Tel: (08) 9444 9711
Web: www.infocusaccounting.com.au

IN THIS ISSUE

ARE YOU A BASE RATE ENTITY? IS THAT ALWAYS GOOD?

As the old saying goes, cash is king. One way for companies to hold onto more cash is to qualify as a Base Rate Entity ("BRE") which reduces the company's tax rate from 30% down to 25%.

On the face of it this appears to be a great concession for smaller companies, however this is not always the case.

A company qualifies as a BRE in a particular income year if ***both*** of the following requirements are met:

1. the aggregated turnover of the company for the income year is less than $50 million (from the 2019 income year onward); and
2. ***no more than*** 80% of the company's assessable income for that income year is Base Rate Entity Passive Income (BREPI).

An entity's aggregated turnover is the sum of the entity's annual turnover, any connected entity's annual turnover and any affiliate's annual turnover. An entity's annual turnover for an income year is defined as ***the total ordinary income that the entity derives in the income year in the ordinary course of carrying on a business***.

An important point to note in respect to the second requirement is that the test is based on "assessable income" and not taxable or net income.

What constitutes BREPI is limited by legislation and can be summarised as:

- corporate distributions (e.g. dividends) other than non-portfolio dividends;
- franking credits on corporate distributions;
- non-share dividends;
- interest income;
- royalties and rent;
- net capital gains;
- gains on qualifying securities; and

- amounts included in assessable income of a partnership or trust, to the extent that they are referable (directly or indirectly) to a category of base rate entity passive income listed above.

If an amount of assessable income does not fit the above criteria it is not BREPI, and therefore it is essential to understand the nature of the income.

By way of example, a business that leases out equipment is receiving income that is classified as royalty income for BREPI purposes. If the company sells the equipment and makes a taxable profit on the sale, that taxable profit is not BREPI as it is neither royalty income nor is it a capital gain.

Whether a company qualifies as a BRE is tested each year and can lead to a company having different tax rates if differing years. As the year progresses it can be prudent to test whether the company will be a BRE in the current year in order to plan for tax position based on the expected tax rate, which may be higher than the previous year.

Qualifying as a BRE has consequences that extend further than the company's income tax liability.

A company's franking rate for dividends is based on its corporate tax rate in the previous year. If the company did not exist in the previous year then the franking rate defaults to the BRE tax rate. The changes in tax rates can cause misalignment between the tax paid on the company's profits, and the franking credits that are attached to the dividends when those profits are paid to shareholders.

Where historical tax rates were 30% but the franking rate is now 25%, it's possible that franking credits get stuck inside the company with no retained profit available to pay them out. Conversely, where historical tax rates were 25% but the franking rate is now 30%, the company may not be able to payout the retained profits as a fully franked dividend, which could be an issue for any foreign shareholders.

For those companies looking to utilise the refundable Research & Development Tax Offset, the rate of the offset is dependent on the company's tax rate. The refundable offset rate is 18.5% plus the company's tax rate in the year of the claim. Therefore, if the company is a BRE in the year of the claim then its refundable offset rate will be 43.5%. If the company was not a BRE its refundable offset rate will be 48.5%. Depending on the size of the R&D claim the cashflow impact could be significant.

Overall, being a BRE is seen to be a positive due to the additional cash that can be retained in the company. However, particular attention needs to be paid to the current year's assessable income as the BRE status changes year on year and lead to unintended outcomes.

If you would like to discuss this matter further, please contact Andrew Lowry or Leonard Tebbutt on 08 9444 9711.

TAX DUE DILIGENCE – SELLING YOUR BUSINESS

If you are considering the sale (or purchase) of a business, be that through a share sale or a business asset sale you need to consider whether pre-sale tax planning is required ***before*** a Terms Sheet or Heads of Agreement is signed.

For business owners who could qualify for the Small Business Concessions, being able to meet the numerous basic conditions, as well as the specific conditions required based upon the asset being sold and the concession sought to be claimed, doesn't often happen by accident.

Having an understanding of the following matters even before a sale is contemplated is vital in ensuring the sale process is structured correctly and for Vendors, the process is as tax effective as it can be:

- Have you determined whether the Net Asset Value of the Vendor and their associated entities is less than $6 Million?
- Will the Business Entity qualify as a CGT Small Business Entity having turnover either this year or last year of less than $2 Million?
- If the Vendor is a Company or the vendor is a shareholder in a Company, are there or have there been any Class shares on issue?
- Where the Vendor is a Shareholder, have you tested the Active Asset Percentage of the Company for at least half the period the shares have been held?
- Where the Vendor is a Shareholder, have you confirmed that the Company itself is valued at less than $6 Million?
- Is the Company the subject of an Interposed Entity Election?

Whilst the receipt of the Terms Sheet usually starts the formal due diligence process, discussing your succession plans with us so we can actively assist you in ensuring that your business interests are in the best shape possible to minimize the tax payable on what could be your last pay day is vitally important.

Ensuring that a discussion on succession becomes part of every client meeting is a good way to ensure that can get a head start in the pre-sale process and can either advise or assist in any pre-sale planning or restructuring BEFORE it is too late.

Some recent matters that we are aware of that would have benefited greatly by some pre-sale planning include:

- The sale of shares in a Company where it was later found an Interposed Entity Election had been made for that Company;
- The sale of shares in a Company where it had previously held excess cash on deposit such that it failed the 80% Active Asset test in some prior years;
- The sale of Shares in a Company that had a G Class shares held by a former shareholder still on issue, even though they had never been utilised;
- The sale of Business Assets in July 2024, when the business turnover for the 2024 year was above the $2 million SBE qualification threshold, yet turnover was below $2 million in the 2023 financial year; and

- The sale of Business Assets rather than shares where most of the Purchase Price was allocated to Plant and Equipment that had been fully expensed under the TFE rules.

In all of the above scenarios, the cost of not getting pre-sale advice was, unsurprisingly, substantially higher than the time and cost that would have been spent on planning for the eventual sale.

If you would like to discuss this matter further, please contact Andrew Lowry or Leonard Tebbutt on 08 9444 9711.

ONUS ON PROPERTY DEVELOPER TO PROVE GST ASSESSMENTS EXCESSIVE?

In a recent Administrative Review Tribunal (ART) case: *ZKSM and FCT [2025] ARTA 1298, ART, Abood GM, 11 August 2025,* a property developer failed to defend its' calculation of its GST liability under the margin scheme, resulting in a $1.047m increase in GST payable.

This case concerned ZKSM's ("the Developer") calculation of the GST payable on their sales of residential properties under the margin scheme concession provided by Division 75 of the GST Act. The margin scheme allows entities to calculate their GST liability as 1/11th of the difference between their acquisition costs from the sale price.

In this instance, the Developer, who engaged in large scale englobo land development, had acquired land from the Australian Capital Territory (ACT) authority (the SLA) by entering into development lease arrangements with SLA which granted the Developer a 99 year lease of land that was then entitled to develop and sell.

The acquisition cost of the land comprised of a significant monetary payment and a non-monetary component, being the "development services" to be provided by the Developer. As required by s 75-10(2) and s 9 -75(1)(b) of the GST Act, the Developer was required to obtain valuations of the acquired land from a qualified valuer. The Developer used this valuation to calculate it's GST liability on the sale of the individual residential property it sold. The Developer also issued a series of tax invoices to the SLA for the 'development services" which included a GST component amounting to $16.3m.

The principal issues in dispute were:

1. whether the Developer was entitled to rely upon the valuations of land it obtained in calculating the non-monetary consideration for inclusion as its acquisition cost for the land;
2. whether the ATO was required to accept the Developer's approach to identifying the GST inclusive market value of the non-monetary consideration due to the Developer's reliance on various private and public rulings made by the Commissioner. *(Notably a private ruling obtained by the Developer from the Commissioner* ***did not*** *specifically address the question of the value of non-monetary consideration)*; and

3. whether the Developer was required to reduce the value of the non-monetary consideration for its acquisition of the land to take into account the additional amount of $16.3m paid by the SLA in respect of the Development Services.

The ATO won on all of the issues in dispute. Notably, the ART held that the Developer had not discharged its burden of proof to establish that the amended assessments issued by the ATO were excessive.

This case serves as a timely reminder of the importance of carefully drafting private ruling requests and objections to consider all possible GST risk exposures in a taxpayer's position.

Additionally, this case shows that as with other taxes, a taxpayer must not only demonstrate that their approach is correct and based on accepted ATO guidelines and case law, they also have the onus of proving why the ATO's approach is not correct. This is often a fine line and one that many clients may not appreciate is particularly nuanced.

If you would like to discuss these matters further, please contact Andrew Lowry or Leonard Tebbutt on 08 9444 9711.