-Up Assistance Office

practical tax case studies for the arts sector

INTRODUCTION

The Goods and Services Tax (GST) is a reality and commences operation on 1 July 2000.

However, there are many issues you must consider before the start date to ensure you are adequately prepared for the changes The New Tax System will make to your activities.

Things you should consider include:

whether you are required to register for GST or should register voluntarily

how GST will affect the prices you pay for materials and services

how GST will impact on the prices you charge for your output

whether your accounting system can deal with GST

how GST will affect your cash flow

These case studies, developed with funding from the Federal Government's GST Start-Up Assistance Office, aim to help you with the decisions you need to make. Many artists and arts organisations helped to create these case studies. However, each study is a composite and none is a specific example.

GST Overview

GST is a 10% tax imposed on the *supply* of goods and services made by a *registered person or business* in the course of carrying out an *enterprise*. GST is also imposed on the importation of goods.

When a registered person makes a supply of goods or services, the GST levied will be 1/11th of the consideration for that supply. The GST that is collected from the client/customer is to be remitted to the Australian Taxation Office (ATO). If a person is unregistered, they will not be liable for GST on the goods or services that they supply.

On the other side, if a registered person purchases goods or receives a service, input tax credits will generally be allowed for GST included in the consideration paid. These input tax credits will be offset against the GST to be remitted to the ATO and only the net difference has to be paid to the ATO. (If the input tax credits exceed the GST collected, an entitlement to a refund arises).

In this way, GST is not a tax paid by businesses, only by final users (ie unregistered businesses or individuals). However, the issues raised regarding cash flow and pricing are all business questions that you need to address.

While an analysis of a normal chain of commercial transactions might normally assume that all parties to the series of transactions are registered (except for the end-user), the situation is very different in the Arts sector, and much more complicated. For example, the artist might or might not be registered for GST, and the same could apply for the artist's suppliers. The artist's customers too could be unregistered individuals, or they could be registered businesses.

The case studies that follow give examples as to how GST will impact upon artists in many different situations. Other discussions address specific areas, such as the treatment of grants and donations. You may find that while none of the case studies exactly matches your circumstances, some aspects from each case study are relevant. These case studies have been designed so that you can draw upon examples from all 15 to create a scenario tailored to your arts business.

Enterprises and Registration

GST law refers to *enterprises* rather than to types of entities. An enterprise is an activity or series of activities in the form of a business or in the nature of a trade. Private recreational pursuits and hobbies are excluded from the definition of enterprise and are, therefore, not included.

Any enterprise with an annual turnover of $50,000 or more ($100,000 for non-profit organisations) must register for GST. An enterprise with a turnover below these levels may **choose** to register, but is not **required** to do so.

If you are in a position where registration is voluntary (ie your turnover is less than $50,000 per annum), the decision to register should be made after considering how registration will affect your cost structure, the prices you are able to charge for your outputs, the impact upon your cash flows, and the costs of complying with GST.

These case studies will help you and give you guidance in making such decisions.

1. Australian Business Number (ABN)

An integral part of The New Tax System is the introduction of the *ABN,* a new identifier for all dealings with the government.

In order to register for GST, you must have an ABN. However, if you do not have to register for GST (ie your turnover is less than $50,000 per annum), you can still apply for an ABN.

From 1 July 2000, a supply to a business where the supplier does not quote an ABN will mean the payer is required to withhold 48.5% income tax from the payment. Although this will be credited in the supplier's income tax return, it is still a significant cash drain on a business.

To avoid having tax withheld from payments, you need to either quote an ABN or provide a written statement that the supply was made in the course of undertaking a hobby activity. If you take the latter approach, you may have difficulty justifying any income tax deductions claimed in your tax return concerning those hobby activities.

2. Cash or Accruals? Monthly or Quarterly?

Once registered for GST, it is necessary to decide if you will adopt the *cash* or *accruals* method of accounting. You also need to determine whether you will lodge GST returns on a *monthly* or *quarterly* basis. These decisions can have a significant impact on the cash flow of your business.

The cash method means you remit GST in respect of supplies made for which payment has been received. Similarly, input tax credits are available for purchases that have been paid for. The cash method is available for businesses with a turnover of less than $1 million per annum.

Businesses with a greater turnover than that **must** adopt the accruals method. Under the accruals method, you account for GST on sales or acquisitions made during the GST period, even if you have not paid for them or received payment. Therefore, if you make a credit sale, there is a chance that you will have to account to the ATO for GST collected before the customer has settled their account. This can place pressure on business cashflow, especially if customers are slow to settle their accounts.

Businesses with a turnover of less than $20 million can lodge their GST returns on a quarterly basis. This reduces the time involved in completing GST returns. In addition, it allows the business the use of GST collected until it needs to be remitted. This can mean up to 111 days free credit, where a cash sale is made on the first day of the GST period. A monthly GST return will be required by the ATO where the taxpayer does not have a good history of tax compliance.

3. Grants

The ATO has issued a public ruling on GST treatment of grants made by both government and non-government bodies. To understand the application of GST to grants, it is necessary to see the grant as being the consideration paid for the supply of something by the grant recipient. That is, the recipient of the grant is making a supply to the grant payer.

The supply in this case may be the grant recipient undertaking to spend the grant funds in a particular way in order to further the objectives of the grant payer. Alternatively, the obligation to report to the grant payer as to the use of the funds, or to give acknowledgment of the receipt of the grant in connection with any works produced or published, may constitute the supply for which consideration (ie the grant) is given.

Usually the grant payer will be registered for GST purposes. However, GST treatment is dependent on the registration status of the grant recipient.

If the grant recipient is registered for GST, the supply will be a taxable supply and, therefore, 1/11th of the grant will be the GST portion remitted by the registered grant recipient to the ATO. The registered grant payer would obtain an input tax credit for GST and be entitled to a refund from the ATO. Therefore, for registered grant recipients, it will be possible to "gross-up" a grant by GST payable, so that the recipient has the same net amount as before. The recipient may be subject to GST on items purchased, but could obtain an input tax credit for any such acquisitions.

With non-registered recipients, the grant will not be subject to GST. Therefore, the payer would not gross-up the amount (as they could not get an input tax credit). The non-registered recipient would still be charged GST on any acquisitions made from registered suppliers. However, no input tax credit would be available to the non-registered recipient, so the net value of the grant would be reduced accordingly.

4. Compliance Costs

With most of the individual case studies, there is a brief breakdown of some of the expenses and income sources that are typical for practitioners in a variety of artistic fields.

However, the case studies do not take into account the cost of compliance with GST. GST requires a disciplined approach to conducting business, and accurate accounting records need to be kept. Many commercially available software packages can deal with GST. However, many small arts businesses may find it necessary to purchase a computer to keep their accounts on, buy or upgrade their accounting software, or hire a bookkeeper or accountant to assist them in the day to day GST compliance factors. These issues must be considered when deciding whether you should register for GST, if that is an option for you.

In many instances, the cost savings of The New Tax System may be eroded by the increased cost of compliance.