Quote of the month

"If it's a good idea, go ahead and do it. It is much easier to apologize than it is to get permission."

Admiral Grace Hopper

What did I miss? 1 July changes

- GST applies to digital products & services imported by consumers
- Small business $20k instant asset write-off extended until 30 June 2018
- Company tax rate reduction to 27.5% for entities with an aggregated turnover of less than $25m (companies with a turnover of less than $10m have been subject to this tax rate since 1 July 2016).
- Major Bank Levy introduced
- 2% temporary debt tax removed from high income earners
- Plant & equipment deductions limited for residential property investors (not yet legislated)
- Residential property investors no longer able to claim travel expenses (not yet legislated)
- First home saver scheme begins (not yet legislated)

Superannuation reforms come into effect:

- Cap on concessional contributions (before tax) reduces to $25,000 for everyone.
- Cap on non-concessional contributions (after tax) reduces to $100,000.
- $1.6 million transfer balance cap limits how much money a member can transfer into or hold in a tax-free pension account. Excess amounts are subject to a transfer balance tax.
- Threshold to access the tax offset for contributions to a spouse increased to $37,000 (partial offset available up to $40,000).
- Threshold for low income super tax offset increased to $37,000.
- The threshold at which high-income earners pay Division 293 tax on their concessionally taxed superannuation contributions reduced to $250,000 (from 300,000).

GST on imports: new rules for goods under $1,000

Last month, Parliament passed legislation that will see GST applied to all consumer imports regardless of their value. Currently, imports below $1,000 are excluded from GST.

The perceived preferential treatment of internet shopping has been a contentious issue for a while with the retail sector lobbying hard to ensure that where a business is benefiting from sales to Australian consumers, the purchase is taxed in the same way as local retailers.

While the start date of the change has been pushed back until 1 July 2018, businesses importing goods into Australia will need to review their position to check whether supply chains are affected and determine which entity is actually liable for the GST. Australian businesses that purchase low value goods from overseas should also check to make sure that overseas suppliers are not imposing GST on supplies of these goods unnecessarily.

The new rules are intended to apply to situations that are not captured by the existing GST importation rules because the goods are worth $1,000 or less. The rules are designed to only apply when goods are delivered to Australian consumers who are either not registered for GST in Australia or where the goods do not relate to an enterprise or business being carried on in Australia. If your business imports goods into Australia and is registered for GST, the tax should not apply to low value goods you import.

GST applies where the supply is to an Australia consumer – it doesn't matter who makes the purchase. So, you could have the scenario where GST applies to a gift purchased for you by an overseas relative if the gift is shipped directly to you.

Where goods are purchased through electronic platform providers, such as Amazon, eBay or Alibaba, responsibility for collecting the GST will rest with the platform provider as they manage the customer billing on behalf of the supplier. However, it will be more difficult for the Government to force foreign companies to comply with the new rules leading to concerns about the costs of the administration required to enforce GST on low value goods.

For overseas suppliers, if the value of goods sold into Australia is greater than $75,000 per annum, the entity is required to register for GST. However simplified options are available for those that only export to Australia and have no need to claim tax credits in Australia.

Generational succession: Do your kids really want to take over your business?

Generational succession - handing your business across to your kids or family – sounds simple enough. But, many families end up in dispute right at the point when the parents, business, and children are most vulnerable. It's important that generational succession is managed as closely and diligently as if you were selling your business to a stranger to avoid misunderstandings and disputes – you need to make sure that everyone understands what the transition will mean and everyone is aware of their role and responsibilities.

If you are looking to hand your business to your children or relatives, there are a few key issues for you to think about:

Capability and willingness of the next generation – do your kids really want the business?

There needs to be a realistic assessment of whether or not the business can continue successfully after the transition. In some cases, the exiting generation will pursue generational succession either as a means of keeping the business in the family, perpetuating their legacy, or to provide a stable business future for the next generation. All of these are reasonable objectives, however, they only work where there is capability and willingness.

The alternative scenario can also exist where generational succession is pursued by the younger generation. In some cases, it's seen as their birthright. In these cases the willingness will exist but this does not automatically translate to capability.

In either case, the answer needs to be 'yes' to all of the following:

1. Is the next generation willing and sufficiently committed to take on the responsibility of the business?
2. Do they have the capability to operate and run the business?
3. Can the capital value of the business be maintained and enhanced over time under their management?

Capital transfer – how much money needs to be taken out of the business during the transition?

What level of capital do the current business owners, generally the parents exiting the business, need to extract from business at the time of the transition? The higher the level of capital need the greater the pressure that will be placed on the business and the equity stakeholders.

In the majority of cases, the incoming generation will not have sufficient capital to buy out the exiting generation. This will require the vendors to maintain a continuing investment in the business or for the business to take on an increased level of debt. Either scenario needs to be assessed for its sustainability either at the business or shareholder level.

In many cases the exiting generation will want to maintain a level of equity investment. This might be a means of retaining an interest in the business or alternatively staging their transition. In either case, it is important to map out the capital transition both from a business and shareholder perspective. This needs to be documented and signed off firstly from the business's perspective and then by both generational groups. No generational transition should be undertaken without a clear and agreed capital program.

Income needs – ensuring remuneration is on commercial terms

In many SMEs, the owners arrange their remuneration from the business to meet their needs rather than being reasonable compensation for the roles undertaken. This can result in the business either paying too much or too little. Under a generational succession there should be an increased level of formality around compensation to directors and shareholders. Compensation should be matched to roles and where performance incentives exist these should be clearly structured.

The compensation for all executives should be agreed at a business level first. Thereafter, all of the parties can assess the adequacy of the compensation to their needs and expectations.

Operating and management control

Once the capability and capital assessments have been completed, it is important to look at the transition of control. This can be a very sensitive area. It's essential to establish and agree in advance how operating and management control will be maintained and transitioned. This is important not only for the generational stakeholders but also for the business. Where uncertainty exists around management and decision making there is likely to be either confusion or a vacuum - either will adversely impact the business. Tensions easily arise because:

- The incoming generation want freedom of decision making and the ability to put their imprint on the business
- Without operating control they feel that they have management in name only
- The exiting generation believe that their experience is necessary to the business and entitles them to a continued say
- A perception that capital investment should equate to ultimate operating control
- An uncertainty by either or both generations about the extent of their ongoing roles

The plan for operating and management control should be documented and signed off by all of the parties with either timelines for time driven succession or milestones for event focussed transitions.

Transition timeframes and expectations

Generational succession is often a process rather than an event and achieved over an extended period of time. This is quite different to a sale of business where the owner's active involvement in the business generally ceases shortly after sale. The extended timeframe for the transition requires active management to ensure that there are mutual expectations and to avoid the process being derailed through frustration.

The exiting generation may have identified that they want to scale down their business involvement and bring on other family members to succeed them. This does not necessarily mean that they want to withdraw completely. An extended transition period is not uncommon and can often assist the business in managing the change. This can also work well in managing income and capital withdrawal requirements.

The critical issue here is to identify and ensure that all of the parties have a common understanding and acceptance of the time period over which the transition will take place. This should be included in the documented succession plan.

The need for greater formality and management structure

Generational succession often requires a greater level of formality in the management and decision making process. This formality should achieve a separation of function between:

- Management;
- The Board of the company; and
- Shareholders.

Often in a SME business these roles merge and there are no clear dividing lines or boundaries. Roles, responsibilities and clear key performance indicators (KPIs) for management should be agreed and documented. For management, this needs to include clear job descriptions, authority levels and operating expectations.

Generally, a more formal and functioning board of Directors is required. The process may also be assisted by the inclusion of non-related, non-executive Directors. They should assist to provide some balance between the two generational groups. Where there is a functioning Board, they should meet on a regular basis and receive and direct management in the strategic direction of the company.

Managing and maintaining family relationships

A key component of generational succession is the ability of the parties involved to separate business issues from family relationships. Understandably, this can be problematic and requires a significant amount of discipline by the participants. Leadership in this discipline needs to be provided by the exiting generation.

Business tensions and differences in view about the direction of the business, and certain management decisions can bring significant pressure to bear on normal family relationships. The roles of grandparents and parents need to be kept separate as much as possible from the roles of fellow Directors and Shareholders. While these aren't business issues, they are significant issues in a generational succession. Ultimately, any breakdown in family relationships will have some impact on the business.

The material and contents provided in this publication are informative in nature only. It is not intended to be advice and you should not act specifically on the basis of this information alone. If expert assistance is required, professional advice should be obtained.