Aug/Sep 11

Tax Time

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Residential Care Subsidy and Abolition of Gift Duty

There was some surprise that no new legislation was proposed as a result of the abolition of gift duty. Some saw the removal of gift duty as an opportunity for taxpayers to defeat creditors and gain access to benefits by depriving themselves from ownership of assets by transferring them to a trust.

On face value, residential care subsidies seemed to be one area where the removal of gift duty could have a significant impact. However, the existing rules more than adequately cover this situation and prevent an undue advantage being obtained.

At present, gifts made within five years of applying for a residential care subsidy in excess of $6,000 per application per annum, will be clawed back. ‘Application’ includes a spouse. Thus, a husband and wife can gift no more than $6,000 in total per annum if they wish to avoid claw back. If a couple together gift $54,000 per year, their excess gift over five years would amount to $240,000.

Beyond the five year period, it is possible to gift up to $27,000 per application per year, but anything in excess of $27,000 could also be clawed back.

There is an ability to pay someone for providing a high level of care prior to going into a rest-home. However, any such amount will be included in the total gifting allowance (of $6,000 per annum for five years) and, therefore, may affect the claw back calculation.

The rules also claw back any deprivation of property and income. Deprivation is where there is a deliberate act or omission that results in deprivation of property or income. Deprivation of income includes waiving a right to income, not demanding payment, or investing in non or low income producing assets.

Where assets are transferred to a trust, but in reality the applicant and/or the spouse has a power of appointment or control over the trust assets, claw back may also arise if an asset has been transferred to a trust and not been fully gifted at the rates allowed.

How it affects you

Before engaging in a gifting programme, transferring assets to a trust or other person, you will need to consider the wider implications of such, including matters like loss of control, application of the above rules, family succession objectives, income needs, etc. It is always wise to seek advice before undertaking any gifting.

- From WHK Sharp-As Tax

Treatment of Subvention Payment

The Inland Revenue Department has made a change to its practice of requiring an actual physical payment (transfer of funds and not just book entries) for subvention payment purposes. Previously, for a subvention payment to be complete they required an actual payment. They have now reconsidered their view and in the absence of any statutory definition in the context of a subvention payment, “payment” will be given its ordinary meaning.

In the context of subvention payment agreements, “payment” will be satisfied when the obligation has been discharged. There are a number of ways an obligation may be discharged, including a cash payment or equivalent or by certain accounting entries. An obligation will generally be discharged where the payee can no longer sue the payer for the payment.

Are You Renting Your House Out for the RWC?

With the Rugby World Cup (RWC) fast approaching and the proliferation of homes being offered as accommodation, it is timely to review the income tax treatment of short-term rental activities for a taxpayer.

From an income tax perspective, matters are relatively straight-forward, in that all income derived from the short-term rental accommodation activity should be included in the person's income tax return for the corresponding income year.

Where things become more complicated however, is in relation to deductibility of expenses.

As a general premise, a person is allowed a deduction for an amount of expenditure or loss to the extent to which the expenditure or loss is incurred in deriving their assessable income. However, a person is denied a deduction to the extent to which the expenditure is private in nature.

With respect to a property which is being rented out on a short-term basis for the RWC, there will be an element of deductible expenditure and a much larger element of private expenditure (if you are renting out your own home or a holiday home).

Thus, if you are renting your home for a four week period over the RWC, then you will be entitled to a deduction of 4/52 of the annual expenditure incurred in relation to the property, for example, insurance, rates, interest costs on a mortgage, etc. Other costs that can be directly attributable to the four week stay will also be deductible. This may include electricity, rubbish removal, advertising of the property, cleaning, etc.

The difference between the income received and the expenditure incurred will be taxable income. For a wage and salary earner, this will mean that they will be required to file an income tax return for the 2012 income tax year. The person will also have a terminal tax liability in relation to the net income derived, which would be due on 7 February 2013, or 7 April 2013 if the taxpayer uses a tax agent and has an extension of time.

How it affects you

The Inland Revenue Department has advised that they are reviewing advertisements for accommodation and are contacting those persons directly to remind them of their income tax obligations in relation to renting their property. If you are unsure of what your tax obligations are, we suggest that you contact your usual advisor.

- From WHK Sharp-As Tax

GST on Second-hand Goods

GST may be claimed on second-hand goods by a GST registered person if those goods are bought from a non-registered vendor, provided:

- The buyer actually pays for the second-hand goods before claiming GST on it;
- The buyer keeps sufficient records such as an ordinary invoice because the unregistered vendor will not be able to issue a GST invoice; and
- The goods comply with the definition of second-hand goods in the GST Act.

The GST definition of second-hand goods specifically excludes livestock but land purchased from an unregistered vendor may be second-hand goods; therefore a registered purchaser of such land may be able to claim GST on the purchase price. However, an input tax credit will be available only on that part of land that is related to a taxable activity. For example, if a farmer purchases a piece of land that has a dwelling on it for farming activity then GST cannot be claimed on the dwelling and curtilage.

IRD policy requires the goods be both previously used and previously owned by someone else i.e. prior ownership on its own does not make the goods second-hand. There have been instances where taxpayers incorrectly claim GST under the second-hand goods provisions. The following are some examples:

- When goods are purchased from an unregistered associated party, GST is not claimable if the associated party did not pay GST when buying those goods;
- When GST is claimed on second-hand goods before payment is made because the taxpayer is on invoice basis. Regardless of the taxpayer's GST accounting basis, second-hand goods claims are limited to the amount actually paid during the taxable period; and
- When goods are purchased from a GST registered supplier. Inland Revenue will not allow a claim unless the taxpayer holds a valid tax invoice at the time of filing the GST return. In cases where the supplier claims to be unregistered for GST, it is best to obtain a written confirmation from them that they are not registered for GST.

Deadline for transition to a look-through Company

Legislation passed in December 2010 created a new tax entity known as the look-through company (LTC). The LTC can be used for income years starting on or after 1 April 2011.

If you had an existing QC or LAQC prior to 1 April 2011 and you want to transition to an LTC, you have until six months from the start of the relevant transitional income year to do so.

For example, if your LAQC has a standard balance date of 31 March, you have until 30 September 2011 to make an election. To do this, you need to complete a *Look-through company election (IR 862)* form.

Alternatively, you could become a sole trader (if the LAQC/QC has only one shareholder) or a partnership.

Please contact us to discuss your decision based on your specific needs.

Fringe Benefit or Entertainment?

Employers often enquire about the treatment of expenses made on account of employees – whether they are subject to fringe benefit tax (FBT) or considered to be entertainment expense. Generally, when employers consume or enjoy the expenditure at their discretion, and it is not in the course of their employment duties, then the expenditure is subject to FBT. Examples of such expenses are:

- Subsidised gym memberships;
- Goods sold at a discounted price; and
- Memberships to golf club.

Any expenditure that is subject to FBT is fully deductible by employers. Entertainment expenditure, on the other hand, is an expense that is not enjoyed at the employee's discretion, e.g. staff Christmas parties or entertaining customers. These expenses are only 50% deductible for tax purposes. The following checklist sets out the rules regarding the tax treatment of entertainment expenses.

ENTERTAINMENT EXPENSES CHECKLIST

	50% Claimable	100% Claimable	FBT Payable
Staff Christmas party costs	✓		
Gifts for New Zealand Clients	✓		
Business lunches in New Zealand	✓		
Morning tea 'shout' on employers' premises (for all employees)		✓	
Transport costs provided to employees to attend staff Christmas party		✓	✓
Entertainment consumed overseas		✓	
Gifts to staff		✓	✓
Light meals provided to employees at lunchtime meetings		✓	
Friday night drinks for employees	✓		
Sales staff's meal costs while out of town		✓	
Corporate box costs or season passes	✓		
Subscriptions to sporting clubs e.g. golf clubs		✓	✓

The above list does not cover every situation. Please contact us if you have any queries on any other types of entertainment.

Working for Families Tax Credits Income Changes

The definition of family income for Working for Families Tax Credits has been amended. From 1 April 2011 people receiving Working for Families Tax Credits will no longer be able to use investment losses, such as from rental properties, to reduce their family income. The definition also includes the following income types:

- Attributable trustee income (including income of a company controlled by the trust) if you're a settlor of a trust;
- Attributable fringe benefits – when 50% voting is held by shareholder-employees or their associates;
- PIE income – excluding superannuation funds or a retirement savings scheme;
- Passive income of children – includes interest, dividends and rent. Amounts over $500 a year (per child) are included as family income;
- Income of non - resident spouse – worldwide income;
- Tax exempt salary or wages – under specific international agreements in New Zealand (eg, United Nations);
- Main income equalisation scheme deposits - made by you, your trust or a company controlled by you or your trust;
- Certain pensions and annuities – includes 50% of payments from life insurance policies or a superannuation fund (excluding NZ Super); and
- Other payments – received from any person or entity and used for the family's day-to-day living expenses. This is only included if the total amount exceeds $5,000 per family.

If you are receiving weekly or fortnightly Working for Families Tax Credits payments, you need to let the IRD know if they have any of the above types of income so they can pay the correct entitlement. If you are receiving Working for Families Tax Credits as a lump sum at the end of the year, then let the IRD know before the end of year assessment is completed (year ending 31 March 2012).

Refund of Excise Duty

Often, tax advisers have suggested that taxpayers should take advantage of the ability to obtain a refund of excise duty where vehicles or machinery that use petrol, compressed natural gas (CNG) or liquefied petroleum gas (LPG) are used outside of New Zealand's public roading network.

With the increase in fuel prices in the last few years, the refund available could be substantial.

At present, the rates of excise duty are 56 cents per litre for petrol, 12 cents per litre for LPG, and 3.65 cents per gigajoule for CNG.

For farmers, the obvious situations where this has relevance is in relation to farm bikes, chain saws, and brush cutters.

To claim a rebate of excise duty, a claim form must be completed, which is available from the New Zealand Transport Authority, who can also provide you with information as to the excise duty refund process.

In order to obtain a full refund of any excise duty paid, an applicant must file a claim within three months of the close of a calendar quarter. Thus, for the quarter ending 31 March 2011, the applicant has until 30 June 2011 to file its return. It is possible to claim rebates as far back as two years ago, however, a 10% reduction in the refund amount is applied for any refund not relating to the current filing period.

The refund of excise duty is subject to GST, and any rebates received should be included as outputs for the GST period in question. Any rebate received is also taxable income of the recipient and should be included in the appropriate income tax return.

In the case of farm bikes, where the bike is used both on and off road an apportionment in its use would be required to determine the extent to which an excise duty rebate is allowed.

How it affects you

For farmers in particular, the ability to obtain a refund of excise duty in relation to off road petrol costs provides an opportunity to offset the increasing costs associated with operating farm bikes, chain saws, brush cutters, and the likes.

The refund process is relatively straight-forward and, as such, the cost associated with obtaining a refund should be minimal. If you have any queries as to how to obtain a refund of excise duty or to determine whether you qualify, we suggest you contact us.

- From WHK Sharp-As Tax

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Quick Bits

- 17% of households pay 97% of net taxation.
- Suspicious emails purporting to be from the Inland Revenue Department advising refunds due have again been doing the rounds. These emails are fake and should be deleted. Do not click on the link nor fill in any personal information.