

# Tacks **FAX**



**DON'T LET THE IRD NAIL YOU**

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## **Qualifying companies and trusts**

You will be aware dividends received from a qualifying company by a trust must be passed on to beneficiaries. The client can choose which ones will get the distributions subject to the streaming rules.

Where trustees have elected on behalf of minor beneficiaries, it is easy to overlook re-electing when the first beneficiary comes of age. You may need to diary this date to protect your client.

It can be useful to have a trust owning shares in an LAQC if it has other profits to set off against LAQC losses. However, once the LAQC becomes profitable, you would want to cancel qualifying status if trustees do not wish to make distributions but prefer to accumulate wealth in the trust.

## **New client from overseas**

If you get a new client from overseas, you need to be on your guard for the following:

### **1. Transitional Resident**

New residents, who have either never lived here or have not done so in the last 10 years may qualify for tax relief on certain income derived overseas for a period of 48 months. However, transitional residents do not qualify for tax credits for families. Check out the rules for making elections. An application for family tax credits is an automatic election not to be a transitional resident.

### **2. Foreign trust**

A new client, at the first interview, is unlikely to mention if they formed a trust overseas. However, if you want to avoid the possible high tax rates associated with foreign trusts, which includes tax on distributions of past taxed profits, you must elect to become a complying trust within a year, so ask and make a note of the answer.

### **3. Interest being paid overseas**

Again, you are unlikely to be told about a rental property owned overseas, when you first meet a new client. If the client applies early for Approved Issuer Levy, he/she can pay 2% tax instead of 10% NRWT on interest paid overseas. Often the mortgage is being paid out of the rental income so a question like "Do you pay any interest to an overseas bank" may produce a NO answer. The client forgets about the deduction. IRD will not allow back dating of AIL so the question needs to be asked as soon as possible.

If this occurs, your client (not the trust) will derive assessable income when the trust exercises the option. This could be many years after the transfer. The value of the benefit to the employee is the difference between the market value of the shares on the day the trust acquires them and the amount paid by the trust for the shares. If the trust sells the rights to a non associated person, the employee is assessable on the gain on sale of the rights. If there is a time restriction on exercising the right to purchase check section CE 3 of ITA 2007

## **Family Scheme Income and losses**

If a client is trading as a company and the company has made a loss, the company needs to pay a salary to shareholders to claim In Work Tax Credit. If the client doesn't have a salary then he/she is not in work. Inland Revenue has expressed concern where the salary payment is nominal. The Department is considering this might be tax avoidance.

IRD is partly supported by a case Y1 (2007) but this case involved a family trust and management fees, which is different from merely paying a nominal salary. However it was about contriving to get the maximum family support. LAQC doesn't help you because LAQC losses are added back to increase income S MB 1 (4) of ITA 2007.

## **Clearing 33% ICA credits**

When declaring a dividend, directors must not only comply with the solvency test but also have the money to pay the dividend. In some cases, more than one dividend may be needed because of **lack of funds**.

The quieter summer period could be a good time to sort out which companies should declare dividends and plan when these ought to occur. Some ICA accounts might need to be checked. If the economy is deteriorating, it may be better to get dividends paid sooner than later. Dividends using the 33% ICA credits are limited by the amount of the ICA, which means you can make payments from 2009 or 2010 profits and attach 33% ICA credits to them, if there are enough available. If you are declaring dividends using 30% ICA credits, you have to pay the extra 3% as withholding tax by the 20<sup>th</sup> of the month following payment of the dividend.

<b>Share options sold to trust</b>	<b>Charitable Organisations</b>
<p>A client may receive share options as part of her salary package. She derives income only in the year she exercises her option to buy, even if there's no time limit for doing so.</p> <p>The client could transfer these options to her family trust.</p>	<p>If a charity is not carrying on a business then it is not liable for FBT.</p> <p>However, if the employee of such a charity has the use of the employer's credit cards or similar, and the value of the benefit from this facility in a tax year is more than 5% of the employee's salary or wages for the tax year, then the benefit becomes liable to FBT.</p>

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