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NEWSLETTER

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Risk and Reward

Targeting the cash economy

Inland Revenue's crackdown on 'cashies' continues with their focus on undeclared cash in the construction and hospitality sectors. Last year, the Auckland region saw the most activity. Inland Revenue are now widening their reach. They've been trying to change attitudes among tradies and subcontracting businesses and their efforts seem to be getting results.

Inland Revenue acknowledge people trying to cheat on tax are in the minority but stress that they're a very expensive minority. The so-called 'hidden economy' is a cost to all New Zealand taxpayers, who carry more than their fair share because of it. There's another hidden cost too, as business owners who are meeting their tax obligations find it hard to compete with operators who can undercut on quotes because they don't pay tax. What's this have to do with you, you may ask. Because we're sure you're up to date with your tax obligations. In which case: sweet.

However, if you are in the situation of having under-reported – or unreported – income, now is a great time to straighten it all out.

We want to help you make sure your returns are accurate and timely and, as far as possible, help you avoid penalties and use of money interest on any tax owing.

If you think you might have gotten yourself into a mess with your tax, declaring it early and taking action to correct it goes a long way toward setting you apart from deliberate tax evaders.

You may have made a mistake or filed an incorrect tax return, left out some income from your return or incorrectly claimed expenses. We can help you make a voluntary disclosure which may reduce shortfall penalties by up to 100% and protect you from prosecution.

No More Residual Levies

From April, employers, earners, and motor vehicle owners no longer have to pay residual ACC levies. However, it won't mean reductions across the board.

The residual levy rate calculation was based on old injury rates which have become out-dated, going back 10 years or more. The residual levies themselves were a kind of catch up to make sure there were enough funds set aside to pay for ongoing claims predating 1999.

Now, all businesses will have their levies calculated on the most recent data around injuries and the likelihood of injury in their particular industries. Hence, while most will pay less, some will pay more. The removal of residual levies alone would have seen decreases in their ACC contributions for around 53 per cent of Kiwi businesses, while 47 per cent would be paying more.

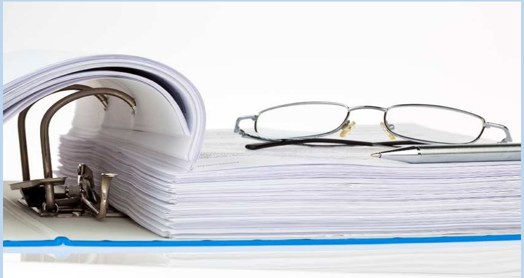
Levy reductions

The Government has agreed to the following changes to levies in 2016/17:

- 11% reduction to the average work levy taking it to 80 cents per $100 of liable earnings
- 4% reduction to earners' levy, taking it to $1.21 per $100 of liable earnings

33% reduction to combined average motor vehicle levies (the petrol levy and annual licence levy), from an average of $194.25 currently, to $130.26 per vehicle

Winding Up a Company



Recently, there has been an increased level of sophistication on the part of Inland Revenue (IRD) when reviewing company windups. Important points to bear in mind when winding up a company are outlined below.

Before applying to the Companies Office for removal from the companies register, a company should have discharged its liabilities to all creditors and distributed its surplus assets to its shareholders. The distribution of the company's surplus assets should be recorded by way of the directors' resolution. The amounts distributed to shareholders on liquidation are taxed depending on the nature of a distribution, as follows:

1. Available subscribed capital (ASC) - represents a company's paid up share capital and can be distributed tax free to shareholders on liquidation.
2. Capital gain amounts - are generally able to be distributed tax-free on liquidation of a company.
3. Remaining funds - to the extent that the distribution exceeds ASC and capital gain amounts, the balance will comprise a taxable dividend. This is typically a company's retained earnings.

In order for capital gains to be distributed tax-free, the process to windup the company must have commenced. Ideally, commencement of a liquidation is evidenced by a shareholders' resolution signalling the intention to commence winding up the company. The IRD accept that in some circumstances, a less formal step may be sufficient to commence the liquidation, provided the step is overt and carried out with the aim of achieving removal from the register.

We have seen an increasing number of cases where IRD has specifically requested documentation to evidence when the liquidation process was commenced. Therefore it is important to ensure the commencement resolution is drafted and dated correctly, or alternatively, a less formal course of action (if applicable) is supplemented by supporting documentation.

The Income Tax Act also prescribes a specific formula that is to be used to calculate the capital gain amount. This will not necessarily equate to the capital gains recorded on the company's balance sheet. Through its review process IRD are asking for a copy of taxpayers' capital gain calculations.

During the removal process approval must be obtained from IRD to remove a company from the register. The request to IRD should be made in writing after the liquidation process has commenced and once all tax compliance obligations have been met, e.g. final GST and income tax returns have been filed.

If the final distribution is subject to resident withholding tax, this will also need to be filed and paid before IRD approval is given. The IRD have a list of information that must be provided as part of this request, which is available on their website.

If approval is obtained, IRD will issue a letter stating they have no objections to the company being removed from the register. However, this approval provides no defence if a subsequent review, as described above, identifies mistakes when the various elements of the distribution were calculated.

Care must be taken. If IRD take the view that a capital gain was distributed prior to 'commencement', the costs could be significant.

R&D Tax credits

Does your business conduct research or development which is making a tax loss? Let us know, as you may be eligible to cash out your R&D tax losses for the 2015/16 tax year. We'll need to check your eligibility and register your business in the Investment Management System (IMS).

If you have any questions about the newsletter items, please contact us, we're here to help and look forward to your feedback.

Tax Talk

In April, the Government announced proposals to simplify business tax, with legislation to be passed in the coming months. The earliest of the changes would take effect from April 2017, with more coming online in 2018. At the moment, this would change the tax landscape to look something like this:

From 1 April 2017

Use of money interest 	Hundreds of thousands of taxpayers will be better off following the government's proposed revamp of business tax, as they will be removed from Inland Revenue's use of money interest regime, says Tax Management NZ chief executive Chris Cunniffe. Taxpayers using the standard uplift method (paying 105% of last year's tax bill) will no longer be charged interest if they underpay at their first and second provisional tax dates, provided they pay the income tax they owe at their last provisional tax date. Businesses and individuals who have residual income tax below $60,000 will also not be subjected to interest. It is expected that 67,000 taxpayers will benefit from this.
Penalties	Incremental late payment penalties will be removed from new debt for goods and services tax, income tax and working for families tax credits.
Credit reporting of tax debt	Inland Revenue can disclose significant tax debts to credit reporting agencies, so that other businesses considering extending credit can make more informed commercial decisions.
Information sharing	Inland Revenue can share information with the Registrar of Companies to help enforce company law requirements. This will help weed out non-compliant companies continuing to trade with an unfair commercial advantage over compliant businesses.
Withholding tax and schedular payments	Contractors will be able to elect their own withholding tax rate. Contractors working for labour-hire firms can be covered by withholding tax. Contractors and their payers can forge voluntary withholding agreements so that contractors can have tax withheld on a payday basis, reducing the impact of provisional tax.

From 1 April 2018

A new way to calculate and pay provisional tax 	The accounting income method (AIM), which will be available to taxpayers with turnover of $5 million or less, will allow those who have IRD-approved accounting software to pay income tax on a two-monthly basis. Up to 110,000 taxpayers will be eligible. Companies can pay tax as agents for shareholder-employees in respect of their shareholder-employee salary. This will reduce the impact of provisional tax for shareholder-employees. Taxpayers who are forced to use the estimate method due to volatility or seasonality may find tax pooling a useful option to manage income tax payments, as they will be subjected to IRD interest. Tax pooling would also provide businesses with cashflow constraints greater flexibility around when and how they pay their provisional tax payments.

But what will it mean for me?

The outcome of the consultation phase on tax simplification may still change how or whether some aspects are implemented but it seems certain that the broad outline of the changes will go through.

Best case scenario for small businesses: this should reduce complexity and make it easier to pay tax. You'll pay tax more frequently based on your business' actual income. You may end up paying less in tax, penalties, and interest. However paying tax more frequently may require you to keep a closer eye on cashflow to keep money coming in to pay the bills.

Worst case scenario for small businesses: you may end up paying more tax if you don't stay aware of your tax obligations and ensure the accuracy of the data input into your business software. We can assist you with regular monitoring and checking your systems are accurate and fit for purpose.

Setting the record straight

Inland Revenue have signalled they will be looking at businesses' record keeping systems. Key targets will be that all jobs and all income are being recorded and that GST is being handled properly. Recent prosecutions indicate that PAYE records are another hot topic, along with the corresponding employment records. If sketchy records are a quick way to set off the IRD alarm bells, this could be a great time to do a sense check on your records and systems.

As a business owner you're required by law to keep certain records. Poor record keeping lets you down just in terms of the penalties that apply for record keeping failures (up to $12,000). Inadequate systems also make it harder for you to keep track of what you owe, how much you have already paid, to whom and what for and who owes what to you. You lose track of things, miss key deadlines and your costs increase in proportion to how much of a nightmare it is to straighten it out.

With the advances in online systems of recent years, many businesses have overhauled their systems and are in good shape to pull out regular management reports that detail their position clearly. However, there may still be areas where things fall through the cracks.

This applies particularly in industries such as construction where large amounts stay on the table as retentions until the job is completed and it is difficult to keep track potentially across several tax years.

At the other end of the scale, the high volume and high speed cash transactions of the hospitality sector can also punch holes in the records.

If you are still making do with the basic systems you started out with, it is possible that your business has outgrown them and they now constitute a business risk. We can help you to look at this and do something about it, if necessary.

Mileage Rate Changes

Inland Revenue announced in May that the Commissioner had reduced the mileage rate from 74c to 72c/km for the 2016 tax year (1 April 2015 to 31 March 2016 for standard balance dates). If you rely on the standard mileage rate when reimbursing your team for travel, make sure your payroll system is updated to reflect the reduced rate.