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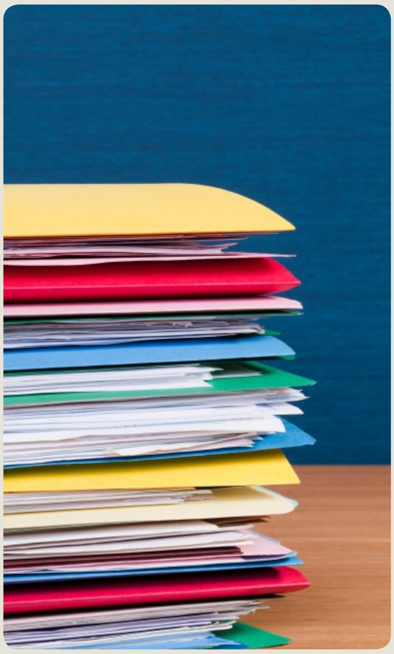

TAX UPDATE

Since the end of February, new businesses will be able to register as an employer at the same time they incorporate their company through the New Zealand Companies Office website.

Registering as an employer separately often meant that most of the information already provided had to be duplicated.

Under the current system, the business can choose to register for GST and income tax when incorporating on the Companies Office website.

YEAR END STRATEGIES

THE 2013/2014 TAX GUIDE FOR YOU AND YOUR BUSINESS

BDSHughes Chartered Accountants

Year end tax planning 2014

One thing is certain. When it comes to planning for taxation the changes are not always for the better, or any easier to understand.

Steps taken by the Government to simplify taxation in one area invariably leads to complications in another.

Combine this with business owner expectations for next year, which suggest increased sales and profitability, and we are all in for an interesting and challenging year. Like all challenges, they are best managed in pieces. Now is the time review the last twelve months, set new goals and begin preparing for the next financial year.

Timing is crucial: ensuring the timing of a transaction or investment is right can minimise your tax obligations. Correct timing can also affect the cash flow impact of your tax payments.

Sending us your accounting and personal records early means we can discuss planning opportunities and help you manage cash flow by giving you early warning of any tax payments due.

Keep your records

One way to prepare for 2014 is to ensure that your business is keeping proper records. It is important to keep relevant records so that the business can prove that all tax deductions are legitimate. All records must be in English and kept for at least seven years.

Some examples of the types of records that must be kept are:

- bank statements
- all income received
- wage records for any employees
- interest and dividend payments
- a list of business assets and liabilities
- all tax invoices and receipts for purchases
- motor vehicle log books

It is also essential to have proper records so that in the event of an Inland Revenue investigation all claims can be justified with minimum time and effort.

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Tax Bill gives greater clarity

Various changes to bring greater clarity to tax rules have been proposed under The Taxation (Annual Rates, Employee Allowances and Remedial Matters) Bill.

The proposed changes are aimed at making it easier for businesses and individual taxpayers to understand and comply with the tax system.

The Bill was introduced into Parliament on 22 November 2013 and is aimed at fine-tuning the tax system and ensuring that it is well-targeted, responsive and efficient.

The measures proposed in the Bill are the result of consultation with businesses and other taxpayers.

The Bill has proposed changes to clarify the tax treatment of allowances and other reimbursement payments paid by employers to employees, and employer provided accommodation.

The Bill also contains measures to deal with issues arising from the current 'black hole' tax treatment of certain items of expenditure.

Another change brought on by the Bill is the clarification to GST rules, which will make it easier for both businesses and individuals to understand their obligations.

New rules for mixed-use assets

The Taxation (Livestock Valuation, Assets, Expenditure and Remedial Matters) Act 2013 that was enacted in July has brought about a number of changes for income tax and GST.

One of these changes has introduced new rules for mixed-use assets and the calculation of expenses for certain mixed-use assets such as holiday homes, boats and aircrafts.

A mixed-use asset is defined as one that is used for both business and private purposes and is also unused for at least 62 days during the income year. The new rules are now based on the amount of time an asset is used in business or private, now how often it is available for business use.

The first mixed-use asset to come under the new rules from the beginning of the 2013-14 income year are land and buildings including holiday homes.

A holiday home is defined as mixed-use if, during the tax year, the property is used both for private use and income-earning use and is also unoccupied for 62 days or more. The new rules do not apply if the property is a residential property used for a long-term rental.

Expenses from mixed-use holiday homes fall into one of the three categories:

1. Fully deductible

Owners can claim 100 per cent of any expense that relates solely to the income-earning use of the holiday home. For example, costs of repairing damage caused by tenants.

2. Not deductible

Owners cannot claim any expenses relating to the private use of a holiday home. For example, the costs of a boat stored in a locked garage that is unavailable to the non-associated people renting the holiday home.

3. Apportioned

If an expense relates to both income-earning use and private use it will need to apportioned using a formula.

There are some exemptions to the above rules. If the owner's income from the use of assets is less than $4000 a year, they can choose to treat the income as exempt.

This will mean that the rental income does not need to be included on their income tax return and no expenses can be claimed.

Addressing common GST risk areas

Inland Revenue's (IR) recently released Compliance Focus paper has outlined common risk areas in association with GST.

Associated party transactions

Special timing rules apply to supplies between associated parties; however IR has noticed that these rules are not always followed.

Businesses should consider GST grouping in the context of supplies between associated parties.

Non-routine transactions

Non-routine transactions are those that are not in the ordinary operations of the business, and are generally a one off; for example, insurance settlements and the sale of an asset.

The GST consequences of these types of transactions may not be correctly accounted for through normal processes and controls, and, therefore, may require special attention.

Time of supply

IR has identified the time of supply rules as a common error despite the relative simplicity of the general principles.

GST return preparation errors

IR receives many GST returns which contain errors resulting in an incorrect return. Common mistakes made are mistakes in arithmetic, transposed numbers, leaving fields blank and not including transactions in the correct return period.

These errors often arise due to returns not being reviewed before filing. IR strongly recommends the use of review procedures to eliminate this type of error.

2014 year end tax tips

Loss offsets

Loss offsets elections must be filed with Inland Revenue before 31 March. Once they are approved they are unable to be reversed.

Repairs and maintenance

The end of year is a good time to take a look at spending throughout the year in order to determine whether items are deductible, or need to be depreciated.

Legal expenditure

Businesses with $10,000 or less of business-related legal expenditure can claim a full deduction in the year the expenditure occurs, regardless of whether the expenditure is capital or revenue in nature.

Building depreciation

The applicable rate of tax depreciation on buildings with an economic life of 50 years of more is 0 per cent effective from the beginning of the 2011/12 year. Fit out of commercial buildings will continue to receive a deduction for depreciation. The tax implications as a result of this will affect the current year, so the impact of this will have to be considered to minimise any shortfall penalties or interests

Prepaid expenditure

Certain expenditure can be incurred in advance of the 2014-year end and, provided it is not capitalised on the balance sheet, may be claimed as a tax deduction in the 2014 financial statements. Some expenses can be prepaid regardless of the amount or period being prepaid.

Valuation of trading stock

Trading stock is required to be valued using a cost valuation method. Market selling value may be used only when it is lower than cost. There is also no provision for the write-off of obsolete stock. To reduce the value of these items they should be physically disposed of, or alternatively, valued at market selling value.

Bad debts

To claim a deduction for a bad debt in the year to 31 March, the debt must be bad and must actually be written off during the year. There must also be evidence to verify that a debt has been written off.

Home office expenses

Areas in the home used primarily for business, or as a storage area for the business, may be able to be claimed as part of the overall costs of running the house as a business expense. Floor area is the most common base used for calculating the portion claimable.

Holiday pay

Amounts payable to employees at balance date for holidays or bonuses are deductible in the year to 31 March 2014 if paid to the employee within 63 days of balance date.

Mixed use assets

The calculation of expenses has changed for certain mixed-use assets, such as holiday homes, boats and aircrafts. The rules are now based on the amount of time an asset is used in business or private, not how often it's available for business use.

Shortfall penalties regime

A shortfall penalty is applied as a percentage of a tax shortfall resulting from actions of a taxpayer.

The law has divided these actions into five categories, with each category having a specified penalty percentage of the tax shortfall:

Lack of reasonable care

The penalty for not taking reasonable care is 20 per cent.

The law requires taxpayers to take reasonable care in meeting their tax obligations. This means that taxpayers need to exercise the care that a reasonable person in the same circumstances would.

For example, a reasonable person would be expected to seek professional advice if they were uncertain of their obligations.

Unacceptable tax position

The penalty for an unacceptable tax position is 20 per cent. An unacceptable tax position is difficult to define; however, it is seen as one that fails to meet the standard of "being about as likely as not" to be correct.

Gross carelessness

The penalty for gross carelessness is 40 per cent. Gross carelessness refers to behaviour that demonstrates high levels of carelessness and disregard for the consequences.

Abusive tax position

The penalty for taking an abusive tax position is 100 per cent. An abusive tax position is one that is based on an unacceptable tax position and has tax avoidance as a dominant purpose.

Evasion

The penalty for evasion is 150 per cent. Tax evasion can involve a variety of situations; for example, using deducted or withheld tax for anything other than its lawful purpose

In some situations, the IRD may consider prosecution before imposing the shortfall penalty.

IRD current targets for 2014

With the year end fast approaching now is the time to get organised and ensure that you are compliant with tax laws and stay off Inland Revenue's tax hit list.

Inland Revenue (IR) has released its 2013-14 Compliance Focus document which discusses IR's compliance priorities and risk focuses over the next 12 months.

The goal of Compliance Focus is to give greater clarity of the tax rules to both small and large enterprises. It aims to deliver information on IR's key areas of focus, and also to encourage voluntary compliance.

It sets out several key specific compliance risks that are facing small to medium sized enterprises and multinational enterprises, as well as reviewing IR's approach and processes to identifying these risks.

The document highlights the areas where non-compliance is most likely to occur. These include transfer pricing, international financing arrangement and GST.

Compliance Focus discusses the new ways in which IR is working towards analysing and identifying key compliance risks. These include:

- continued targeted audit focus on higher risk areas or significant taxpayers
- continued investment in tax avoidance/evasion investigation and prosecution
- increased information gathering
- increased information sharing and collaboration with other governments and revenue authorities
- increased involvement in the OECD's work on base erosion profit shifting

Compliance Focus is a useful tool to assist taxpayers in adopting a strategic approach to managing their tax risk by understanding where Inland Revenue will be focusing their resources over the next year.

Small to medium enterprises

The compliance focus for this group identifies common mistakes by SME's and also provides guidance on how to avoid these mistakes.

Some of the areas identified are GST errors, employer monthly schedules, accurate record keeping, accounting for contractors versus employees, non-resident contractors tax, child support deductions, use of industry benchmarks,

KiwiSaver contributions and income tax for the self-employed.

Employing new staff and establishing the trial period

Many employers can understand the benefits of a statutory 90 day trial period; however, many are confused on how exactly a trial period should work.

It is frustrating for any employer to hire a new employee only to find that their skills and experience are not sufficient to complete the job.

A trial period allows employers to notify the employee of their dismissal without the risk of facing a personal grievance over their dismissal.

Much debate from both employers and employees surrounds the 90 day trial period. It is beneficial to understand the legal implications of 90 day trial periods as it can save the time and effort from dealing with personal grievance claims.

All employers can rely on trial periods to dismiss new staff; however, there is a clear criterion that is strictly applied.

There have been many cases where employees have successfully claimed that a trial period was invalid.

These tips will help employers in setting out trial periods for new employees:

- The employee must be notified of their dismissal within the 90 day period.
- Only employ new staff on a 90 day trial period. Staff members who have previously worked for the business cannot be dismissed under a trial period, even though the role they are performing may be new.
- The trial period must be explained in writing and comply with legal requirements. It should state the length of the trial period (of no more than 90 days), during which the employer may dismiss the employee.

IRD targets investors

The Inland Revenue Department (IRD) will be given more funds to allow them to chase property investors, as well as establishing new rules for tackling international tax avoidance and evasion.

The IRD will have an extra $6.65 million a year to assist them in targeting property investment tax compliance. This increased funding is expected to generate an additional $45 million a year in tax.

Since 2010, the IRD have increased their focus on tax on property investment, in particular where land is acquired for the purpose of reselling it.

The IRD is also planning a further crack-down on foreign investors who artificially load up their New Zealand investments with debt in order to reduce their tax obligations.

In response to this issue, the Government is extending the rules to apply to where more than one foreign investor controls a company, and they are deemed to be acting together.