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ereview
INTELLIGENT ACCOUNTING

Why changing your business structure just got easier.

New rules that apply from 1 July 2016 mean that small businesses can restructure their business operations without triggering adverse tax implications.

For small businesses, new restructuring rules that will apply from 1 July 2016 means that there has never been a better time to review your current business structure and make a change if it is appropriate.

Before the introduction of the new restructuring rules, if a business restructured from say, a partnership to a trust, there was a possibility that the change in structure could trigger capital gains tax (CGT). That is, the tax law would treat the restructure the same way as a sale and the owners could be liable for CGT on their share of any gain based on the current market value of the assets being moved into the new structure.

While the existing CGT provisions already contain a number of roll-overs that can be utilised for business restructures, they generally only provide relief when assets are transferred to a company. Other concessions can potentially apply in a broad range of situations, but will not necessarily provide complete tax relief. This new form of roll-over relief can provide complete income tax relief when assets are transferred to a sole trader, partnership or trust if certain conditions can be met.

The conditions for accessing these new rules are fairly strict. Broadly, the key conditions are:

- The transaction is a genuine restructure of an ongoing business. So, the concessions can't be used for winding down or selling a business.
- Each of the parties to the transaction is a small business entity (revenue under $2m) or is related to a small business entity in the year the transaction occurs. The turnover test is subject to some grouping rules.
- The business owners (the people who have ultimate economic ownership of the assets) and their share in those assets doesn't materially change.
- The asset being transferred is currently being used in a business carried on by the current owner or certain related parties.
- Both the original entity and the entity the business is being transferred into need to be Australian residents.
- The parties involved in the transaction must choose jointly to apply the roll-over.
- None of the entities involved in the transaction are a superannuation fund or exempt entity.

For many small business owners, the business structure they start with is not always the best structure over time. There are a lot of reasons why a business owner might need to restructure:

- Risk & asset protection - separating assets from business activities will generally help protect the assets. Companies and trust structures offer greater protection then operating as a sole trader or partnership of individuals.
- Tax - Your business structure determines the tax rate you pay and how it is paid. In addition, some structures offer greater tax concessions throughout the life of the business (e.g., for research and development activities) or on the sale of assets.
- Compliance - some structures are more expensive to maintain and administer than others and provide less flexibility for succession, sale, and the introduction of investors.

"For too long, the potential cost of restructuring has meant that many good businesses have suffered under a bad business structure. These new rules provide a great opportunity for small businesses to address any issues with their current structure, or move to a structure that will better suit their future plans."

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If you are looking at changing your business structure, there are a few overarching principles you should think about:

1. Keep it simple

Your structure should be as simple as possible and each entity should have a clear reason to exist. The more complex your structure the more expensive it becomes and the more likely that the Tax Office will start querying whether the entity exists for commercial or tax reasons. If reducing tax is the primary reason for structuring something in a particular way then the Tax Office can seek to remove the tax benefits the structure might provide.

2. Think of the future

Your structure should facilitate future growth and should allow for flexibility.

3. Start with the end in mind

You should be aware of your exit strategies from the business. Your structure can make a difference to how you are taxed and what concessions you can access when you eventually exit.

4. The commercial considerations

Different structures have different implications for how you run and manage your business. You need to be clear about the commercial reasons for adopting one structure over another.

5. Separate business activities from valuable assets

Where possible, ensure that valuable passive, business, or private assets are not subject to the risks associated with your business activities.

6. Protect retained profits

In some groups the use of a dormant holding company can help protect retained profits that have been generated by trading entities. The holding company can then operate as the banker for the group of entities, lending funds to operating entities as required (security could be taken over assets of the operating entity).

7. Separate risk between individuals

Within a family group, consider providing some additional asset protection by ensuring that only one spouse is a director of an operating company.

8. Corporate trustees for a trust

The use of a corporate trustee is generally prudent to protect from the risk of being personally liable for the debts of the trust.

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