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Newsletter

24 March 2011

Income tax changes

1 Tax rate reductions continue to have an effect

The last round of personal tax rate reductions took effect from 1/10/10. This means the upcoming financial year from 1/4/11 – 31/3/12 will be the first full year for these lower rates to apply

The rates are:

<u>Income Level</u>	<u>Rate</u>
\$0 - \$14,000	10.5%
\$14,001 - \$48,000	17.5%
\$48,001 - \$70,000	30.0%
\$70,000+	33.0%
Companies	28.0%
Trusts	33.0%

2 Tax credits attached to Dividends

With the introduction of the 28.0% company tax rate there is greater incentive to retain income in the company to achieve the lowest possible tax rate.

However, when the company tax rate was reduced, the Government did not reduce the amount of 'credits' which must be attached to a dividend. This remains at 33%, - 28¢ of these are allowed to come from company tax paid (imputation credits).

The other 5¢ of 'credits' must be paid as Withholding Tax to IRD on the 20th of the month following the dividend – as DWT – dividend withholding tax.

Financial year end for 2011

Below are a number of common matters that you need to consider to ensure correct year end tax calculations.

1 Trading Stock at balance date

A stock take is required unless the closing value is less than \$10,000 and your turnover less than \$1.3 m.

Only in these circumstances stock value can be estimated. Always value at cost less GST.

2 Holiday pay and bonuses

If these are to be claimed in the accounts and accrued at balance date, (31/3) they must be paid within 63 days of balance date, ie 2/6/11.

3 Bad debts

To be claimed these must be written off before 31 March out of the debtors ledger. There must be clear evidence this has been done.

4 Foreign investments

For investments in foreign companies you need to list and value them as at 31 March 2011. This forms the basis of income calculations under the Foreign Investment Fund (FIF) regime.

If you are using a fund manager they should do this for you.

5 Fixed asset review

Look at your fixed asset schedule from last year's accounts and advise us of any that have ceased to be of use, or are broken or have been disposed of.

Other tax changes

1 GST

- (a) From 1/4/2011 there are new rules applying to GST on the sale of land.

GST registered vendors will be required to charge GST at the rate of 0% on any supply, to another GST registered person, that wholly or partly consists of land, if at the time of settlement:

- The recipient intends to use the goods for making taxable supplies, and
- The supply is not a supply of land intended to be used as the principal place of residence of the recipient or a person associated with the recipient.

Note:

- i) the purchaser has an obligation to provide to the vendor advice of their registration status and intentions in respect of the land
- ii) the definition of 'land' excludes most commercial leases
- iii) for transactions entered into before 1/4/11 but for which the time of supply is after 1/4/11, the supplier has the option of treating the transaction as being governed by either the current GST rules or the new rules.

(b) Private use adjustments on cars

As of 1 April the rules for calculating private use adjustments on vehicles for sole traders and partnerships have been simplified.

By way of example, if you expect business usage to be 80%, then you simply claim 80% of the GST on the cost of the car and any running expenses. Sounds logical, some would say obvious (accountants have been suggesting this to IRD for years).

If you underestimate your private usage by 10% or more, or if any GST over-claimed due to such underestimating comes to more than \$1,000, an adjustment has to be made.

There's a wash up calculation when you sell the car and it can be complicated.

Call us so we can assist.

2 Redundancy tax credit

Redundancy payments made on or after 1/4/11 will no longer be entitled to this tax credit.

3 New tax depreciation rules

From 1/4/11 depreciation cannot be claimed on buildings with a useful life of 50 years – these are houses and commercial buildings – not milking sheds, hay or wintering barns.

Depreciation can be claimed on the fit-out of commercial and industrial buildings.

The law has been clarified so that commercial and industrial fit-outs remain depreciable property.

Items of fit-out that are shared between commercial and residential purposes, eg, lifts, electrical cabling, fire protection, sewerage and water reticulation, in a mixed-purpose building, will be depreciable if the dominant purpose of the building is commercial.

A definition of "dwelling" has been added that excludes a number of types of buildings that provide residential-type accommodation. This ensures that fit-outs associated with these buildings will continue to be depreciable property. The types of buildings that will be specifically excluded from the meaning of dwelling are:

- hospitals
- hotels, motels, inns, hostels and boarding houses
- certain serviced apartments
- camping grounds
- convalescent homes, nursing homes and hospices
- rest homes and retirement villages - from hospital care through to residential care facilities.

A new rule will allow commercial building owners, who don't itemise building fit-out separately from the building cost, to record up to 15% of the building's cost, claimed at 2% straight-line per year until the building is sold.

Residential fit-outs not depreciable

Residential fit-outs are generally non-depreciable.

4 Minimum family tax credit increase

From 1/4/11 the after tax income level will raise from \$21,008 to \$22,204 per year.

Farmer clients – especially dairy farmers

Careful planning to your balance date of 31 May is needed this year. We suggest, you compare gross monthly milk income to last year, calculate the increased income, and plan wisely to prevent Inland Revenue Department being the main benefactor.

We suggest – spend, using this formulae:

- 1 ⅓ on claimable expenses
- 2 ⅓ on debt repayment – or on capital purchases, development costs
- 3 ⅓ retained for tax, or pay to IRD early voluntary Provisional Tax (especially for a company or trust)

If no, or very low debt, no problem with a new kitchen, or personal spending – but retain that ⅓ for taxation.

Do not overlook a Farm Study Tour – like Farm to Farm Tours, from Rangiora – usually 50% claimable, and a great experience to USA, Europe, UK, Ireland, Wales, or Australia.

If unsure of your net income position – we are available as an extra service, to process your accounts promptly before your balance date – and calculate income earned to date – livestock numbers are needed. Tax is avoidable – you need to plan to achieve a good tax paid result.

Māori Authority update

If you're a Māori authority the tax rate will reduce to 17.5% on 1 April 2011. Māori authorities are taxed as a proxy for their members. The tax rate was 19.5% as this was the marginal tax rate of most people who received distributions from Māori authorities. With the change in personal tax rates effective from 1 October 2010, the Māori authority tax rate has been re-aligned. The Government chose the 17.5% rate as this is the marginal tax rate that applies to most recipients, and RWT rate on interest to Māori authorities.

Working for Families (WFF)

There has always been a difference between a person's assessable income for taxation calculations and their income for Working for Families.

From 1 April 2011 the definition of 'family income' for Working for Families calculations has been widened to include an extra nine types of income.

This will have an immediate effect on WFF credits you can receive, especially for those who are self-employed. There is a real danger now to receive WFF monthly – it is always spent - then to have to repay it at year end plus penalty to IRD, due to these changes.

1. Attributable trustee income
2. Attributable fringe benefits
3. PIE income other than registered superannuation schemes such as Kiwisaver and retirement benefit schemes
4. Passive income earned by children (includes interest, dividends and rent). Amounts over \$500 per child will be included as family income
5. Worldwide income received by a non-resident spouse
6. Tax exempt salary or wages under specific international agreements
7. Income equalisation deposits made by you, your trust, or a company controlled by you or your trust
8. Certain pensions and annuities – includes 50% of payments from life insurance policies or a superannuation fund (excludes NZ super)
9. Other payments received from any sources that are used for your family's day-to-day living expenses (but only if the total amount from those sources is more than \$5,000). An example of this might be board received.

In future, when you apply for WFF tax credits, you'll need to let IRD know about amounts from any of the above sources.

If you receive or are entitled to WFF credits, when we prepare your 2012 tax return, this extra information will be required. It will be more difficult to obtain WFF from 1/4/2011.

Gift Duty to be abolished

Gift duty has been with us for 125 years but it is to be abolished.

It was established in 1885 and worked in conjunction with Estate (Death) Duties to discourage individuals from gifting away their assets prior to death, and to raise revenue.

Estate Duty was abolished in 1992, but Gift Duty was preserved to provide protection for creditors (to stop you giving away your assets) and to stop people taking advantage of social assistance regimes (eg giving away your assets to qualify for a rest home subsidy).

Since the 1970's when you have gifted money (or assets) away (usually to a Family Trust) you have had to pay gift duty on any gift over \$27,000.

It usually operated when people 'sell' an asset, like a family home, to a trust at Market Value, and in exchange take an interest free, on demand loan for the amount owed. The loan is then progressively forgiven at the rate of \$27,000 a year. For high value assets such as a home, this progressive gifting takes a long time.

It is now to be abolished as a review by the IRD showed it generated high compliance costs (estimate \$70m) compared to the small amount of revenue generated (\$1.6m in 2009/2010 year).

There were also a large number of requests for the threshold to be raised to reflect modern values.

Concerns

- The abolishment could result in difficulties enforcing personal guarantees when the guarantor has given away all his assets.
- Social assistance programmes – individuals could deliberately impoverish themselves to qualify for Rest Home Subsidies, Working for Families and other such programmes.
- Relationship property – assets could be gifted away to a trust controlled by just one spouse or partner thus defeating a claim by the other spouse.
- Contesting wills – if all assets have been gifted away then spouses, partners, children, grandchildren will have no assets to claim against.

- A significant rise in the formation of Trusts and an increase in the number of transfers into trusts.

However, the IRD deems these risks as low and have suggested policy changes to counter any abuse of trusts – such as the Ministry of Social Development extending the period to take into account any asset transfers made within recent years of an application for social assistance.

Other law protecting creditors is considered sufficient, although it could be a costly process to go to the courts to set gifts aside or to review relationship property.

Trust administration

While the new law removes gift duty it does not remove the requirement to record, appropriately, gifts made. Gifts should still be documented where assets are transferred to a trust, mortgage payments are made on behalf of a trust or personal funds are spent on the renovation of the family home.

Trustees must still regularly review the trust's affairs and continue to ensure trust minutes are maintained to avoid any sham trust agreement.

Conclusion

The abolition of gift duty will present difficulties and a need to ensure correct documentation of trust matters and a need to consider and possibly change previous business practices.

Expect some changes in other areas, (see in this newsletter, Attributable trustee income needing to be included for Working for Families).

The abolition will also present opportunities, one of which will be the ability of a current account to be gifted to another entity, eg company current account to be gifted to a trust for creditor protection reasons.

Call us to help you manage and take advantage of these changes.

Qualifying Companies, LAQCs

Over the past few weeks we have been communicating regularly with clients affected by the far reaching LAQC reforms that come into play on 1 April 2011 this year. We've commenced a personalised review of each client LAQC and you will be advised of the best alternative replacing the LAQC for you.

Employment law changes

Changes to both the Holidays Act and the Employment Relations Act will come into force on 1 April 2011. These changes are intended to reduce compliance costs, increase business confidence in recruiting new staff as well as speed up the resolution of workplace disputes. The main changes include:

- Employees will be able to cash in one week of their four weeks' leave
 - Employees who have irregular working hours and pay will now have their holiday, sick and bereavement leave calculated on an average daily pay basis
 - Employers and employees will be able to agree to transfer taking a public holiday to another working day
 - The minimum wage will increase from \$12.75 to \$13.00 from 1 April, while the training and new entrants' minimum wage will rise from \$10.20 to \$10.40, effective as of the same date
 - The 90-day trial period is being extended to all employers (currently limited to those with less than 20 employees). From 1 April employers and employees can enter into an employment agreement which provides for a trial period of 90 days or less. During the trial period the employer can dismiss the employee without risking a personal grievance
- Employers will have to keep detailed personal files for each employee. These files must contain signed copies of employment agreements, other terms and conditions, handbooks, as well as any intended agreements (even where these have not been agreed to by the employee). These documents must be available to employees on request. Employers have until 1 July to get their files up to the new standard. We estimate that a good number of our clients will have some work to do here!
 - Union representatives will need an employer's permission to enter the workplace
 - Employers will be able to communicate with employees during collective bargaining
 - Minimum requirements establishing a fair and reasonable dismissal process will be set out in the Act and employers will have a much clearer process to follow. This is great news for our employer clients, who can be fearful of dismissal processes being scrutinised for minor defects.

Minimising shareholder employee ACC levies

Changes were made last year enabling shareholder employees to be classified under their individual occupation rather than the business activity of their employer company. This change can make quite a difference to the levies you pay. For example, the levy rate for an office manager is much lower than that of a factory supervisor.

You need to review your cover structure and premiums, to ensure your cover is appropriate and levies are minimised.

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