



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

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## **Attribution rule and payment of dividends**

Some clients, (who derive 80% of their income...) choose to attribute instead of paying out an extra director's salary. When this happens a credit is put into the ICA to prevent the income being taxed twice.

Now the income tax on companies is 30%, the ICA credit is inadequate. The system is to be changed. You will put in the ICA credit based on the 30% tax rate (42.86%). However, when you pay the dividend, you will cancel the ICA credit and treat the dividend as not taxable as though it were coming from a Qualifying Company.

This is not yet law but it is expected to be passed into law very soon and to be back dated.

## **Penalty for early termination of loan**

At first sight the penalty charged by banks, known also as break fees, would appear to be not tax deductible. Expenses incurred in borrowing money are tax deductible. Expenses incurred in ending a loan are not.

The financial arrangement rules override the capital/expenditure distinction and break fees are part of a financial arrangement.

If you terminate a loan, you must make a base price adjustment. The break fee is part of this and so should become immediately deductible.

However if the break fee arises from merely varying an existing loan, non cash basis persons would have to spread the break fee over the term of the new loan.

## **More on the DTA with Australia**

### **Pensions**

When the new DTA with Australia is ratified, a client who is entitled to a tax exempt Australian pension, and who lives here, will not have to pay tax on that pension in NZ, to the extent the pension would have been exempt in Australia. Normally these pensions would still be taxable under our law.

### **Royalties**

Tax on royalties will now be 5%. Payments for leasing assets are no longer included as royalties. The reduction will be great news for companies who receive royalties as the overseas tax is not a credit to the imputation account.

## **Six months deadline for crediting beneficiaries to go**

The law is to be changed to do away with the 6 months time limit for crediting or paying distributions from family trusts to beneficiaries, starting with the 2010 year. Great? May be. Some trust deeds will have been written giving trustees six months from balance date to allocate income. You'll need to check each one and keep an eye on those having this time limit.

## **More on accruing accounting fees**

The issue is whether the client has incurred the cost. Could it be sued for? If you have a company being wound up and you get a special engagement letter signed, listing all the work involved from preparing a special resolution for winding up to getting the company removed from the Companies Office register, arguably, if the fee is fixed, the client has committed and hence incurred the cost. If the charge is to be on a time basis, the "sued for" argument is weaker. Some commentators say if the work has been started, there is a commitment. Others are more cautious. So, the more work that has been done before balance date, the stronger the case for accruing the final accounting fee.

## **Cash basis holder extended but...**

From 2010 the cash basis will no longer be limited to a natural person. Trusts and companies will be subject to the same rules as individuals. Goodbye to accruals for many clients.

Some clients have been able to accrue interest in their companies but pay tax on a cash basis as individuals. This practice is now blocked. If the client's company is accruing an interest expense then the client receiving the interest can lose cash basis status.

## **Fines and Penalties**

IRD has issued a draft interpretation statement. It wants all fines and penalties to be non deductible even if they are directly related to deriving income. While parking fines are not mentioned specifically, it seems they are to be included. As the interpretation statement is only a draft, there could be change.

IRD argues breaking the law is against public policy so all fines are not tax deductible. The IRD is supported by a recent TRA case involving overloading a logging truck.

## **Client going to live in Australia**

Clients going to live in Australia should check out their tax situation and set up their affairs to take advantage of any tax benefits available to them, before they leave New Zealand. For example, if a client has a trust in NZ, it may pay to distribute all the income of the trust to beneficiaries for a while after the client leaves New Zealand.

We understand Australia has a "temporary resident" exemption. For New Zealanders moving to Australia the "temporary resident" exemption can provide much greater benefits than Australians moving to NZ can expect to receive under our "transitional resident" rules. However, there may be some strings attached, like not taking out Australian citizenship and not having a de facto relationship with an Australian citizen. Get Australian tax advice early.