

TAXING MY CASH FLOW: THE INFLUENCE OF TAX ON SMALL SERVICE SECTOR BUSINESS CASH FLOW

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ABSTRACT

This article reports the findings of a multiple case study of the perception of small business owners in the service sector in relation to the effect taxation has on their business cash flow. In particular, the project investigates the potential cash flow effect due to Fringe Benefits Tax ('FBT'), Goods and Services Tax ('GST'), Income Tax, Pay as You Go ('PAYG') Withholding and Superannuation Guarantee ('SG'). The findings suggest that small business owners have the greatest concerns about GST and PAYG on cash flow stability, with less concern about the impact of FBT, SG and Income Tax. The impact of tax on cash flow is not identified primarily as a cash flow issue, instead other business factors appear to have a negative impact on the tax and cash flow relationship.

Keywords: cash flow, small business, tax, GST

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I INTRODUCTION

The ability to maintain a viable business can be challenging for business owners. This may be due to restricted cash flow which results in an inability to satisfy the businesses outgoings. Clearly, tax should influence the cash flow of a business, as tax can be an outflow of cash payment(s) by a business to the revenue authority, although it can also result in an inflow of cash.¹ To the extent that additional cash is held by a business through collecting tax from others — such as goods and services tax ('GST') — in theory this could aid the cash liquidity of the business for a period of time. Another way that tax could influence cash flow is in terms of the provisioning and timing of payments, as tax (similar to other liabilities) has to be managed and timed. Furthermore, in managing the tax obligations of a business this can result in compliance costs, and paying for these compliance costs could influence the overall cash flow of a business. While cash flow is an issue for all businesses regardless of their size, for small businesses — due to particular characteristics (including financing problems)² — cash flow is an important consideration. Relevantly, prior studies have observed that tax may have a negative impact on cash flow stability for small businesses.³ However, some taxes may have a larger impact than others. Wallschutzky and Gibson,⁴ who investigated the effect of taxation on small business in the early 1990's, identified the wholesale sales tax ('WST') as the only tax system that had a detrimental effect on cash flow. This was because the payment of the WST tax liability to the Australian Taxation Office ('ATO') was often due for payment before it was received from trade debtors. More recent research conducted by Belle Isle, Freudenberg and Copp⁵ has supported the findings of Wallschutzky and Gibson⁶ in terms of GST (recalling that the GST essentially replaced the WST). Small business owners ('SBOs') indicated that GST had a detrimental effect on cash flow given that the tax liability was often not received from sales before it was due to be paid to the ATO.⁷ However, in both studies, it should be highlighted that paying the tax liability itself was not the sole cause of the cash flow constraints.

¹ This inflow of cash could occur when there is a refund of tax paid, or in relation to the goods and services tax ('GST') where the GST input tax credits are greater than the GST payable on taxable supplies (which could especially arise for those businesses that largely have GST Free supplies).

² David Deakins, Alana Morrison and Laura Galloway, 'Evolution, Financial Management and Learning in the Small Firm' (2002) 9(1) *Journal of Small Business and Enterprise Development* 7.

³ Patrick Hutchinson, 'How Much Does Growth Determine SMEs' Capital Structure?' (2004) 12(1) *Small Enterprise Research* 81, 85.

⁴ Ian Wallschutzky and Brian Gibson, 'Small Business Cost of Tax Compliance' (1993) 10(4) *Australian Tax Forum* 511.

⁵ Melissa Belle Isle, Brett Freudenberg and Richard Copp, 'Cash Flow Benefit from GST: Is it Realised by Small Businesses in Australia?' (2014) 29(3) *Australian Tax Forum* 417.

⁶ Wallschutzky and Gibson (n 4).

⁷ If using the accruals method, the tax liability of the wholesale sales tax ('WST') and GST can be incurred at the time of sale and paid sometime in the future.

Research conducted in the United Kingdom ('UK') and France by Messina and Walton⁸ suggested that taxes paid in advance have a negative impact on cash flow, whereas taxes held and paid at a later date result in a cash flow benefit, although, it should be acknowledged that the positive effect was marginal. Australian research appears to be inconsistent with findings in the UK and France, which could be due to differences in trading practices and/or the administration of tax systems, or to how cash flow benefits and constraints were measured in the differing studies. However, some studies have called into question the burden of tax on small businesses compared to other regulatory burdens, especially those that relate to employment.⁹

Currently, in Australia, the major Federal tax systems that most small businesses must comply with include (but are not limited to) fringe benefits tax¹⁰ ('FBT'), GST,¹¹ income tax,¹² and pay as you go ('PAYG') withholding.¹³ Additionally, there is the superannuation guarantee¹⁴ ('SG') which is not a tax system, however, due to the reliance of the calculation of the SG based on PAYG withholding, and the regularity of reporting obligations, it is included in this research. Normally the tax liability for these tax systems is incurred and paid sometime in the future. Considering the findings of Wallschutzky and Gibson,¹⁵ and more recent research conducted by Belle Isle, Freudenberg and Copp,¹⁶ it could be implied that negative effects on small business cash flow cannot solely be explained by the timing of the payment of the tax liability.

This study seeks to gain a deeper understanding of how tax influences the cash flow of small businesses operating in the service sector, with a focus on the five Federal tax systems noted above. The study expands prior case study research which only focused on GST,¹⁷ or was conducted nearly thirty years ago.¹⁸ The reason for the focus on the service

⁸ Michel Messina and Peter Walton, 'The Impact of Government on Company Cash Flows in France and the United Kingdom' (1998) 7(2) *Journal of International Accounting, Auditing and Taxation* 273.

⁹ Board of Taxation, *Scoping Study of Small Business Tax Compliance Costs: A Report to the Treasurer* (Canberra, December 2007) [10.7]: 'Many businesses in industries such as manufacturing, and construction rated occupational health and safety (OH&S) and licensing rules as more significant causes of compliance burden than taxation.'

¹⁰ *Fringe Benefits Tax Assessment Act 1986* (Cth) ('FBT Act').

¹¹ GST registration is mandatory for enterprises with a turnover of \$75,000 or more, although voluntary registration is available to enterprises below this threshold, see *A New Tax System (Goods and Services Tax) Act 1999* (Cth) s 23-5 ('GST Act').

¹² *Income Tax Assessment Act 1997* (Cth) ('ITAA97'); *Income Tax Assessment Act 1936* (Cth) ('ITAA36').

¹³ If the organisation is an employing entity. Non-employing entities are not required to adhere to PAYG.

¹⁴ *Superannuation Guarantee (Administration) Act 1992* (Cth) ('SG Act').

¹⁵ Wallschutzky and Gibson (n 4).

¹⁶ Belle Isle, Freudenberg and Copp (n 5).

¹⁷ Ibid. This prior research involved a case study with semi-structured interviews with 12 small businesses.

¹⁸ Wallschutzky and Gibson (n 4). This prior research involved a case study with semi-structured interviews with 12 small businesses.

sector is that it provides more than three-quarters of the economy's income¹⁹ and employs more than 87% of all Australian private sector employees. Further analysis suggests that small businesses make up a large part of the service sector, employing 4,127,000 of the total service sector employment of 9,410,000. Considering the economic significance of the small business sector, it is important to investigate the factors that may influence their cash flow.

For this research project, the term 'small business' incorporates those businesses identified by their quantitative measures by the ATO and Australian Bureau of Statistics ('ABS') as being 'micro' and 'small', an annual turnover of \$10 million or less and a full time workforce of 20 or fewer employees.²⁰

This article is structured as follows: Part II will provide an overview of our understanding of the influence of tax on small business cash flow; Part III will provide the research methodology undertaken, which is followed by participants' demographics in Part IV; Part V will outline the results. Through the analysis of the results in Part VI, recommendations will be proposed, with future research being outlined in Part VII of the article before concluding in Part VIII.

II SMALL BUSINESS TAX AND CASH FLOW

Below is the discussion about our current understanding of cash flow management practices by small businesses, and how tax may influence a business' cash flow.

A Cash Flow Management

A critical issue for all businesses is maintaining a consistent cash flow; this can especially be acute for small businesses due to restricted access to finance. Cash flow is the extent of cash or near cash assets available for use, along with any inflow or outflow of cash related to these assets.²¹ Therefore cash flow is any business activity that alters the balance of the cash accounts. Previous research in Australia suggests that SBOs have recognised that cash flow is of particular importance to their ongoing survival,²² although it can be difficult for them to manage.²³

¹⁹ Note: Income for this research is reported as Gross Value Added ('GVA') as opposed to Gross Domestic Product ('GDP') due to the focus of the research on the service industry.

²⁰ Australian Bureau of Statistics, *Counts of Australian Businesses including Entries and Exits (Jun 2015 to Jun 2019)* (Catalogue No 8165.0, 2 February 2020); Australian Taxation Office, *Taxation Statistics 2015–16* (27 April 2018).

²¹ Ignatius Ekanem, 'Liquidity Management in Small Firms: A Learning Perspective' (2010) 17(1) *Journal of Small Business and Enterprise Development* 123.

²² Belle Isle, Freudenberg and Copp (n 5); Wallschutzky and Gibson (n 4) 527.

²³ Melissa Belle Isle and Brett Freudenberg, 'Calm Waters: GST and Cash Flow Stability for Small Businesses in Australia' (2015) 13(2) *eJournal of Tax Research* 492.

The reasons contributing to difficulty include that small businesses can be subject to seasonal variations in sales.²⁴ This can mean that rapid growth can be evident in one economic cycle followed by periods of contraction in subsequent cycles.²⁵ Businesses that receive a cash influx as a result of rapid growth should store this cash for future periods of contraction. However, research suggests that this is not a common practice followed by the small business community.²⁶ Cash received is either tied up in goods produced, spent on incidental items or held in outstanding debtor invoices.²⁷ Without cash at the ready, critical payments cannot be made, potentially resulting in business failure.²⁸ Those small businesses with a greater portion of liquid assets are less likely to run out of cash.²⁹ Cash inflow should be of the highest priority for small business, as they can survive for lengthy periods without profit although this is not the same outcome for trading without cash.³⁰ Due to the finance constraints on small business — such as reliance on owner equity for much of the capital and the reluctance of banks to provide credit — managing cash is critical. For example, a small business owner can use their own personal credit cards rather than accessing formal lines of business credit.³¹ This may be due to their reluctance to do the formal paperwork for the bank loan, or to the perceived lack of availability of business loans to small businesses.

Cash flow management has been identified as one of the most important problems for businesses in the UK, United States of America and Australia.³² Effective cash management is important to business survival irrespective of the size of the business.³³ When assessing small business liquidity it has been suggested that small business are less liquid and exhibit more volatility with cash flow and profit than their larger competitors.³⁴ SBOs should try to avoid extended cash shortages, as supply constraints affect the ongoing

²⁴ John A. Welsh and Jerry F. White, 'A Small Business is not a Little Big Business' (1981) 59(4) *Harvard Business Review* 18, 26.

²⁵ Ibid.

²⁶ Ibid.

²⁷ Ibid.

²⁸ Chris Evans, Shirley Carlon and Darren Massey, 'Record Keeping Practices and Tax Compliance of SMEs' (2005) 3(2) *eJournal of Tax Research* 288, 292; Pedro J. García-Teruel and Pedro Martínez-Solano, 'Short-Term Debt in Spanish SMEs' (2007) 25(6) *International Small Business Journal* 579, 583; Michael J. Peel and Nicholas Wilson, 'Working Capital and Financial Management Practices in The Small Firm Sector' (1996) 14(2) *International Small Business Journal* 52, 52.

²⁹ García-Teruel and Martínez-Solano (n 28) 583.

³⁰ Ibid; Peel and Wilson (n 28) 58; Welsh and White (n 24) 29.

³¹ Department of Industry, Innovation, Science, Research and Tertiary Education, *Australian Small Business Key Statistics and Analysis* (Canberra, 2010).

³² Scott Holmes and Des Nicholls, 'An Analysis of the Use of Accounting Information by Australian Small Business' (1998) 26(2) *Journal of Small Business Management* 57, 57; Peel and Wilson (n 28) 19.

³³ Arthur R De Thomas and William B Fredenberger, 'Accounting Needs of Very Small Business' (1985) 55(10) *The CPA Journal* 14.

³⁴ Peel and Wilson (n 28) 19.

operations of the business.³⁵ In order to reduce cash constraints and achieve better control of cash flow SBOs need to implement effective liquidity management practices.³⁶

Inadequate SBO management skills can be especially concerning where SBOs struggle with the management of cash flow, as well as with the requirement to adhere to taxation and employer obligations. These 'employer obligations' can be a central issue, as a small business without employees is unlikely to grow and will be more likely to remain as a micro business that provides income for the owner.³⁷ These inadequate management skills could be exacerbated if the SBO also has limited taxation literacy as the cash flow of the business may also be impacted by tax liabilities that are due but have not been included in cash flow projections.³⁸

B Tax and Cash Flow

Research into the effect of taxation on small business has been a popular research topic over the last three decades.³⁹ The majority of this research focused on the impact of compliance and administration costs for small businesses,⁴⁰ identifying that tax is burdensome for small business in terms of compliance costs. These compliance costs can impact cash flow as an outflow of cash in meeting the expenses, such as paying staff or external advisors. However, few studies have investigated the interplay of small business cash flow and taxation.⁴¹ Research has suggested that the cash flow of small businesses is

³⁵ Ekanem (n 21) 124–25.

³⁶ Michael Peel, Nicholas Wilson and Carole Howorth, 'Late Payment and Credit Management in the Small Firm Sector: Some Empirical Evidence' (2000) 18(2) *International Small Business Journal* 17, 19–24.

³⁷ Department of Industry, Innovation, Science, Research and Tertiary Education, *Australian Small Business Key Statistics and Analysis* (Canberra, 2012) 8.

³⁸ Freudenberg et al, 'Tax Literacy of Australian Small Businesses' (2017) 18(2) *Journal of Australian Tax* 21.

³⁹ Francis Chittenden, Saleema Kauser and Panikkos Poutziouris, 'PAYE-NIC Compliance Costs: Empirical Evidence from the UK SME Economy' (2005) 23(6) *International Small Business Journal* 635; Evans et al, 'Small Business and Tax Compliance Costs: A Cross-Country Study of Managerial Benefits and Tax Concessions' (2014) 12(2) *eJournal of Tax Research* 453; John Glover and Binh Tran-Nam, 'The GST Recurrent Compliance Costs/Benefits for Small Business in Australia: A Case Study Approach' (2005) 1(2) *Journal of Australasian Tax Teachers Association* 237; Philip Lignier and Chris Evans, 'The Rise and Rise of Tax Compliance Costs for the Small Business Sector in Australia' (2012) 27(3) *Australian Tax Forum* 615; Philip Lignier, Chris Evans and Binh Tran-Nam, 'Tangled Up in Tape: The Continuing Tax Compliance Plight of the Small and Medium Enterprise Business Sector' (2014) 29(2) *Australian Tax Forum* 217; Rametse et al, 'Estimating Start-Up Compliance Costs of the Malaysian Goods and Services Tax for Small- and Medium-Sized Enterprises' (2020) 26(6) *New Zealand Journal of Taxation Law and Policy* 153; OECD, *Taxation of SMEs in OECD and G20 Countries* (OECD Tax Policy Studies, 2015); Kate Ritchie, 'The Tax Compliance Costs of Small Business in New Zealand' in *Tax Compliance Costs: A Festschrift for Cedric Sandford* (Prospect Media Pty Ltd, 2001) 297–316; Cedric Sandford, Michael R Godwin and Peter J. W. Hardwick, *Administrative and Compliance Costs of Taxation* (Fiscal Publications, 1989); Wallschutzky and Gibson (n 4).

⁴⁰ Ibid.

⁴¹ Eliza Ahmed and Valerie Braithwaite, 'Understanding Small Business Taxpayers Issues of Deterrence, Tax Morale, Fairness and Work Practice' (2005) 23(5) *International Small Business Journal* 539; Belle Isle, Freudenberg and Copp (n 5); Evans, Carlon and Massey (n 28); Wallschutzky and Gibson (n 4).

influenced by tax systems, both in Australia and throughout the world.⁴² This influence could be both positive and negative.

Researchers have proposed that cash flow stability has a negative relationship with tax liabilities.⁴³ In the UK, the largest reported reason for small business failure was an inability to settle outstanding tax debts.⁴⁴ Of course, these businesses with outstanding tax debts could have been insolvent for years and had used their unpaid taxes to pay off other creditors. In a sense, the relevant tax authority can be used as an unofficial line of credit to support business operations. Businesses may choose not to pay their taxes when due and instead pay other creditors, especially those who are essential to the continuing operations of the business (such as those supplying inventory or materials). A study in New Zealand suggested that small businesses incur late tax payment penalties in an attempt to improve their business cash flow.⁴⁵ Findings in France and the UK suggest that cash flow is negatively impacted by tax systems that are paid in advance, whereas taxes that are held and paid at a later date could be beneficial to cash flow.⁴⁶ When taxes are held and paid sometime in the future, this could have a positive effect as it allows businesses to legitimately use their outstanding tax liabilities as an easy source of finance to fund other aspects of their operations (i.e., use of the GST collected to pay off other creditors).⁴⁷

In Australia, the current evidence is conflicting in relation to the effect that taxation has on small business cash flow. While some research suggests that Australian small businesses are not unduly suffering from the impact of various forms of taxation,⁴⁸ opposing arguments suggest that cash flow is constantly impinged upon particularly when small businesses are responsible for paying their own taxes and collecting tax on behalf of others.⁴⁹ Other business factors can be a contributing force regarding whether cash flow is influenced by taxation such as terms of trade, industry, cash flow management and low profit margins.⁵⁰ Where tax liabilities are due and cash flow is short, small

⁴² Ahmed and Braithwaite (n 41); Belle Isle, Freudenberg and Copp (n 5); Evans, Carlon and Massey (n 28); Lignier and Evans (n 39); Messina and Walton (n 8); Sandford et al, *Costs and Benefits of VAT* (Heinemann Educational Books, 1981); Wallschutzky and Gibson (n 4).

⁴³ Margaret Drever and Patrick Hutchinson, 'Industry Differences in the Determinants of the Liquidity of Australian Small and Medium Sized Enterprises' (2007) 15(1) *Small Enterprise Research* 60, 64–65, 74; Karen Ness, 'Small Business Success Factors in Regional Queensland' (2004) 12(2) *Small Enterprise Research* 1; Mervi Niskanen and Jyrki Niskanen, 'Small Business Borrowing and the Owner-Manager Agency Costs: Evidence on Finnish Data' (2010) 48(1) *Journal of Small Business Management* 16, 17.

⁴⁴ Ahmed and Braithwaite (n 41) 554; Evans, Carlon and Massey (n 28) 290.

⁴⁵ Elisabeth Poppelwell, Gail Kelly and Xin Wang, 'Intervening to Reduce Risk: Identifying Sanction Thresholds Among SME Tax Debtors' (2012) 10(2) *eJournal of Tax Research* 403, 405.

⁴⁶ Messina and Walton (n 8).

⁴⁷ Belle Isle, Freudenberg and Copp (n 5); Poppelwell, Kelly and Wang (n 45).

⁴⁸ Belle Isle, Freudenberg and Copp (n 5) 424; Evans, Carlon and Massey (n 28) 310.

⁴⁹ Ahmed and Braithwaite (n 41); OECD (n 39) 90.

⁵⁰ Belle Isle, Freudenberg and Copp (n 5) 424; Evans, Carlon and Massey (n 28) 310.

businesses have been known to use working capital funds to settle their tax liability.⁵¹ SBOs have also suggested that the number of different tax obligations due within a short period of time is the cause of the cash flow problem, as they have to manage these different timings and obligations.⁵² The extent of these problems may explain why, in 2017–18, small businesses earning less than \$10 million were responsible for almost two-thirds of the total outstanding tax debt recognised with the ATO.⁵³

In 1995, the Senate Economics References Committee ('SERC')⁵⁴ suggested that any tax would be an imposition on small business cash flow, although the study by Wallschutzky and Gibson⁵⁵ argued that SBOs perceived only that the WST caused cash flow problems. Participants did not feel negatively about other Federal tax systems in place at the time of the research. The Wallschutzky and Gibson study in the early 1990s involved a case study with semi-structured interviews of 12 small businesses, supplemented by interviews with some accountants and ATO staff.⁵⁶ Approximately twenty years later, in a case study with semi-structured interviews of 12 small businesses, Belle Isle, Freudenberg and Copp⁵⁷ solely focused on the effect of GST on cash flow, and found that payment practices and tight profit margins were more of a concern than the GST itself.

The prominent issue identified by Wallschutzky and Gibson,⁵⁸ and by Belle Isle, Freudenberg and Copp,⁵⁹ in relation to the WST and GST respectively, was that income is generally earned and recognised at the time of invoicing (commonly known as the accruals method). However, payment from the debtor is often not received until sometime in the future. The time delay in the payment of the invoice means that the portion of tax held in income earned is not always received when the obligation to pay the tax to the ATO arises. This is especially relevant to those businesses using an accruals (i.e., non-cash) method to account for their tax liabilities. In contrast, those businesses using the cash method of accounting would not recognise a GST liability until payment for goods and services supplied is received from the debtor. Thus, under the accruals method of accounting for GST, as opposed to the cash method of accounting for GST, businesses must submit the GST to the ATO irrespective of cash receipt, hence negatively impacting on their cash flow.⁶⁰ The impact on cash flow for those on a non-cash method can be further exacerbated by the 'sharp' payment practices of some debtors. For example, the Australian Small Business and Family Enterprise Ombudsmen found that debtors

⁵¹ Evans, Carlon and Massey (n 28) 288.

⁵² Ibid 289; Messina and Walton (n 8).

⁵³ Australian Taxation Office, *Management of Small Business Tax Debt* (30 May 2019).

⁵⁴ Senate Economics References Committee, 'A Question of Balance: The Tax Treatment of Small Business' (28 June 1995) [7.1].

⁵⁵ Wallschutzky and Gibson (n 4).

⁵⁶ Ibid.

⁵⁷ Belle Isle, Freudenberg and Copp (n 5).

⁵⁸ Wallschutzky and Gibson (n 4).

⁵⁹ Belle Isle, Freudenberg and Copp (n 5) 424.

⁶⁰ Belle Isle, Freudenberg and Copp (n 5).

(particularly large businesses) would not pay their bills to small business creditors on time.⁶¹

In comparison, those businesses that collected tax at the point of sale still experienced difficulty complying with their tax obligations, although this appeared to be more a result of low profit margins on their goods and services, rather than the tax system being overly burdensome.⁶² Determining the effect of trading practices on small business cash flow is problematic due to the diversity of businesses classified as service sector businesses. Trading practices are not specific to the service sector itself but are defined by the service classification that the business resides in. This means that trading practices throughout the service sector are a mixture of those who collect revenue at the point of sale and others who offer a line of credit, making it difficult to define any industry norms for the service sector.

However, GST is not the only tax that small businesses have to consider. The current Australian Federal tax systems that relate to the majority of small business taxpayers include FBT,⁶³ GST,⁶⁴ income tax,⁶⁵ PAYG withholding⁶⁶ and SG.⁶⁷ All of these tax systems have the liability incurred and held by the taxpayer or tax collector, and are paid sometime in the future.⁶⁸ However, a number of these tax systems require taxpayers to pre-pay amounts in advance in the form of instalments.⁶⁹ Part of the logic behind pre-instalments is to reduce the potential for a large tax liability to arise at the end of the reporting period by instead paying regular contributions towards a predicted tax liability throughout the year. The pre-instalment value can be based on previous earnings or tax liabilities from prior tax periods. Pre-instalments are required for income tax⁷⁰ and FBT⁷¹ if a taxpayer has previously submitted a return for these tax systems. Also, a GST⁷² instalment can be paid quarterly for complying entities. There is no known research into the effect that tax pre-instalments have on cash flow stability in Australia. Of further interest is the

⁶¹ Australian Small Business and Family Enterprise Ombudsman, *Payment Times and Practices Inquiry — Final Report* (Report, April 2017) <https://www.asbfeo.gov.au/sites/default/files/ASBFEO_Payment_Times_and_Practices%20Inquiry_Report.pdf>.

⁶² Belle Isle, Freudenberg and Copp (n 5).

⁶³ *FBT Act* (n 10).

⁶⁴ *GST Act* (n 11).

⁶⁵ *ITAA97* (n 12).

⁶⁶ *A New Tax System (Pay As You Go) Act 1999* (Cth) ('*PAYG Act*').

⁶⁷ *SG Act* (n 14).

⁶⁸ *GST Act* (n 11) ss 27-5, 27-10, 27-15, 27-30, 33-3, 33-5; *PAYG Act* (n 66) s 6-5(2); *FBT Act* (n 10); *ITAA97* s 5-5; *SG Act* (n 14) s 46.

⁶⁹ *GST Act* (n 11) s 162-70; *PAYG Act* (n 66) s 6-5(3); *FBT Act* (n 10) ss 102, 103.

⁷⁰ *PAYG Act* (n 66) s 6-5(3).

⁷¹ *FBT Act* (n 10) ss 102, 103. Note instalments for FBT are only payable if the entity's previous years FBT liability was greater than \$3,000.

⁷² *GST Act* (n 11) s 162-70.

multitude of payments that are required to be made in order to adhere to the compliance requirements of the five Federal tax systems listed. As illustrated in Table 1 below, payments can range from being due 5 up to 26 times throughout each calendar year, dependent on whether businesses report annually, quarterly or monthly and whether they are affected by all five tax systems.

TABLE 1: TAX PAYMENT DATES DEPENDENT ON REGISTRATION STATUS OF BUSINESS

OBLIGATION	COMPLIED BY	DUE DATE
Activity Statement December	Monthly registered	21 January
FBT Third Instalment	Some FBT entities	21 January
SG October–December	All	28 January
Activity Statement January	Monthly registered	21 February
Activity Statement October–December	Quarterly registered	28 February
PAYG Instalment October–December	All employing	28 February
GST Instalment October–December	All GST registered	28 February
Income Tax Return	Self-preparing entities	28 February
FBT Third Instalment	For deferred BAS FBT payers	28 February
Activity Statement February	Monthly registered	21 March
Activity Statement March	Monthly registered	21 April
FBT Fourth Instalment	Some FBT entities	21 April
Activity Statement January–March	Quarterly registered	28 April
PAYG Instalment January–March	All employing	28 April
GST Instalment January–March	All GST registered	28 April
SG January–March	All	28 April
FBT Fourth Instalment	For deferred BAS FBT payers	28 April
Annual Fringe Benefits Payment	All affected by FBT	21 May
Activity Statement April	Monthly registered	23 May
Activity Statement May	Monthly registered	21 June
Activity Statement June	Monthly registered	21 July
FBT First Instalment	Some FBT entities	21 July
Activity Statement April–June	Quarterly registered	28 July
PAYG Instalment April–June	All employing	28 July
GST Instalment April–June	All GST registered	28 July
SG April–June	All	28 July
FBT First Instalment	For deferred BAS FBT payers	28 July
Activity Statement July	Monthly registered	21 August
Activity Statement August	Monthly registered	21 September
Activity Statement September	Monthly registered	21 October
FBT Second Instalment	Some FBT entities	21 October
Activity Statement July–September	Quarterly registered	28 October
PAYG Instalments – Final Payment	All employing	28 October
GST Instalment July–September	All GST registered	28 October
SG July–September	All	28 October
FBT Second Instalment	For deferred BAS FBT payers	28 October

Income Tax Return	Individual, Partnership and Trust	31 October
Activity Statement October	Monthly registered	21 November
Activity Statement November	Monthly registered	21 December

Notes: Adapted from the ATO website <<https://www.ato.gov.au/business/reports-and-returns/due-dates-for-lodging-and-paying/>>.

It should be highlighted that these obligations in Table 1 (above) relate only to the five tax systems in this project. Individual businesses may have a multitude of other tax obligations that could increase the frequency and variance of their business reporting and payment requirements. In overseas countries, cash flow difficulties in small businesses have been associated with the number of taxes that must be complied with, along with the multiple deadlines for tax payments in any given year.⁷³

It is considered important to determine whether taxation is the primary issue for small business cash flow or whether there are other factors that influence cash flow, and whether taxation just aggravates those factors. Research prior to the introduction of the GST suggests that the timing of tax payments was not the primary issue for small businesses.⁷⁴ Instead the problem was that small businesses have poor cash flow management practices and record-keeping skills.⁷⁵ Evans, Carlon and Massey⁷⁶ propose that small business use the cash at bank balance as an indicator of business health, however, little consideration is given to the portion of tax liability that is held in that balance.

The current research expands substantially the research conducted by Belle Isle, Freudenberg and Copp⁷⁷ in 2014 which only investigated the effects of GST on cash flow. This research now considers the influence of taxation on cash flow by focusing on five of the Federal tax systems operating in Australia including FBT, GST, income tax, PAYG withholding and SG. The impact of tax reporting and payments is also analysed, with particular reference to prior theoretical propositions which consider the relationship between similar tax systems and small business cash flow.

III RESEARCH METHODOLOGY

It should be noted that this research was conducted mainly from September 2016 to June 2019 and therefore prior to the economic effects of COVID-19.⁷⁸ The research seeks to

⁷³ OECD (n 39) 90.

⁷⁴ Wallschutzky and Gibson (n 4).

⁷⁵ Senate Economics References Committee (n 54) [7.34].

⁷⁶ Evans, Carlon and Massey (n 28) 300.

⁷⁷ Belle Isle, Freudenberg and Copp (n 5).

⁷⁸ COVID-19 is a mild to severe respiratory illness that is caused by a coronavirus (*Severe acute respiratory syndrome coronavirus 2* of the genus *Betacoronavirus*), is transmitted chiefly by contact with infectious material (such as respiratory droplets) or with objects or surfaces contaminated by the causative virus, and is characterized especially by fever, cough, and shortness of breath and may

explore the perception of SBOs in the service sector in terms of their cash flow and the influence that tax may have on it. To address this a case study methodology was adopted, as it was seen as an efficient method for examining this phenomenon.⁷⁹ The case study has been a popular methodology used by tax researchers in prior studies to obtain an in depth understanding of the research problem and contribute to theory.⁸⁰ Yin's⁸¹ case study design was the foundation for this project with replication of the same procedure undertaken for each case.⁸² This suggests that data should be collected from participants within a specific time and while they are engaged in the same activity. To satisfy this requirement, the collection of data from all participants in the multiple case study was secured over a six-week period from 14 September 2016 to 31 October 2016. During this period, small businesses in Australia are likely to have many reporting and payment obligations due to the ATO (see Table 1 above).

The group that the research primarily focused on were individuals who operate small businesses in the service sector, and they were classified in accordance with ABS catalogue no. 1292.0 and ranged from a variety of service classifications.⁸³ Securing participants from the small business sector was a challenging exercise, which has also been acknowledged in other qualitative research projects completed in Australia to date.⁸⁴ As a result, purposive sampling techniques were used to ensure that volunteer participants were selected according to those service sector classifications⁸⁵ and to their adherence with the unit of analysis for the project. The unit of analysis required that participant SBOs had an annual turnover of \$10 million or less and a full-time workforce of 20 or fewer employees.⁸⁶ SBOs who were engaged to participate in the multiple case study were sourced from a variety of platforms including social media platforms (i.e., Facebook and LinkedIn), by email distribution through accounting firm databases and by approaching personal, professional and university networks.

progress to pneumonia and respiratory failure, see Merriam Webster, 'COVID-19' (2021) <<https://www.merriam-webster.com/dictionary/COVID-19>>.

⁷⁹ J. Clyde Mitchell, 'Case and Situation Analysis' in *Case Study Method: Key Issues, Key Texts* (Sage Publications, 7th ed, 2009) 165–186, 170; Wallschutzky and Gibson (n 4) 516; Robert Yin, *Case Study Research Design and Methods* (Sage Publications Inc, 4th ed, 2009) 9.

⁸⁰ Belle Isle, Freudenberg and Copp (n 5); Belle Isle and Freudenberg (n 23); Glover and Tran-Nam (n 39); Ritchie (n 39) 304; Wallschutzky and Gibson (n 4).

⁸¹ Yin (n 79) 57.

⁸² Yin (n 79).

⁸³ Australian Bureau of Statistics, *Australian and New Zealand Standard Industrial (ANZSIC)* (Catalogue No 1292.0, 26 June 2013).

⁸⁴ Belle Isle, Freudenberg and Copp (n 5); Belle Isle and Freudenberg (n 23); Binh Tran-Nam and John Glover, 'Estimating the Transitional Compliance Costs of the GST in Australia' (2002) 17 *Australian Tax Forum* 499–536; Wallschutzky and Gibson (n 4).

⁸⁵ Australian Bureau of Statistics (n 83).

⁸⁶ Australian Bureau of Statistics (n 20); Australian Taxation Office, *Taxation Statistics 2015–16* (27 April 2018).

The benefits of including interviews in research are that they allow a more in-depth appreciation of the research problem, based on human actions and experiences.⁸⁷ For this project, semi-structured interviews were employed in the collection of data from SBOs in the multiple case study. Both qualitative and quantitative questionnaire formats were used.

To code the data, content analysis techniques were employed, which involves the manual identification of similar subject matter from the transcribed interview scripts.⁸⁸ Files are created based on the categories already established and the text satisfying each category from the transcripts is copied into the relevant file.⁸⁹ Once all transcripts have been thoroughly analysed and the data copied to the relevant files, the data is further analysed into sub-categories.⁹⁰ Sub-categories can include codes that were previously expected to be present and new codes uncovered from the data collection process.⁹¹

Content analysis in the current project initially involved reading over all transcripts before copying any data into files. Different colours were assigned to each category and highlighted text in the transcripts that satisfied individual categories. Some textual concepts addressed more than one category and therefore comments were made in the transcript document about the relevance of that text to the identified categories. A second reading of the transcripts was then carried out to ensure that the consistency of the analysis techniques was employed for all transcripts. Once this was completed, the highlighted text was copied to the relevant category file.

Then each file was read and identified sub-categories and relationships that appeared to be apparent in the data. Files were created for each sub-category and the process previously completed for categories was carried out again for the sub-categories. The category and sub-category documents assisted in determining how the results would be presented in the research documentation. Important quotations were also included where relevant.

IV DEMOGRAPHICS

As a result of the sampling techniques utilised, seventeen SBO participants were engaged for the multiple case study. It was proposed that at least one business from each ANZSIC⁹² service classification would be included in the case study. Unfortunately, it was not possible to satisfy this proposition. The participating SBOs engaged were classified into nine of the fifteen service groups. The classification groups that were not represented in the case study included categories D (Electricity, Gas, Water and Waste Services), F

⁸⁷ Svend Brinkmann, *Qualitative Interviewing: Understanding Qualitative Research* (Oxford University Press, 2013) 47, 49.

⁸⁸ Gubrium et al, *The Sage Handbook of Interview Research: The Complexity of the Craft* (Sage, 2nd ed, 2012) 198.

⁸⁹ Ibid.

⁹⁰ Ibid.

⁹¹ Brinkmann (n 87) 64; Gubrium et al (n 88).

⁹² Gubrium et al (n 88).

(Wholesale Trade), I (Transport, Postal and Warehousing), L (Rental Hiring and Real Estate Services), O (Public Administration and Safety) and R (Arts and Recreational Services).

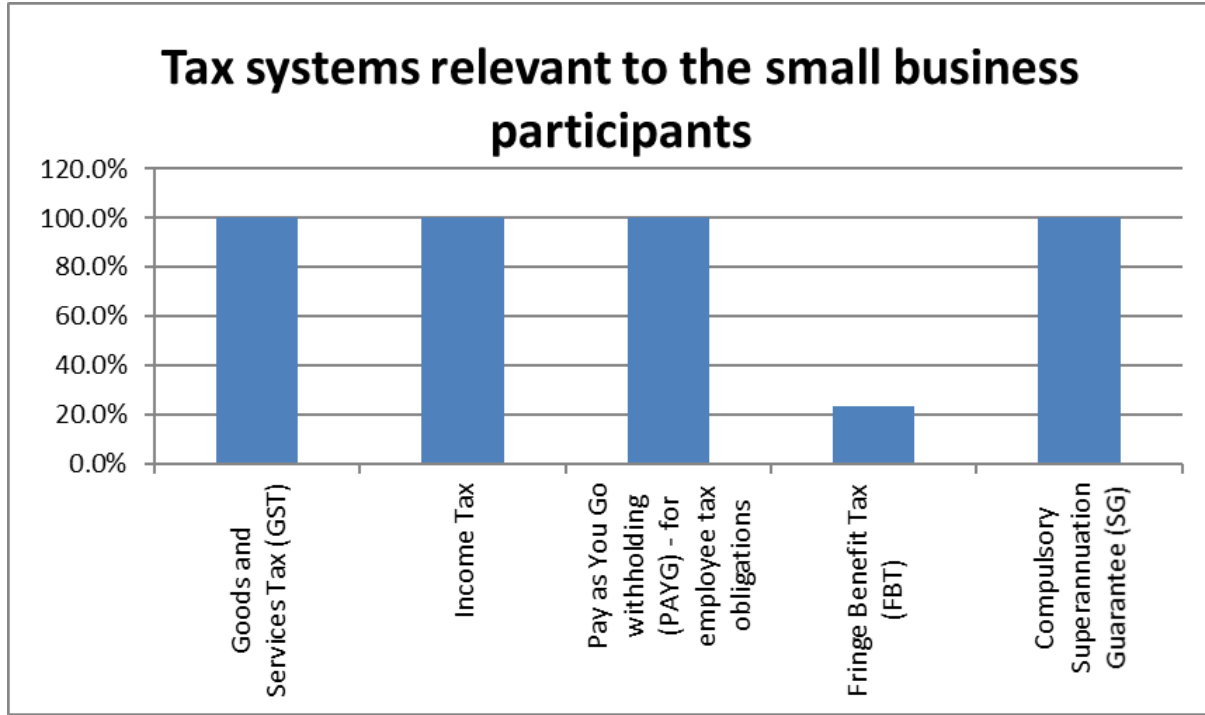
Table 2 below demonstrates an overview of the participating SBOs in terms of annual turnover, years trading, number of employees, business activity statement ('BAS') and PAYG reporting cycle, business form, trading partners, services provided, ANZSIC category, use and type of computer accounting software ('CAS'), preparation and lodgement of BAS and compliance with the five Federal tax systems within the study, including whether businesses had a requirement to pay a PAYG or a FBT instalment.

TABLE 2: PARTICIPANT DEMOGRAPHICS FOR MULTIPLE CASE STUDY

Participant No.	Annual Turnover (\$)	Years Trading	F/T Employees	BAS Reporting	PAYG Reporting	Business Form	Consumer Sales (%)	Business Sales (%)	Service Provided	ANZSIC Category	Uses CAS	CAS Type	BAS Prepared By	BAS Lodged By	PAYG	FBT	SG	Income Tax	GST	Paid PAYG Instalment	Paid FBT Instalment
1	500,000 < 2,000,000	28	4	Qtrly	Qtrly	Discretionary Trust	100	0	Sale imported goods	G	N	Excel & Bank statements	Self	Accountant Tax Agent	Y	N	Y	Y	Y	Y	N/A
2	2,000,000 < 5,000,000	18	17	Qtrly	Mthly	Company Trust Combo	5	95	Commercial Plumbing	E	Y	SimPro and MYOB	Self	Self	Y	N	Y	Y	Y	N	N/A
3	< \$250,000	10	1	Qtrly	Qtrly	Sole Trader	0	100	Bookkeeping	K	Y	MYOB	Self	Self	Y	N	Y	Y	Y	Y	N/A
4	\$250,000 < \$500,000	5	3	Qtrly	Qtrly	Company	80	20	Cleaning	MN	Y	MYOB	Bookkeeper	Bookkeeper	Y	Y	Y	Y	Y	Y	N
5	\$500,000 < \$2,000,000	17	2	Qtrly	Qtrly	Trust	100	0	Financial Planning	K	Y	Reckon 1	Bookkeeper	Bookkeeper	Y	Y	Y	Y	Y	Y	N
6	\$2,000,000 < \$5,000,000	2	18	Mthly	Qtrly	General Partnership	90	10	Fruit and Vegetables	G	Y	Xero	Accountant Tax Agent	Accountant Tax Agent	Y	N	Y	Y	Y	N	N/A
7	\$2,000,000 < \$5,000,000	2	20	Qtrly	Mthly	Dis Trust	100	0	Day-care Centre	P	Y	MYOB	Accountant Tax Agent	Accountant Tax Agent	Y	N	Y	Y	Y	N	N/A
8	< \$250,000	3	1	Qtrly	Qtrly	Dis Trust	10	90	Account/Tax	M	Y	Xero	Self	Self	Y	N	Y	Y	Y	Y	N/A
9	\$500,000 < \$2,000,000	10	1	Qtrly	Qtrly	Company	100	0	Restaurant	H	Y	MYOB	Self	Bookkeeper	Y	N	Y	Y	Y	N	N/A
10	\$500,000 < \$2,000,000	5	6	Qtrly	Qtrly	Company	2	98	Software Development	J	Y	MYOB	Bookkeeper	Accountant Tax Agent	Y	N	Y	Y	Y	Y	N/A
11	\$500,000 < \$2,000,000	11	8	Qtrly	Mthly	Company	98	2	Take-away Food	H	Y	Xero	Accountant Tax Agent	Accountant Tax Agent	Y	N	Y	Y	Y	N	N/A
12	\$500,000 < \$2,000,000	1	1	Qtrly	Qtrly	Company	0	100	Technical Engineering	M	Y	Xero	Self	Self	Y	N	N	Y	Y	N	N/A
13	\$500,000 < \$2,000,000	2	3	Qtrly	Mthly	Company	5	95	Technical Engineering	M	Y	Harvest and Excel	Bookkeeper	Bookkeeper	Y	N	Y	Y	Y	Y	N/A
14	\$2,000,000 < \$5,000,000	5	11	Qtrly	Mthly	Company	0	100	Team Training	P	Y	MYOB	Bookkeeper	Bookkeeper	Y	Y	Y	Y	Y	Y	Y
15	\$500,000 < \$2,000,000	13	2	Qtrly	Mthly	Discretionary Trust	100	0	Psychology	Q	Y	Xero	Accountant Tax Agent	Accountant Tax Agent	Y	N	Y	Y	Y	Y	N/A
16	\$500,000 < \$2,000,000	30	2	Qtrly	Mthly	Company	2	98	Electrical Engineer	E	Y	Xero	Self	Accountant Tax Agent	Y	N	Y	Y	Y	Y	N/A
17	\$500,000 < \$2,000,000	30	10	Mthly	Mthly	Company	100	0	Dental	Q	Y	Reckon 1	Employee	Employee	Y	Y	Y	Y	Y	Y	N

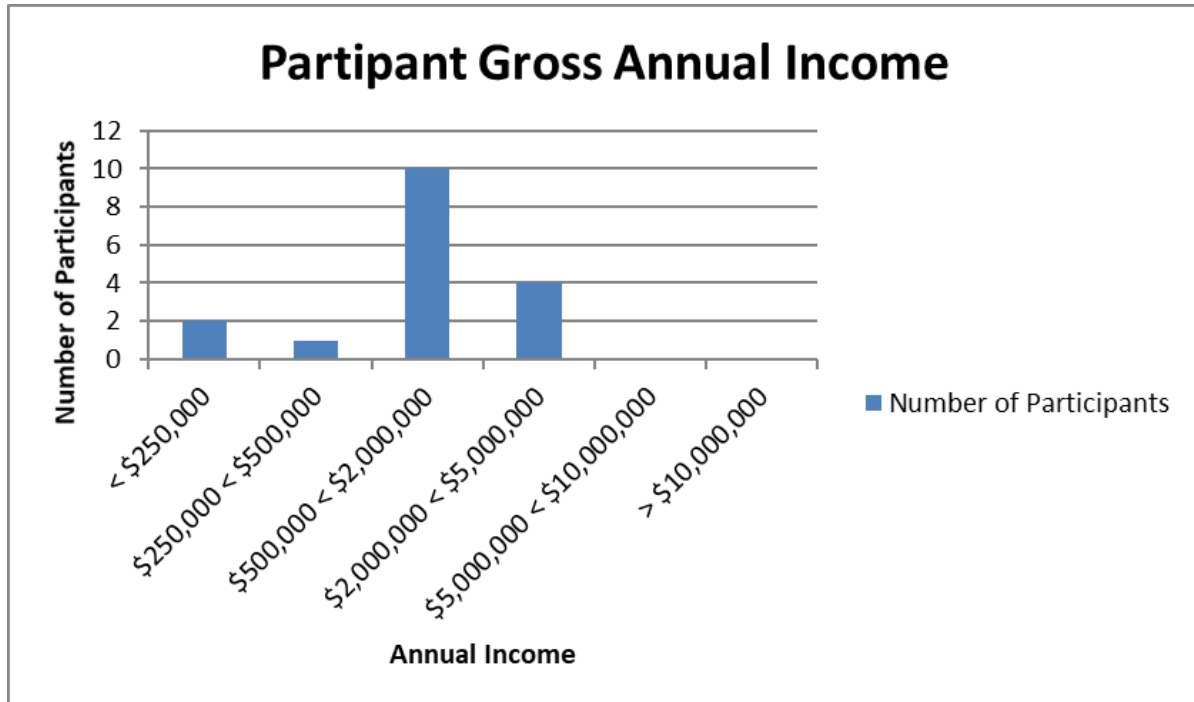
Table 2 (above) and Figure 1 (below) illustrate that all participating SBOs reported for PAYG, income tax, GST and the SG. Four businesses or 24% reported for FBT. Of the four businesses complying with FBT, only one business (representing 25% of complying entities) paid an FBT instalment.

FIGURE 1: ILLUSTRATION OF THE TAX SYSTEMS RELEVANT TO SMALL BUSINESS PARTICIPANTS



In comparison, PAYG instalments were made by 65% of PAYG compliant entities. Quarterly reporting for both PAYG and BAS was most common among the participating businesses. Nine participants reported for PAYG and fifteen for BAS on a quarterly basis, in comparison to eight entities for PAYG and two for BAS reporting monthly. Most businesses had either a bookkeeper or an accountant/tax agent to lodge their BAS (12 entities), whereas only nine (53%) of the participating businesses used an external party to prepare their BAS ready for lodgement.

Figure 2 below illustrates that no participating SBOs that derived an annual turnover of between \$5,000,000 and \$10,000,000. This means that the experiences of more sizeable businesses (\$5,000,000 – \$10,000,000) are outside the scope of this stage of the research.

FIGURE 2: GROSS ANNUAL INCOME OF PARTICIPATE SMALL BUSINESSES

The information in Table 1 above illustrates that the trade relationships of the participating SBOs are almost even when comparing business-to-consumer trade and business-to-business trade. Nine participants predominantly carry out their business activities with consumers and eight participants conduct business primarily with other businesses.

Table 1 above also demonstrates that those businesses earning the largest annual income are mostly employing the greatest number of staff. The four SBOs generating an annual income of more than \$2 million employ between 11 and 20 full-time employees. In contrast, those SBOs earning under \$250,000 have only one full-time staff member. It is possible that these micro businesses are simply a vehicle for income generation for the owner. The annual income category of \$500,000 < \$2,000,000 has the greatest employment diversity. Full-time employment figures range from 1 to 17. This variation might be explained by the size of the annual income category. It is difficult to determine whether the full-time employment variation relates to the services provided by the business, as the employee numbers of those running professional businesses (Participants 15 and 17) differ considerably, with one business employing 2 full-time employees and the other employing 10. This circumstance is similar for the two businesses providing food services (ANZSIC Category 'H'). The restaurant employs one full-time employee, whereas the takeaway food provider employs 8 full-time employees. This demonstrates that income size does not necessarily relate to the number of full-time employees, or the services being provided.

Below is a presentation of the results in terms of the cash flow and the tax.

V RESULTS

The results are now discussed in terms of cash flow stability, the impact of taxation and the five Federal taxes considered.

A *Cash Flow Stability*

The interviews started with an initial broad question to provide greater integrity to the research, so as not to 'lead' the small business owner into identifying 'tax' as a cashflow issue. The SBO participants in the case study were asked: '*Does your business consistently meet its short-term cash commitments?*', as this prompts participants to consider overall the effectiveness of their cash flow management. Without this question it could be asserted that there is research bias or that the responses are being directed down a certain path. It is important to establish where tax is placed in terms of other possible constraints.

Eleven participants responded that they do meet their short-term cash commitments; nine responded with certainty that they pay their outstanding debts on time; the two remaining businesses were not as confident:

Yes, actually we do because we have been in business for almost 28 years and we sort of have the experience of how to manage the cash flow and we also know what we are expecting and when payments are due so usually yes (Participant 1).

The six SBO participants who suggested that they did not or have not always paid their short-term commitments by the due date had varying reasons for not doing so. Five of the six business participants suggested it was a result of restricted cash flow, which were predominately a result of debtors not paying within trading terms. This is similar to the findings of Belle Isle, Freudenberg and Copp,⁹³ and those of the Australian Small Business and Family Enterprise Ombudsman,⁹⁴ who found that it is common practice in Australia to receive payments from debtors later than the trading terms offered. Other responses for not paying on time included restrictions on time, business growth and reduced revenue:

The main reason would be cash flow regarding big multi-national organisations taking 90 days to pay us (Participant 14).

Predominately the issue is cash flow. A lot of it is due to business growth, our business has grown, and we have had an increase in payroll and a lot of our revenue is subject to 60-day terms. Obviously, we have to pay our staff on time, so if cash is not received for 60 days our bills have to wait (Participant 4).

Overall, it appears from the limited sample that two-thirds of SBOs are meeting their short-term commitments. Those who suggested that they do not always satisfy their short-term cash commitments had varying reasons for not doing so with the most common response related to late payments from creditors. However, business growth was also evident. It could be possible that businesses in a growth stage incur expenses before they realise growth in revenue. From the feedback, it appeared that the initial

⁹³ Belle Isle, Freudenberg and Copp (n 5).

⁹⁴ Australian Small Business and Family Enterprise Ombudsman (n 61).

responses from SBOs did not raise concerns about the influence of taxation on cash flow.⁹⁵ The interviews were therefore used to explore further information relating to the possible taxation and cash flow relationship.

B Cash flow and Taxation

Questions posed to SBOs, in various formats to attempt to uncover SBOs general feeling regarding the tax and cash flow relationship. More specific questions were then posed about the five tax systems which were the focus of the research. Participants were asked a broad question: *'What does tax mean to your business?'* It was found that not all business owners were negative about the requirement to adhere to tax obligations, as some businesses saw taxes as just another payable and part of doing business:

Taxes are just a payable, it forms part of a cash flow requirement (Participant 2).

Similar to findings of Wallschutzky and Gibson,⁹⁶ small business participants did not convey unfavourable comments about the majority of their tax obligations. The responses from the remaining seven participants were not as favourable. Participant comments related to the general burden of tax obligations:

Taxes are a massive hindrance to my business (Participant 4).

More specific feedback was associated with the time and cost involved in complying. It appears from these comments that the issue may not be the amount of tax but the compliance costs and the complexity of tax:

I think taxes are a bad thing. Just an imposition, none of it benefits me. It's an administrative overhead and there are accounting and bookkeeping costs too and my time (Participant 10).

Similar responses have been evident in compliance cost research since the introduction of the GST. SBOs are concerned about the heavy cost and time burden of tax on their business, particularly in comparison to their larger competitors.⁹⁷ These findings may suggest that there needs to be more focus on decreasing tax complexity and compliance costs for small businesses.

Small businesses were then asked several questions to attempt to explore any common themes associated with cash flow and taxation. The first question asked: *'Is there anything you would like to discuss as to how tax can influence your cash flow?'* Common responses related to the effect of tax on business growth and on the administration of taxes, each of which is discussed below.

⁹⁵ This is similar to the findings of Wallschutzky and Gibson (n 4).

⁹⁶ Ibid.

⁹⁷ Evans et al (n 39); Glover and Tran-Nam (n 39); Lignier and Evans (n 39); Lignier, Evans and Tran-Nam (n 39); Biagio Marco Pizzacalla, 'Developing a Better Regime for the Preferential Taxation of Small Business' (PhD Thesis, Monash University, 2014); Ritchie (n 39).

C Business Growth

At least six SBOs suggested that taxation limits the growth of their business. Comments related primarily to the costs associated with employment tax obligations:

The more people we employ, the more tax we pay so there is no incentive to do so. (Participant 11).

When I think about employing new people, I think two Australian employees are going to cost \$50,000 per year in tax. I could instead use a computer system or offshore services and the cost is a lot less. I'd go with the cheaper way. This is not good for Australia. So, tax hinders business growth (Participant 8).

Three of these responses related to employing staff, which suggests that business growth is restricted due to the requirement to adhere to PAYG withholding or superannuation obligations. Part of the issue with growth might also be that it can involve employing staff who are an immediate cost, however, the income earned from those staff may not be realised until sometime in the future. This feedback is concerning when considering that Australian employment is heavily reliant on the small business sector.⁹⁸ However, recent statistics about small business employment growth — 148% in 2016 when compared to the previous year — indicate that many small businesses are still employing new people despite the apparent discouragement of tax obligations.⁹⁹

D Administration and Timing of Tax payments

Research conducted by the Organisation for Economic Co-operation and Development ('OECD')¹⁰⁰ proposed that overseas businesses experienced cash flow issues from taxation. These issues were related to the timing of the tax payment and the multitude of tax payments required throughout each financial year. The interviews uncovered similar experiences for the SBO participants. The participant responses related to administrative procedures in the first year of trading, to holding the tax liability on behalf of the ATO for lengthy periods of time and to the multitude of payments.

Respondents reflected on the cash flow issues they experienced after the first year of trading. They suggested that more education was required at business start-up in relation to what the likely tax obligations would be at the end of the first year. The cash flow issues related to not paying any tax in the first year of trading and having a large tax liability in the second year as a result.¹⁰¹

⁹⁸ Australian Bureau of Statistics, *Australian Industry, 2018–19* (Catalogue No 8155.0, 29 March 2020); Australian Bureau of Statistics (n 20); Department of Parliamentary Service, *Are Small Businesses the Driving Force Behind Private Sector Employment and Total Industry Value Added?* (Research Paper Series, 17 November 2017).

⁹⁹ Department of Parliamentary Service (n 98).

¹⁰⁰ OECD (n 39).

¹⁰¹ Note: In Australia, lodgement for Income Tax for sole traders, partnerships and trusts is due on 31 October and for self-reporting companies, 28 February, following the end of the financial year on 30 June. The PAYG instalment system does not become an automatic obligation until after businesses lodge their first income tax return (if they meet the threshold). As a result, a tax liability will not be due for start-up entities for up to 16 months for sole traders, partnerships and trusts, and 20 months

Year one of business, I paid nothing all year and then I was hit with a massive tax bill. Now in year two, I prepay¹⁰² some which is a lot better for cash flow (Participant 6).

Participant 12 indicated they were conscious of the fact that they would have a tax liability, and therefore had undertaken some planning (even if it was a rough estimate) to accommodate the tax liability that would be due in the future. Participant 6, in contrast, suggested that it was not until they experienced cash flow constraints that they realised the tax administration problem. It is acknowledged the ATO website suggests that new businesses should enter the PAYG instalment system voluntarily to avoid the situation of little or no cash to satisfy the tax liability at the end of the first year of trading.¹⁰³ Unfortunately, it is not apparent to what extent businesses are aware and/or follow this advice.

Other SBO participants suggested that being a tax collector for the ATO creates a cash-flow problem. With reference to the tax systems explored in this research, businesses are required to collect tax on behalf of the ATO for GST and PAYG withholding. SBOs highlighted cash flow issues arising from the tax liability being held for too long in the business bank account before remitting to the ATO. Comments appeared to refer to PAYG withholding, as they suggested that cash flow would be better supported if the tax liability was paid weekly or was consistent with each payroll cycle:

I don't think it is the actual tax that is the problem. I think it is the time between incurring the tax and the time it is paid that is the issue. If it was not stored in your account for long periods and left weekly, I think cash flow would be easier to manage (Participant 16).

A number of SBOs expressed the requirement for an overhaul of the current tax system, although they were unsure of how the system should be readministered. Their frustrations related to the number of tax systems and the different reporting and payment dates for each system:

There's IAS¹⁰⁴, BAS, super, FBT, company tax and payroll tax. It's quite complicated, there are so many touch points. FBT reporting in April, why is that? There is not much relief for small businesses on taxes (Participant 14).

Nearly thirty years ago in Wallschutzky and Gibson's¹⁰⁵ study SBOs suggested that only the WST had a negative impact on cash flow, whereas the SERC findings suggested that all tax systems would have unfavourable consequences on small business cash flow.¹⁰⁶ The current research, therefore, examined the perception of service SBOs about whether they believed that tax influenced their business cash flow. The following question was

for companies. This could cause a restraint to cash flow if SBOs have not forecasted for such tax liability.

¹⁰² Prepayment relates to PAYG instalment.

¹⁰³ See, eg, ATO, 'How to Start Paying Instalments' (2021) <<https://www.ato.gov.au/general/payg-instalments/how-to-start-paying-instalments/?anchor=Voluntaryentry#Voluntaryentry>>.

¹⁰⁴ IAS is an instalment activity statement used for reporting PAYG withholding tax on a monthly basis or used by taxpayers who are not registered for GST.

¹⁰⁵ Wallschutzky and Gibson (n 4).

¹⁰⁶ Senate Economics References Committee (n 54) [7.1].

posed to the interviewees: *'Do you think it is the tax itself or some other influence that causes the cash flow problem'*? Only two respondents suggested that it was the tax itself that caused a problem for cash flow. Those respondents were from varying ANZSIC¹⁰⁷ service industries. One business resides in category 'N' Administrative and Support Services and the other offers Education and Training classified under category 'P'. Their comments are presented below:

I mean obviously, the tax itself is probably the main issue (Participant 3).

Yes, the payroll tax is the issue (Participant 7).

It should be acknowledged that the response from Participant 7 relates to payroll tax which is a State tax system and outside the scope of this research, but it should be noted that payroll tax can relate to the cost and complication of employing someone.

In contrast, four participants proposed that restrictions in cash flow are not related to tax obligations. Instead, cash flow restrictions were seen to be a consequence of reduced profit margins, a decline in revenue or the health of the economy and trade partners. Respondents 9 and 11, whose businesses both reside within the ANZSIC¹⁰⁸ category 'H' of Accommodation and Food Services, attributed their cash flow constraints to reduced profit margins. This may be a result of their trading partners, as both participants 9 and 11 are involved in business-to-consumer transactions, and prior research by Belle Isle, Freudenberg and Copp¹⁰⁹ found that small businesses with consumers as trade partners appear to have problems settling tax liabilities due to low profit margins:

Profit margins are not large enough at all and everything has increased especially food prices. I look at menus from 10 years ago, we have probably increased a pasta dish by \$2 in 10 years. (Participant 9).

Participant 1, who also trades with consumers (classified under category 'G' Retail Trade), suggested that cash flow is inhibited by a decline in revenue or the health of the economy and not the tax itself:

I think it is consumer appetite for spending and the overall economy. If the economy is not healthy then people don't spend. Also, our trading is seasonal. We are very busy over Christmas but quiet when school goes back. We still have wages, rent and other overheads to pay (Participant 1).

The last remaining SBO (Participant 13) who did not consider tax as the cash flow problem suggested that their choice of trading partners was the problem. In contrast to Participant 9 and 11, who trade with consumers, Participant 13 trades with other businesses, offering Technical Services (Category M) for the Mining Industry:

Tax is not the big issue for my cash flow, the problem is that I deal 95% with business customers. Extremely large businesses in the Mining Sector. Although they are on 60-day payment terms, we are not receiving funds until six months later. That could equate to an invoice for \$130,000 (Participant 13).

¹⁰⁷ Australian Bureau of Statistics (n 83).

¹⁰⁸ Australian Bureau of Statistics (n 83).

¹⁰⁹ Belle Isle, Freudenberg and Copp (n 5).

This response from Participant 13 appears to be an example of issues experienced by other small businesses, as reported in the Payment Times and Practices Inquiry.¹¹⁰ Large businesses have been associated with delaying payments to small entities for longer periods than is specified in the small business trading terms.

The remaining businesses indicated that cash flow problems are experienced due to the combination of tax obligations and other outgoings associated with running a business. Two participants associated cash flow problems to tax and terms of trade. For example:

We are tendering a \$55,000 contract. If we get that contract our payroll goes up straight away for new staff and we will need new equipment. The money has to come from somewhere and it will be 45 days before we get paid for the work (Participant 4).

Other participants stated that it is a multitude of business transactions that together hinder cash flow. This combination of issues included repairs and maintenance costs, variations in revenue, fixed costs and taxation.

In summary, initial responses from SBO participants in the interviews indicated that the cash flow of most of the case study businesses is stable. Two-thirds of participants reported that they settle their short-term debts on time. Similar to the findings by Welsh and White,¹¹¹ those businesses that expressed concerns with settling short-term debts proposed that this was associated with cash being held in overdue debtor invoices.

The interview was then used to investigate how participants viewed taxation generally and in connection with their cash flow. One-quarter of service SBOs gave favourable feedback in relation to taxation, believing that tax obligations are a normal part of operating a business, treated like any other liability. The remaining participants had opposing views on taxation, implying that it was a burden for their business, resulting in extra time and cost in order to comply.

The case study identified that SBOs were not inspired to grow their businesses due to the influence that tax would have on their cash flow, especially in relation to employment related taxes. Concerns for cash flow also related to the timing of tax payments and the multitude of tax obligations.

Whether it was the tax or some other business factor that was affiliated with restrictions in cash flow, the results indicate that the majority (15 out of 17 participants) did not consider taxation as being the sole cause of cash flow problems. Consistent with research by Belle Isle, Freudenberg and Copp¹¹² trade partners (low profit margins and/or extended trade terms) appear to be of more concern to cash flow. Other business factors, such as variations in revenue, repairs, maintenance and fixed costs plus taxation, were considered to cause restrictions to cash flow.

¹¹⁰ Australian Small Business and Family Enterprise Ombudsman (n 61).

¹¹¹ Welsh and White (n 24) 26.

¹¹² Belle Isle, Freudenberg and Copp (n 5).

E Federal Tax Systems and Cash Flow

Following the generalised questions relating to taxation and cash flow, SBO participants were asked more specific questions associated with the five Federal tax systems focused on for this research project. Participants were asked ‘*Do some taxes affect your cash flow more than others?*’ and ‘*Can you rank them from having the most to the least effect on cash flow and discuss why?*’¹¹³ Some respondents suggested that it was the combination of all five of the tax systems, while other replies focused on specific tax systems.

1 The Combination of All Five Tax Systems

Responses relating to the aggregate effect on cash flow of all five tax systems primarily focused on being a tax collector for the ATO. For GST there is some theoretical contention that the tax collected should create a cash flow benefit for the collecting entity.¹¹⁴ However, research suggests that small businesses rarely recognise any benefit because of market conditions or late payment by trade debtors.¹¹⁵ Responses from SBO participants supported prior research, as service SBOs emphasised their concerns about the impact on cash flow coming from being a tax collector. Further concerns related to the tax component that would be due to the ATO at a later time, giving service SBOs a false impression of cash flow levels of the business (it should be recalled that many small businesses just use the balance of the cash at bank as an indicator of the health of their business)¹¹⁶:

A combination of all of those taxes affects cash flow. When you're collecting money for the Government, it's not set up to benefit small business. It would be better if that money never came in. It makes life very difficult (Participant 4).

The combination of all taxes may also relate to the fact that with multiple taxes to manage (with different tax rules and different due dates) there may need to be more skill required of the service SBO to manage the multiple taxes as opposed to just one or two taxes. The remaining comments by service SBOs regarding effects on cash flow were more specific to one or more of the individual tax systems within the research. Details are discussed below.

2 PAYG Withholding

The largest number of SBOs in the case study perceived PAYG withholding and GST to have the greatest impact on their cash flow. Participants 2 and 5 could not differentiate between the two tax systems, and suggested that they both impede their cash flow. For example:

¹¹³ It was explained to participants that these questions only related to the Federal tax systems involved in the research project.

¹¹⁴ Peter Costello, ‘Tax Reform: Not A New Tax, A New Tax System’ (Australian Government, 1998) Foreword; Cedric Sandford, ‘Minimising the Compliance Costs of a GST’ (1998) 14(2) *Australian Tax Forum* 125.

¹¹⁵ Belle Isle, Freudenberg and Copp (n 5).

¹¹⁶ Evans, Carlon and Massey (n 28) 300.

It's a toss-up between GST and PAYG withholding. Both have a large effect on my cash flow (Participant 2).

Five SBOs indicated that PAYG withholding had the largest impact on their cash flow. A common response, even from those who did not report PAYG withholding as having a significant impact, was that PAYG withholding should be paid out regularly to avoid disruption to cash flow:

PAYG is most difficult, but I pay it monthly which is good because it allows it to be spread out rather than having it all in one hit (Participant 15).

This comment also has a nexus about being a tax collector for the ATO. PAYG withholding is a tax collected on behalf of employees and paid sometime in the future to the ATO. These findings support prior literature suggestions that collecting tax on behalf of others can have negative consequences for the cash flow of small businesses.¹¹⁷

The extent of the PAYG withholding liability was another concern for some service SBOs. Those participants who discussed the magnitude of the PAYG withholding liability all employed eight or more full-time staff:

To run our store, we have a lot of staff so our PAYG per month is between \$6,000 and \$10,000. So just when you think you're making headway, there goes another \$10,000 because we have to pay PAYG (Participant 11).

In summary, SBO participant responses indicate that those businesses with large numbers of employees reported having difficulty managing cash flow due to the size of the tax PAYG withholding liability. Other SBO participants were concerned with the frequency of remitting the PAYG withholding liability to the ATO. Feedback suggests that cash flow could be easier to maintain if the PAYG withholding liability is paid more frequently to the ATO, reducing the 'shock' of a big tax payment.

3 Goods and Services Tax

As already noted, GST emerged as one of the most concerning taxes for the SBOs involved in the case study. As found in research by Belle Isle, Freudenberg and Copp¹¹⁸ restrictions on cash flow appear to be associated with low profit margins, absorbing the GST on sales and not receiving the GST liability from invoices prior to the date that the tax liability is remitted to the ATO:

GST has the most effect on cash flow because it is such a huge amount. For small business, GST is a lot of money every quarter. There is so much competition in our sector that we can't charge higher prices, so we are not making as much to cover all of our taxes easily (Participant 9).

I'd say GST most affects my cash flow. I was late paying once because a debtor hadn't paid me on time. I had to use other cash to keep the place running (Participant 8).

As for prior research, the limited sample indicates that compliance with the GST affects the cash flow of small businesses This could be attributed to other business factors'

¹¹⁷ Ahmed and Braithwaite (n 41) 539; Evans, Carlon and Massey (n 28) 290; OECD (n 39) 90.

¹¹⁸ Belle Isle, Freudenberg and Copp (n 5).

market competition, the incidence of the tax liability, the variability of incoming revenue and the trade partners of the SBOs.¹¹⁹

4 *Fringe Benefits Tax*

Just under one quarter (four of seventeen) of participant SBOs reported for FBT. Apart from Participant 14 giving unfavourable feedback about the difference of the reporting year for FBT in comparison to other taxes, there were no other negative responses about complying with FBT. None of the FBT complying businesses made any comments about the effect of FBT on their cash flow. This may be due to the small number of SBO participants who comply, or it could be that FBT has minimal consequences to small business cash flow. The requirement to pay an FBT instalment was adhered to by only one of the four complying entities. The effect that FBT instalment has on cash flow did not appear to be of major concern to this participant, as there was no mention of it having any positive or negative impact to that participant's business. This finding suggests that the requirement to pay tax in advance has minimal or no impact on small business cash flow, which contradicts research conducted in the UK.¹²⁰ Alternatively, the results could be a consequence of the low amount of FBT liability required to be paid by the complying SBO participants. The payment of tax in advance is explored further below regarding income tax.

5 *Income Tax and PAYG Income Tax Instalment*

Four business participants recollected their experiences with income tax. Only one participant suggested that income tax had the largest effect on their cash flow, in comparison to the other taxes. The remaining comments were all associated with the PAYG income tax instalment. An equal number of negative and positive comments were made about the PAYG instalment. Two participants suggested that the PAYG income tax instalment was beneficial to their cash flow position. For example:

Certainly, income tax affects our cash flow the most. If I wasn't paying throughout the year, I'd get a giant chunk of tax owing at the end of the financial year. The quarterly instalment actually made my cash flow look better (Participant 3).

The comments from the remaining two participants were not as favourable. It appears that the instalment payment made it easier to satisfy the obligation at the end of the financial year. However, participants were concerned that the instalment amount was based on previous income and noted the missed opportunity to earn interest on the money paid throughout the financial year. For example:

From an income tax perspective, I think it is more the tax instalment that creates a cash flow problem. I know it is better to have some money sitting elsewhere over that year that we can access later to satisfy our final income tax bill, but that money once paid to the ATO is of no benefit to my business. It benefits the ATO. They will earn interest on that money and if it isn't needed at the end of the financial year because our obligation

¹¹⁹ Ibid 424; Evans, Carlon and Massey (n 28) 310.

¹²⁰ Messina and Walton (n 8).

wasn't as large as expected then that money would have been more useful in our bank account (Participant 16).

The data indicates that service SBOs agreed that paying an income tax instalment was of some benefit in helping them manage their cash flow in order to settle their income tax liability at the end of the financial year. The only unfavourable feedback related to paying an instalment amount that may not be indicative of current earnings of the business, and the opportunity foregone by not having the income earning interest in the bank account of the SBO.

6 *Superannuation Guarantee*

The impact of SG on cash flow did not appear to be a major concern for case study SBO participants. Only three participants commented on SG and of those participants, only one service SBO suggested that SG created a financial burden on their business.

Every three months there goes another \$15,000–\$20,000 because of super (Participant 11).

The remaining two SBO participants were more concerned with the administration of SG. One participant was concerned about the requirement to transfer funds to a Superannuation Clearing House up to five days before the due date, in order for the money to be received, and in turn to be able to claim the tax deduction. The other participant suggested that if SG was remitted more frequently it would be easier to manage.

I think super should be paid more often than quarterly as it is easier to manage cash flow that way. It should be monthly or automatically go at the time of paying employees (Participant 16).

These findings suggest that there is minimal concern regarding SG, when compared to the other four tax systems within the research project.

7 *Summary of the Relationship Between Cash Flow and Taxation*

Analysis of the data collected in the semi-structured interviews suggests that SBOs have minimal concerns for their cash flow when complying with their tax obligations for FBT, income tax and SG. In contrast to prior research in the UK, SBOs in Australia found benefits from paying tax in advance. Respondents identified the payment of a PAYG instalment as a useful tool in managing cash flow throughout each tax year. Common responses from SBO participants suggest that more regularity in making payments would assist them to keep control of cash flow, especially in regard to employment related taxes.¹²¹ Other business factors were recognised as adding to the financial burden of the GST include the choice of trade partners, the market competition and the incidence of the tax liability. Overall, the tax systems reported to be causing the greatest disruption to cash flow were PAYG withholding and GST. SBOs with PAYG withholding and GST obligations are effectively collecting tax on behalf of the ATO. This could suggest that the PAYG

¹²¹ Superannuation and PAYG withholding.

withholding and GST compliance burden impacts service SBOs ability to manage cash flow.

F Relationship Between the Small Business Demographics and the Case Study Findings

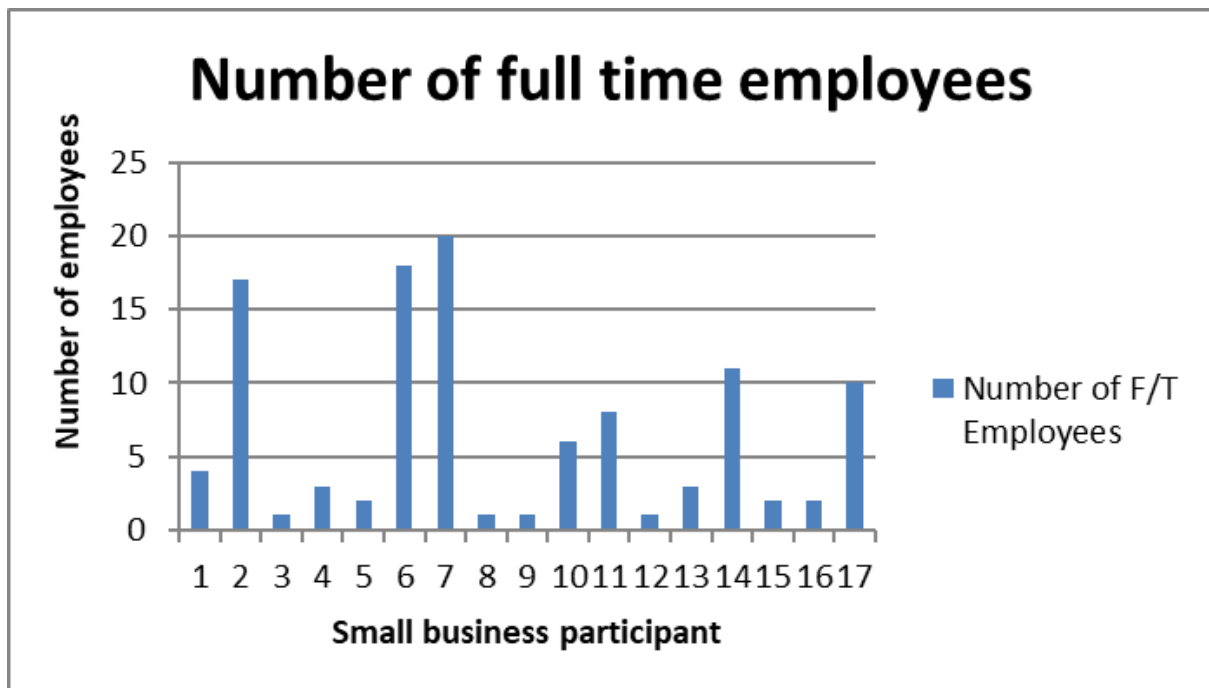
1 Demographics and SG, FBT and Income Tax

Due to the limited sample of SBOs in the case study and the limited feedback given about the effect of SG, FBT and income tax on cash flow, comparative analysis with participant demographics is limited to PAYG Withholding and GST.

2 Demographics and PAYG Withholding

Those businesses employing the highest number of full-time employees seem to have their greatest concern with PAYG withholding. However, this assumption cannot be fully satisfied because the second largest employing participant (Participant 6) suggested that GST and income tax were as burdensome as PAYG withholding. Figure 3 below illustrates the number of full-time employees engaged in each business. SBO participants 2, 5, 7, 11, 15 and 17 were concerned that cash flow was restricted as a result of PAYG withholding. Analysis of Figure 3 below demonstrates that only three of those participants (2, 7 and 17) employ 10 or more full time employees. This suggests that regardless of the number of employees, PAYG withholding may be restricting the cash flow of SBOs. It may be that as a business grows, in terms of employee numbers, more sophisticated measures are adopted to help manage cash flow, in terms of PAYG withholding and SG.

FIGURE 3: THE NUMBER OF FULL-TIME STAFF EMPLOYED BY SMALL BUSINESS PARTICIPANTS



3 *Demographics and GST*

Analysis of the demographics and data collected suggests that the GST hinders cash flow more than any other tax system in the research. It should be acknowledged that the SBO participants who reported concerns about cash flow and the GST were entities that would generally be required to charge GST on the services they provide. With participants 1, 2, 5, 8, 9, 10, 14 and 16, who reside in categories G, E, K, M, H, J, P and E respectively, all charge GST on their services.

In comparison to those who reported PAYG withholding as having the greatest influence to cash flow stability, three of the seven participants SBOs reside in industries where their services are GST Free.¹²² Participants 7, 15 and 17, which provide Early Education, Psychological and Dental services respectively have businesses in the ANZSIC categories of Education and Training, Health Care and Social Assistance. Health Care and Education are predominantly GST-Free industries in Australia.¹²³ Therefore it would be unlikely that these SBOs would perceive the GST to have a significant negative influence on their cash flow, as they are likely to be getting a refund of GST input tax credits on purchases.¹²⁴ It could therefore be suggested that the GST recorded the highest number of unfavourable comments regarding its effect on cash flow. Eight of the fourteen (57%) SBOs that charge GST on their services, perceived the GST to affect their cash flow on a larger scale than any of the other taxes in the research. It is likely that GST liability on taxable supplies¹²⁵ for these businesses would exceed their GST input tax credits,¹²⁶ therefore giving them a net GST liability to the ATO. These results are consistent with research conducted by Wallschutzky and Gibson¹²⁷ in the 1990s. As noted earlier, the tax system causing the greatest burden to small business cash flow at that time was the WST, which was replaced by the GST.

G *Summary of the Tax and Cash Flow Case Study Findings*

From the demographic data it was found that all participants reported for PAYG withholding, income tax, GST and SG. However, only four participants lodged a fringe benefits tax return. Initially the perception of service SBOs was explored in terms of their ability to meet their short-term cash commitments. One-third of the SBO participants suggested that they faced constraints in paying their short-term obligations on time. The common response for this inability was because of their trading partners paying outside of payment terms. Taxation was not a cause of concern for the ability of SBOs to settle short-term commitments. It therefore seems that the ability of service SBOs to manage their trading terms and trading partners could be more important than tax.

¹²² *GST Act* (n 11) Div 38.

¹²³ *Ibid.*

¹²⁴ *Ibid* s 11-5.

¹²⁵ *Ibid* s 9-5.

¹²⁶ *Ibid* s 11-5.

¹²⁷ Wallschutzky and Gibson (n 4).

The general perception that service SBOs had towards taxation was then examined to determine whether cash flow of Australian small businesses is influenced by tax obligations. Most participants viewed it as a business obligation and part of carrying on an enterprise. Service SBOs proposed that tax can be administratively difficult, especially the number of tax obligations for businesses in each tax year. Taxation was also identified as being an inhibitor to business growth. Service SBOs suggested that taxation was a deterrence to employing staff, due to the requirement to pay SG and PAYG withholding.

The five Federal tax systems within the research were then explored. Service SBOs were asked if any of the taxes have a greater influence on cash flow than the other tax systems. A small number of SBO participants suggested that the overall tax obligation was detrimental to their business cash flow, whereas other participants focused on specific tax systems. In particular, GST and PAYG withholding were identified as having the greatest detrimental effects on cash flow, which are taxes collected by businesses on behalf of the ATO. In contrast, the PAYG instalment was seen to be a beneficial cash management tool which allowed service SBOs to stay abreast of their tax liabilities. The majority of the SBO participants proposed that cash flow constraints cannot be solely explained by the obligation to pay tax. Other factors involved in the tax and cash flow relationship include business trading terms, profit margins, market competition and revenue restrictions.

Comparative analysis of the demographic information and the data collected in the interviews suggests that the majority of the SBOs recognised cash flow concerns from complying with the GST, with the exception of those SBOs that reside in industries that are predominantly GST Free or who are suppliers of services that are input taxed.

Overall, taxation can be seen as an inhibitor to growth, especially with the tax obligations around employing staff and the multitude of administration requirements around complying with FBT, GST, income tax, PAYG withholding and SG. The influence of specific tax systems on SBO cash flow is evident. GST is followed by PAYG withholding in being viewed as the most problematic tax systems for SBO cash flow. In contrast, PAYG instalments are considered to be a beneficial mechanism for managing and preventing cash flow constraints.

Overall, the research findings suggest that, regardless of the tax system, SBOs believe that taxation has minor consequences for small business cash flow. The research outcomes identified that some components of tax administration can create cash flow constraints including the requirement to comply with multiple tax systems, rather than being related to the obligation to pay the tax liability.

VI RECOMMENDATIONS

Given that it appears that the findings suggest that it is not 'tax' itself that is the core problem to cash flow, but the practices and management of cash flow broadly, which tax

is just one part of. This would tend to suggest that initiative of the ATO of developing the Cash Flow Coaching Kit for advisors to support their business clients makes sense.¹²⁸

The findings of the research have also emphasised that improved trading terms and/or adherence by debtors to the payment terms appears to be very important for small businesses. If small businesses are not paid on time then they could be liable for tax payments prior to receiving actual payment. This would indicate that the recommendations by the Australian Small Business and Family Enterprise Ombudsman should be given careful consideration, such as the establishment of the National Payment Transparency Register to highlight Australian businesses that pay small business suppliers in 30 days or less, and provides performance against payment practices.¹²⁹ Other recommendations are industry codes which regulate business to business transactions to include best payment practices including set payment times for particular industries.¹³⁰

Additionally, it appears that during times of business expansion tax can be problematic for cash flow, which can include the appointment of employees. Appointment of employees can cause cash flow restraints given that the potential increase in revenue could take a while to be received while employment expenses can increase more immediately. Also, employment can lead to increased compliance time and cost for the business. To address this, consideration should be given as to whether there is a way to alleviate the additional tax impost and compliance cost for employing someone by a small business. It may be that the lower corporate tax rate should be only available to those corporations that meet a certain employee threshold, as the engagement of employees is a good indicator of a business contributing to the economy, as well as addressing the additional employer obligations that can arise when employing someone. Currently, the low corporate tax rate is freely available to corporations meeting the income threshold and with at most 20% passive income.¹³¹ Providing an additional 'employment' requirement may provide for a better targeted concession, as well as providing some compensation for the additional compliance and regulatory costs involved in employing someone.

Also, consideration should be given to whether the number of tax obligations could be condensed so there are less reporting and payment dates for small businesses. Given advances in technology and reporting obligations, consideration should be given to the possibility for small businesses to make real time instalments of GST and income tax on

¹²⁸ See, eg, ATO, 'Cash Flow Coaching Kit' (2021) <<https://www.ato.gov.au/Tax-professionals/Support-and-communication/In-detail/Cash-flow-coaching-kit/>>.

¹²⁹ See Australian Small Business and Family Enterprise Ombudsman (2021) <<https://www.asbfeo.gov.au/sites/default/files/documents/ASBFEO-NPTR-240718.pdf>>.

¹³⁰ Australian Small Business and Family Enterprise Ombudsman (n 61).

¹³¹ From the 1 July 2017 income year, the lower corporate tax rate is available for 'base rate entities', now defined to exclude corporate tax entities that have more than 80% of assessable income that is passive income (such as interest, dividends, rent, royalties and net capital gains). The entity's aggregated turnover must also be less than the relevant threshold for the year in question (\$25 million in 2017-18 and \$50 million in 2019 to 2024).

receipt of payment from debtors to the ATO. In conjunction with this, it should be explored whether a 'tax bank account' could be held through the ATO. Such a tax bank account would be entitled to interest and would not be immediately accessible to the ATO. In this way, such money is held separate to the businesses' other trading funds but is still available to the business if need be. This account then could be used to formally pay the ATO at the required payment time.

Given the concerns raised about GST, it may be that businesses need more awareness of the cash basis for GST, so they can better match their tax payments to when they actually receive the funds. This is important, as all of the participants in the current study would appear to be eligible to account for GST on the cash basis given that their turnover is less than \$10,000,000. In this way, a business may report GST on a cash basis and then income tax on an accrual basis. However, this mixture of derivation methods could itself add complexity.

Also, there needs to be greater awareness that a business in its first year of operation can voluntarily enter into the PAYG instalment system in terms of paying an estimated income tax liability. There appears to be low awareness that this currently exists, as recently the Ombudsman called for this reform even though it is already in existence.¹³² This could involve the ATO contacting new ABN registrants in the first six months of registering about the option to voluntarily make PAYG instalments. Fundamentally, if a small businesses tax reporting and payment can become a natural part of the process of the business this will aid compliance, and the ability to manage tax as part of the business cash flow.

VII LIMITATIONS AND FUTURE RESEARCH

There are a number of limitations of this study that should be acknowledged. Firstly, the study only explored the perception of SBOs, the actual practices or consequences of tax on cash flow for small service sector businesses could be different. Also, this research is based on sensitive information related to small business management practices, and SBOs may have felt inclined not to be fully frank with their answers. Additionally, the study focused on those businesses in the service sector and does not explore other sectors including Manufacturing, Agriculture, Forestry and Fishing or Mining. The participant small businesses also were not representatives of all service sector classifications. While the sample size is small, the case study provided some rich data that may be the basis for future research, such as an expanded qualitative study replicating the case study method used in this project. This could address the limitations recognised for the small number of participants, the exclusion of businesses not residing in the service sector and the service sector classifications not covered in the existing research. Research could also explore other variables that may influence cash flow, being the ability of SBOs to

¹³² Australian Small Business and Family Enterprise Ombudsman, *A Tax System that Works for Small Business* (Canberra, 2021) Recommendation #10(b).

implement effective cash flow management practices and the level of tax literacy of the SBO.¹³³

VIII CONCLUSION

In terms of cash flow, research has suggested that Australian SBOs do not believe that taxation is particularly concerning.¹³⁴ The findings emphasised that other business factors, including trading partners, competitive markets and cash flow management abilities were relevant to being able to pay the tax liability when it was due and payable. Although the previous WST did have some concerns for SBOs, more recent research into the GST,¹³⁵ also raised concerns about the ability to maintain a consistent cash flow as a result of complying with GST obligations.¹³⁶

Service SBOs in the case study reported that GST, PAYG withholding, and SG can have negative consequences for cash flow stability. In particular, the amount of the tax liability for PAYG withholding and SG, when paid to the ATO each quarter, can result in cash flow constraints. These employment-related business taxes were also identified as being inhibitors for growth, as service SBOs explained that they were hesitant to employ new people due to the associated employment costs. Service SBOs expressed that their greatest concern for cash flow came from complying with GST. However, it should be acknowledged that, as in prior research,¹³⁷ the negative impact of GST on cash flow is due to a combination of business factors that includes market competition, the variability of incoming revenue and the non-receipt of payments from trade debtors before the GST liability is due to the ATO.

It would appear that overall small businesses need some assistance in managing their cash flow. While tax can influence cash flow in some adverse ways, it is other business factors that appear to have a greater detrimental effect, especially non-adherence to payment terms. With this understanding a number of recommendations were formulated to assist small businesses manage their cash flow, and thereby improve their stability and ability to add to the economy.

¹³³ Belle Isle and Freudenberg (n 23); Freudenberg et al (n 38).

¹³⁴ Wallschutzky and Gibson (n 4).

¹³⁵ The successor of the WST.

¹³⁶ Belle Isle, Freudenberg and Copp (n 5).

¹³⁷ Ibid; Wallschutzky and Gibson (n 4).

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