NEWSLETTER

Issue 3
Aug – Oct 2019

INSIDE THIS EDITION

Saving time and cost with tax

Various tax concessions exist that can save significant time and money, but they are often overlooked. You may want to save this article as a handy reminder to take advantage of these options whenever possible.

Business-related legal fees are tax deductible irrespective of whether they are capital in nature, provided the total amount for the year is $10,000 or less. The concession is not just for companies – trusts and individuals can also take advantage of it. Because the concession allows capital expenditure to be claimed, it can be applied to legal fees to purchase or sell assets. The Government has accepted a recommendation by the Tax Working Group to increase and expand it to other categories of professional fees and some feasibility expenses, providing a tax incentive for businesses to invest and expand, so watch this space.

For indirect taxes, the preparation of GST returns can be time consuming. When most businesses initially register for GST they ‘default’ to having a two-monthly filing frequency. However, for smaller businesses with annual sales below $500,000, taxpayers have the option to choose the six-monthly filing option instead.

For taxpayers making payments of interest, for example a company paying interest to a shareholder, or to a related entity, Resident Withholding Tax (RWT) needs to be accounted for and paid to IRD. However, there is no withholding requirement where total interest payments for the year are less than $5,000. At the other end of the scale, RWT exemption certificates are available for taxpayers with gross income of more than $2m.

The Fringe Benefit Tax (FBT) regime can be complex to navigate, however there is a useful de minimis threshold for 'unclassified benefits' provided to employees, such as gift vouchers, flowers and chocolates. FBT is not payable when the value of such benefits in a quarter is below $300 per employee, and the total value of unclassified benefits provided to all employees does not exceed $22,500 in the past year. For example, if 10 employees are each given $200 vouchers at Christmas, no FBT would be due providing no other benefits in the quarter were provided and the $22,500 annual threshold is met.

Finally, provisional tax payments for income tax can cause a headache for many small businesses, however the rules were simplified from the 2018 tax year. Now, where Residual Income Tax (RIT) for a year is between $2,500 and $60,000, provisional tax payments can be paid based on the standard uplift method, with any RIT not due until terminal tax date. This removes the requirement to estimate tax payments in advance, reduces interest costs and provides cash flow benefits.

Further simplification to the provisional tax regime is expected following the Government's recommendation that Inland Revenue should consider increasing the provisional tax threshold from $2,500 to at least $5,000. This would be a welcome change for taxpayers who fall into the provisional tax regime due to a one-off transaction.

And as a final bonus to using an accountant, there is a specific provision that allows a deduction for expenditure relating to determining your tax liability. The provision also overrides the capital limitation, so in most cases, fees charged by your accountant should be tax deductible.

Working remotely

In recent years, we have seen many businesses shift away from traditional office spaces and make the move to an open plan work environment.

Whilst open plan offices have been credited with boosting collaboration, breaking down hierarchies and encouraging conversation, new research suggests that working remotely can be a great way to increase productivity and boost employee morale.

The benefits of working remotely are in abundance for employees, such as avoiding the daily commute, enjoying a less stressful environment, and eliminating the unavoidable distractions of the office. However, the benefits for employers are often overlooked, with research suggesting that both the employee and employer can benefit through the creation of happier and more productive workers.

Technological developments providing the ability for employees to work remotely means that employers seeking new hires are granted access to a wider pool of applicants, meaning companies can hire the best of the best as they are no longer bound by geographical restrictions. Once those employees are in the door, the ability to work flexibly may also mean they stick around longer.

A study conducted by Stanford professor, Nick Bloom, found that employees who were able to work remotely were happier and less likely to leave their job than those who went into the office on a regular basis. Moreover, companies are likely to see financial benefits from implementing the freedom to work from home. By allowing employees to work from a home a couple of days a week, paired with a hot-desking policy for those in the office, the amount of office space required can be reduced, providing a corresponding reduction in rent and operating expenses.

Those opposed to the idea of working remotely are often deterred by what they perceive as a loss of control, direct oversight and the ability to witness productivity first-hand. Often, managers are guilty of equating employee presence with employee productivity. However, we all know there are plenty of distractions and ways to be unproductive in the office!

Like any company policy, the success of remote working will hinge on the guidelines set by management, continuous monitoring, and an ongoing commitment from employees to deliver what is expected of them. Remote working works best when people are accessible, communicate effectively, stay connected, and show that remote working positively impacts their work.

While remote working is unlikely to work for everyone, those who can manage it successfully are likely to reap the rewards.

Residential bright line

The Income Tax Act 2007 has long contained provisions to tax the sale of property (or other assets) acquired with the intention of disposal. However, 'intention' is a subjective concept and has been difficult for Inland Revenue to police. Hence, the brightline test, (section CB 6A) was introduced as a means to tax profits made on property purchased and sold within a short space of time. It has been in effect for a few years and it is now worth revisiting how it works.

The brightline test applies to land for which a person first acquired an interest in, on or after 1 October 2015. Typically, a person acquires an interest in land when a Sale and Purchase Agreement (S&P) is executed. This is important because if this occurred before 1 October 2015, the brightline test does not apply. When the brightline test was first introduced it applied if the period between the change of title to the purchaser and the date they subsequently entered into a S&P to sell, was less than 2 years. If the change in title was not registered, it is measured from the date the person first acquires an interest in the land (e.g. the date of the S&P).

When the current coalition government took office, the 2 year period was extended to 5 years. The extended 5 year period applies if the owner first acquired an interest in the land on or after 29 March 2018. Again, this is important because the shorter period of 2 years applies if a person acquired their interest in their land between 1 October 2015 and 28 March 2018.

The provision captures a broad array of residential land, including land with a consent to erect a dwelling, and bare land zoned for residential purposes. However, the provision does not apply to the 'main home', farmland, and property used predominantly as business premises. Properties acquired by way of inheritance are exempt, while roll-over relief applies to transfers under a relationship property settlement.

In most cases, people will apply the 'main home' exemption. To do so the person must have lived in it for most of the period of ownership. If the house is in a trust, the main home exemption is basically only available if a beneficiary and the trust's principal settlor lived in it. The main home exclusion can only be used twice in the two-year period prior to a disposal and cannot be used if a person has a regular pattern of buying and selling residential land.

Because the section has been drafted narrowly, it can apply unfairly. For example, if an investment property owned by an individual for 20 years is transferred to their family trust on 30 March 2018. For brightline purposes, 30 March 2018 becomes the acquisition date to the trust and a sale within 5 years will be taxable, even though 'the family' has owned it for over 20 years.

The brightline provisions are straightforward at first glance, but the devil is in the detail and deciphering the exemptions and timing requirements can be complex.

Finicky Bothersome Tiresome (FBT)

Fringe Benefit Tax (FBT) on privately used vehicles is neither new nor rare. However, errors in FBT calculations are common due to the murky and complicated nature of the rules and principles that apply.

Generally, FBT is payable when a business-owned vehicle is available for private use by an employee. The availability component of this definition is often misinterpreted; as FBT is payable when a vehicle is simply available to the employee, whether or not the vehicle is actually used privately.

By definition, if a vehicle is used for home to work travel, this counts as private use. However, that same travel from home to work is ignored if the vehicle qualifies as a "work-related vehicle".

This leads to our next common error - the application of the work-related vehicle definition. To qualify, the vehicle can't be designed principally to carry passengers, the name of the employer's business needs to be identified permanently and obviously on the vehicle's exterior, and finally, it needs to be a condition of employment that the employee stores the vehicle at home.

A common error is to treat a sign written sedan as a work-related vehicle – in factory form, sedans will not qualify for the exemption as they are principally designed to carry passengers.

When it comes to calculating the amount of FBT payable, the formula seems simple enough: multiply the proportion of days that the vehicle was available for private use during the quarter by the relevant vehicle value and a specific percentage. However, each of these elements can be misunderstood.

There are two methods available to determine a vehicle's value - either the cost price method, or the tax book value (TBV) method. The TBV method is the original cost price less its total accumulated depreciation at the start of the FBT period. A minimum value of $8,333 applies when using the TBV method.

Once a method has been chosen for a particular vehicle, the same method must be used for five years. Typically, the lowest value is achieved by using the cost price method from acquisition, with a change to the TBV method after five years. Cue our next common error: when changing to the TBV method, the $8,333 minimum amount is not an automatic option; it can only be used if the vehicle's TBV is less than $8,333. As a general rule, FBT is calculated based on GST inclusive vehicle values. GST exclusive values can be used, but the percentage needs to be adjusted accordingly.

FBT can be frustrating because it takes considerable time to calculate for what can seem like a small amount of tax. But it is worthwhile reviewing both the availability on which FBT is being calculated and the calculation itself. There may be savings to be had or errors to be identified, both of which can add up over time.

Snippets

New provisional taxpayers beware

Changes to the provisional tax regime, effective from the 2018 tax year, have generally been well received by taxpayers.

Prior to the change, Inland Revenue charged interest from each provisional tax date if a taxpayer's actual liability exceeded their 'uplifted' amount from prior year(s). This effectively meant taxpayers were required to predict their full year results as early as five months into the year. Now, providing payments are made under the standard uplift method, no interest is payable - providing any excess tax is paid by the third provisional tax date where tax payable is over $60k, or by terminal tax date where Residual Income Tax (RIT) payable is less than $60k.

However, there is a caveat for "new provisional taxpayers". IRD have released "Questions we've been asked" 19/04 for taxpayers in their first year of business. If the first year's tax liability exceeds $60,000, then the 'Use of Money Interest' (UOMI) concession is not available, and will apply to from the first provisional tax date, as per the old rules.

For example, where a large business is restructuring and diverges part of its business into a new company, the new company cannot rely on having a nil standard uplift liability, so if RIT exceeds $60,000 interest will be charged on any tax shortfall from each provisional tax date. New taxpayers should pay heed of this rule to avoid unexpected interest charges in their first year.

US tax rules

You may think New Zealand's tax rules are difficult to follow. The following unusual, yet permitted deductions in the US may change your mind.

A man in the US was prescribed regular swimming to treat his arthritis, and so had a swimming pool installed on his property. The associated expenses were subsequently approved by the IRS as tax deductible medical expenses! A similar US provision allowed a tax deduction for the cost of a clarinet and lessons, on the basis of an orthodontist's recommendation that playing the instrument would help correct a child's overbite.

An American TV personality once claimed the cost of formal dresses in her tax return. Although initially declined by the IRS, they were permitted as a legitimate business expense once she explained the dresses could only be worn on TV, and not for other personal use, because they were so tight she couldn't sit down!

But don't think that means everything is deductible. The cost of lettuce and tomato were denied as a medical expense for a diabetic on a restricted diet, as were the cost of bath oils for a taxpayer suffering from dry skin.

If you have any questions about the newsletter items, please contact us, we are here to help.