

Tacks **FAX**



DON'T LET THE IRD NAIL YOU

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Giving tax advice

A practitioner finished a letter to a client with a warning the advice was based on tax law at the time. The law could change. Subsequently, a major court case did change the law. The practitioner referred back to his advice and was relieved to see he had added this extra note.

We think all tax advice needs to be given with a warning about the risk of the law or its interpretation changing. Clients could also be warned the IRD could challenge a tax decision and the cost of arguing could be prohibitive. Finally, what about untrained staff offering their advice to clients? We suggest you use your engagement letter to cover this. You could put in a clause like "we only accept tax advice given by a principal of the firm in writing..."

Switching from accruals to cash basis

If you want to switch a client company or trust to a cash basis holder, you will need to make an adjustment to your financial arrangements.

The cash basis adjustment formula requires a catch up calculation to the current income year, with the difference between the old method and the new method being returned as income or expenditure in the current income year.

Time to sort out trusts

Reminder: Some trust deeds will still require distributions to be made within 6 months of balance date. Now is a good time to identify these and have the deeds amended to take into account the extension of the beneficiary distribution deadline.

Applying for an instalment arrangement

You can now save time by sending an email request to pay off tax in instalments. Go to <http://www.ird.govt.nz/taxagents/working-ird/instalment>. You will find instructions plus a template to complete.

Reimbursements can include depreciation

S. CW 17 of the IT Act 2007 permits employers to reimburse employees for expenditure, based on a reasonable estimate. The income to the employee is not taxed and the expenditure is tax deductible. You are now allowed to include depreciation. S. CW 17 (4) says "In this section, expenditure includes an amount of depreciation loss." This section seems to have been slipped into the law in the last tax Act. The change is effective from 1 April 2008, but does not apply in relation to a tax position taken by a person in circumstances stated in S CW 17.

Unpaid dividends

Unpaid dividends should be credited to each shareholder. Do not open an unpaid dividends account and tip all the dividends into it. After a dividend is declared by resolution, the amounts need to have been subsequently "dealt with in the interests of the shareholders" to be considered paid. The solvency test has to be re-applied at the time of ultimate payment.

Current uncertainty about future income tax rates makes the decision about which companies should declare dividends using 33% ICA credits now, that much more difficult. You could write to the borderline clients, give them the facts and let them choose.

Clients are using wrong PIRs

It is worth checking clients are using the correct PIR? Sometimes a financial advisor is using the default rate instead of the low rate, costing the client a lot of money. Other clients are using the low rate instead of the high rate.

A new resident can use the 19.5% rate when investing in a PIE, regardless of income. This is because you take the lower of the last two years income and the non resident will have one of those years, at least, with no income at all. From 1 April 2010, this PIR could be as low as 12.5%.

GST ratio can save cashflow

Now is the time to consider if the GST ratio could assist some clients. The deadline for registering to use it in 2011 is 31 March 2010.

Freedom from UOMI is not the only benefit the ratio has to offer. Clients who would most benefit are those whose profitability (net profit to sales) is rising; the very successful clients. These are usually the ones who are experiencing the worst cash flow as they struggle to finance increasing working capital requirements.

The GST ratio can help. Example: A client would have had a ratio of 5% for 2009. If something like 10% is expected for 2010, the client could have been paying income tax at the rate of 5% of sales for the 2010 year and part way into 2011. The 5% rate will continue until the 2010 return is sent in. As the ratio only kicks in when reset by IRD after they receive the 2010 return, a good part of the 2011 tax is deferred to 7 April 2012. So long as the profitability ratio continues its upward trend, the GST ratio is truly helpful.

Foreign withholding tax and FDR

When you calculate FIF income using FDR, which is compulsory for companies, remember, if there have been any dividends, you are entitled to claim withholding tax up to the limit of tax incurred in New Zealand on that income.