GARY CHAPMAN + ASSOCIATES LTD

NEWSLETTER

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Managing Working Capital

Irrespective of the stage of a business's life cycle, managing working capital is extremely important. During the growth phase, many businesses have failed due to growing too rapidly, and not having the corresponding cashflow to keep up with the expanding needs of the business. Meanwhile, mature businesses need to maintain sufficient working capital to ensure funds exist to meet liabilities as they fall due and to take advantages of business opportunities as and when they arise.

There are two fundamental questions an organisation should ask itself when managing working capital. The first is how much working capital is required and the second is how should it be funded?

A good indication of the working capital requirements of a business can be determined by the 'cash conversion cycle'. This is the length of time from the purchase of inventory or materials to the receipt of cash from customer sales. The length of this cycle can be influenced through the management of debtors and creditors.

Other financial measures that can be used to monitor working capital requirements include debtor days, debtor turnover, inventory days, inventory turnover, creditor days and working capital days. Monitoring these types of ratios over time can help identify problems before they manifest themselves in other more damaging ways, thereby enabling pre-emptive action to be taken.

Tangible 'best practices' that can be adopted to manage accounts receivable, i.e. cash inflows, include establishing a credit policy, making invoicing clear to facilitate payment, invoicing earlier, reducing payment terms, following up on overdue accounts, offering early settlement discounts and stopping credit to debtors that don't pay. Such practices need to be balanced against their potentially negative impact, such as customers going elsewhere because of unfavourable credit terms.

Conversely, managing cash outflows is also important by taking advantage of early payment discounts, prioritising suppliers, only making payments when they are due, ensuring invoices are checked for accuracy before payment, negotiating extended credit terms or putting procurement practices in place that are price driven, not relationship driven. However, care needs to be taken to ensure continuity of supply of materials and inventory.

Finally, inventory management is an important aspect of working capital. Techniques can be utilised in order to determine the optimal level of inventory a business should hold, and the ideal re-order point. A common model that is used is the 'Economic Order Quantity' model which determines the optimal amount of inventory a company should order by balancing ordering costs and carrying costs. Other considerations also include calculating the optimal re-order point so as not to run out of stock, and the consideration of holding 'safety stock' to avoid shortages.

Whether your business is starting up or well established, managing working capital is integral to success.

Home Is Where The Heart Is

If an individual is a New Zealand (NZ) tax resident they will be taxed on their worldwide income. Conversely, if a person is non-resident they will only be taxed on their NZ sourced income. This makes it important for a person to confirm their tax residency when they leave the country as it determines the extent of their continuing NZ tax liability.

A person is a NZ tax resident if they are either in NZ for more than 183 days in a 12 month period or if they have a 'permanent place of abode' in NZ. A person will be non-resident once they are absent from NZ for more than 325 days in a 12 month period and they do not have a permanent place of abode in NZ.

The concept of a permanent place of abode is not defined under the legislation. But the courts have considered the issue on a number of occasions. One recent case has arguably shifted 'the line'.

The Taxation Review Authority recently considered whether a taxpayer was a NZ tax resident over the four year period to 31 March 2007. The taxpayer had worked for the NZ Army for 25 years. After he retired in 2003 he left NZ to work in Papua New Guinea on a 12 month contract providing personal security.

The taxpayer gave evidence that when he left NZ in 2003 he had no intention of returning to live here. After the contract finished in Papua New Guinea, he spent approximately four months living in Queensland, before he began working in Iraq. In Iraq he also provided security services, completing a number of contracts up until April 2012, when he moved back to Australia.

Despite such a lengthy absence, the individual was found to be a NZ resident (and liable for tax on his worldwide income) because he was deemed to have a permanent place of abode here. The following factors were relevant to the decision:

- The taxpayer separated from his wife in 1994 and they had four children together. The taxpayer maintained close family and financial ties to his ex-wife and his children, and he provided financial assistance to them.

- Although absent from NZ for the majority of the time, between July 2004 and March 2007 (covering the period in dispute), he visited NZ every five to six months, with an average time in NZ of 42 days per year.

- The taxpayer owned rental properties in NZ with his ex-wife (personally and then through a company) that would have been available to him if he served the required notice under the Residential Tenancies Act 1986. Those properties were in the same locality as his ex-wife and children.

- The taxpayer's ex-wife had a debit card to access his US based bank account, to pay property and family related expenses.

Looking at the overall circumstances, the TRA found that the taxpayer continued to have a strong and enduring relationship with NZ, deeming him to be a NZ resident during the four years in dispute. The taxpayer was also deemed to have taken an "unacceptable tax position", which is subject to a shortfall penalty based on 20% of the tax shortfall.

The IRD has also recently issued an Interpretation Statement (IS 14/01) that came into effect on 1 April 2014, that sets out its view on how to determine whether a person is a NZ tax resident. The effect of the TRA decision has been taken into account in preparing the Interpretation Statement, namely the permanent place of abode test requires that a dwelling is available that can be used by the person in NZ. This does not necessarily mean ownership or control over a dwelling. If a person is able to use a property as a place to live on an enduring basis, then it can still be their permanent place of abode irrespective of whether the property is rented to someone else while the person is residing overseas.

Whether someone has a permanent place of abode is not easily determined. It takes judgement to weigh the particular facts and independent professional advice should be obtained.

Livestock Herd Scheme 2014

The IRD have recently announced this year's livestock Herd Scheme Values and we think this is a great opportunity to update you on the latest movements The Herd Scheme Values are the National Average Market Values as determined by a process involving a review of the livestock market as at 30 April.

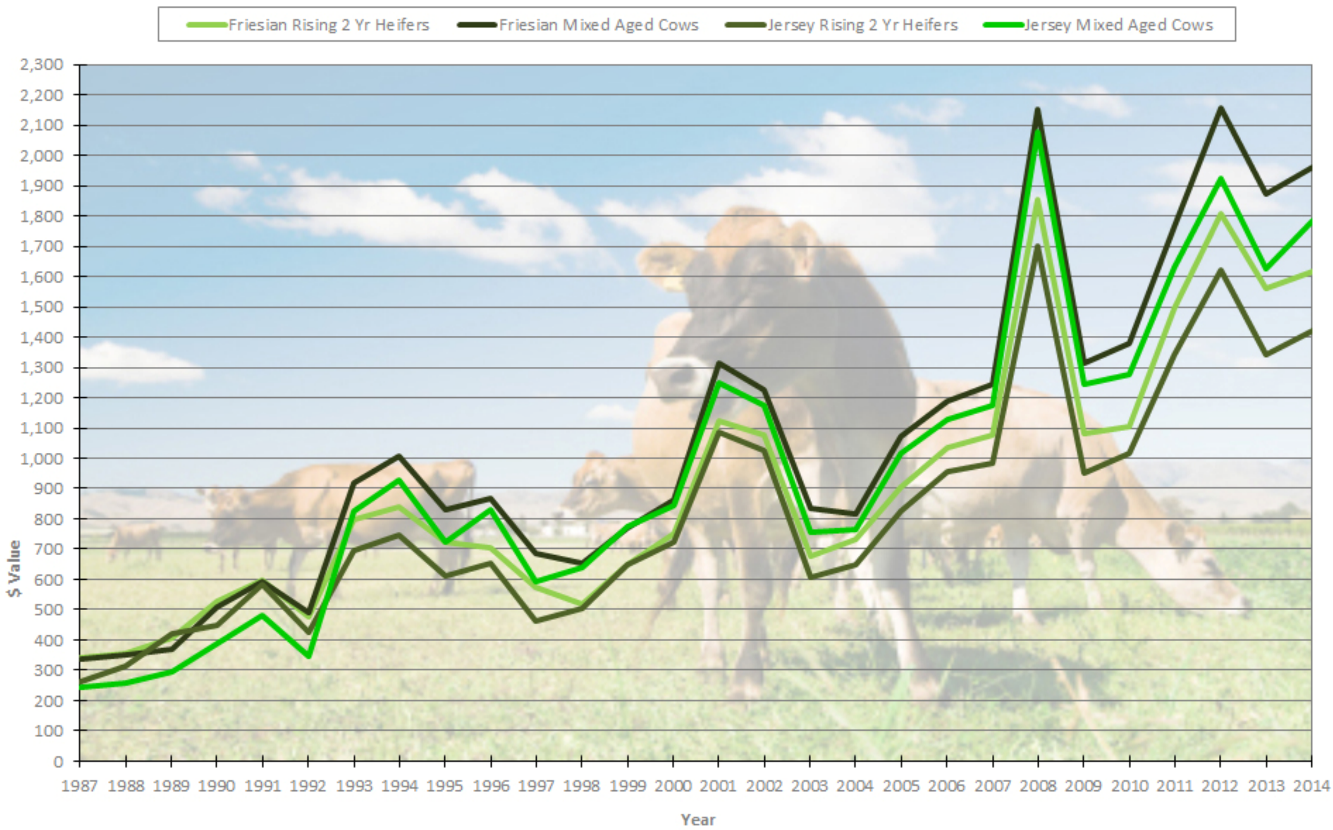
Dairy Cattle

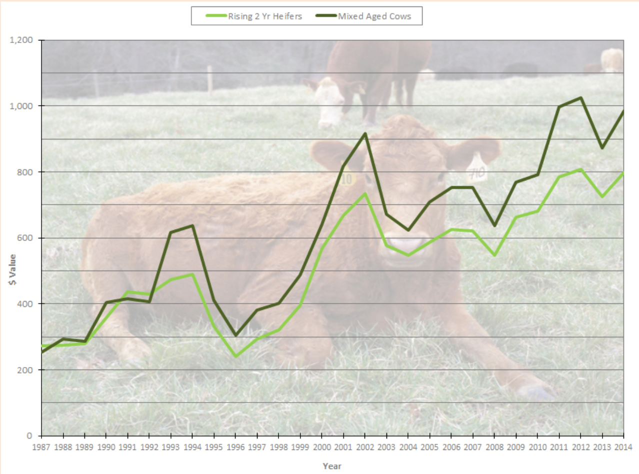
Following the drop in values after the widespread 2012/2013 drought we have seen an increase in values once again in the 2014 National Average Market Values (Herd Scheme Values). Mixed age Friesian cows have increased by 4.8% to $1,963 and mixed age Jersey cows by 9.5% to $1,782.

Following last year's significant drop in rising one year heifers we have seen a modest increase this year - with Friesian heifers increasing by 6.1% to $946.

While we have seen some dairy herds being sold for in excess of $2,000 per head, the herd values are an average throughout the country. Given that some parts of the country were once again hit by summer droughts the average is perhaps a bit lower than some commentators were expecting. If new herds have been purchased at values in excess of $2,000 per head there may be an opportunity to move these animals to the herd scheme with minimal tax impact.

The values for dairy cattle over this and the previous three years have shown a fundamental shift in the historic value of animals. The average of the last four years for a mixed age Friesian cow is $1,939 compared to the previous four year average of $1,521.





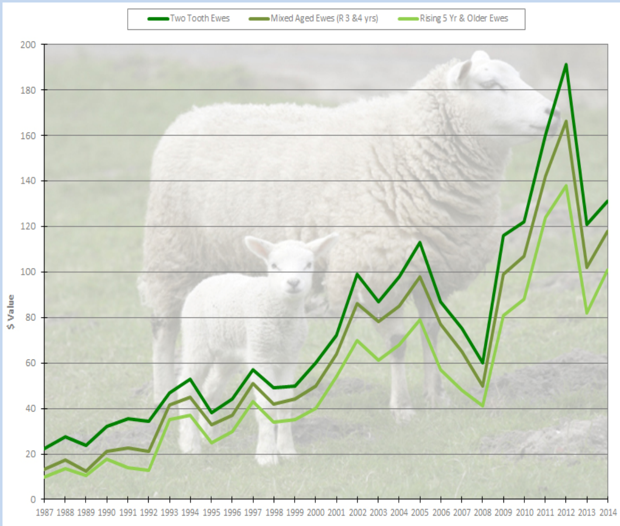
Beef Cattle

Following last year's drop in value we have seen an increase in values again this year - almost back to where they were in 2012. The value for a mixed age beef cow has increased from $872 per head to $986 (13% increase) with rising one year heifers increasing from $456 to $506 (11% increase) per head.

Demand for cattle following the widespread 2012/2013 drought has no doubt played a big part in these increases as farmers restock.

Sheep

As with other categories of livestock, we have seen good increases in sheep values as demand increases following the selling off of capital livestock during the 2012/2013 drought. Two tooth ewes have increased by 8.3% to $131 per head and mixed age ewes by 15.7% to $118 per head**.**



General Summary

Careful consideration needs to be given to your livestock election choices. Whether you elect to value increases using herd scheme values will depend on a number of factors - such as:

- where we are in the cycle of livestock values (e.g. at the bottom, or at the top)
- if the increase is a permanent or a temporary one
- your longer term intentions

As the decision is clearly one that should be made on a case-by-case basis, we will naturally discuss your valuation options with you on review of your 2014 financial statements and taxation returns.

Important Information About IRD Cheque Payments

We want you to know about an important change that will affect customers who make payments to the IRD by cheque. From 1 October 2014, you will need to ensure the IRD receives your cheque payment on or before the due date to avoid penalties and interest.

This means you will no longer be able to post cheques on the due date. You can however, make payments online up to and including the due date. It is recommended if you pay online, you use the "pay tax" function provided by most New Zealand banks. To make an online payment or find out more about making payments, go to www.ird.govt.nz and search "make a payment".

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