



Newsletter

Winter 2007

It is time to talk tax

TAX law is changing rapidly and is becoming complex. Some of these changes are likely to affect **you**. You need to know about them.

Residential rental property

IRD is revising the depreciation rules. It proposes having anything which is a part of the house depreciated at the same rate as the house. This will reduce some of the depreciation claims being made. Property investors can expect to pay more tax but the adjustments will probably not be too dramatic.

Portfolio Investment Entities (PIEs)

Savers, using managed funds, should know about these two varieties of investment available from 1 October 2007. Some investments, complying with rules laid down by the Government, will be called Portfolio Investment Entities (PIEs). This section tells you the difference between the two schemes available to you for direct investment. A third scheme, which we are not discussing, deals with superannuation schemes.

Portfolio tax rate entities

Portfolio Tax Rate Entities (PTRE), will have their income taxed at the individual investor's income tax rate. These funds will be attractive to those on low tax rates. They will pay only 19.5% on their share of the fund's profit. High income earners will pay 33% instead of 39%. Those who tell the fund their tax rate is 19.5% when it should have been 33%, must correct the error through their tax returns. Inland Revenue says these PIEs will become the main type of savings scheme.

Portfolio Listed Companies

Another scheme will be a Portfolio Listed Company. It will pay tax at 33% on income and allocate dividends to investors, which will **not** have to be included in their personal tax returns. However, if your income will be taxed at 19.5%, you will be permitted to declare the dividends. This will probably qualify you for a tax refund. Some of the dividends may be a mixture of capital and income, so a refund is not a certainty.

Income from both these schemes will not be included when calculating Working for Families tax credits, Student Loans and Child Support.

Student loans

IRD is accessing information from HM Customs to ensure certain students travelling overseas do not get interest free loans. The rules for charging interest to these students are still changing.

Tax credits

The Government is expected to reintroduce tax credits to encourage research and development. It was also planning to offer incentives for market development and skills training. However the Minister of Finance announced, in a recent speech, that these incentives are not going to proceed.

New Partnership Act

The Government is considering introducing a new Partnership Act. The old one will celebrate its 100th birthday next year! The Act will include provision for limited partnerships. These will be partnerships which have the protection of a limited liability company. The limited partners will not normally be involved in management. Losses for these partners will be limited to the amount of money actually lost by the partner. It has been suggested this will lead to the abolition of qualifying companies.

Change to tax payment dates

GST is now payable on the 28th of the month instead of the end of the month. If the 28th falls at a weekend or public holiday, including Anniversary Day, the GST can be paid and the return sent in, on the next working day.

From 1 April 2008, income tax dates will be aligned with GST dates. Provisional tax will become payable six times a year. To achieve this, income tax and GST period end dates will have to be aligned. Where they are not, the taxpayer will have to put in an extra GST return to achieve this or change their accounting year end by a month, subject to the Inland Revenue Department approval.

Setting your selling price

A CLIENT was out shopping for Christmas presents.

“My partner budgeted \$100 for each of our grandchildren,” he said, “We found a couple of presents which looked promising, and they were priced at only \$40 each. She rejected them because they were too cheap! I told her to buy them and then if she was concerned she could buy something more for the children.”

Christmas Day arrived and her son emailed her a photo of her

grandson playing with the \$40 Christmas present. He couldn't put it down. There is a business lesson in this for sellers.

The woman wanted to spend about \$100 on a gift. The price was of considerable importance. She felt to pay only \$40 would be cheap-skating.

Base your price on the amount you think the customer is willing to pay. Use cost price to cross check you are making a satisfactory profit. Selling price must cover the cost of making

or buying the article, or your time in supplying the service, and a fair share of overheads and hopefully a profit.

Satisfy your customer's **wants** and do not confuse this with **needs**. The shopper needed a present but wanted one costing about \$100. Customers buy to satisfy the want, not the need.

If you are in the business of providing services and your quality is outstanding, customers will pay more for you than for someone else. Price accordingly.

Assignment of income

TAKING the advice of his financial advisor, a client lent his wife a large sum to invest so she could derive the interest and the pair of them could save some tax. When we suggested this transaction was wrong, because it was an assignment of income, the financial advisor said we were being pedantic. Take tax advice from those who know tax.

If you lend money to another person for investment, so the interest can be taxed at a lower rate than it would be in your own hands, you are assigning your income. This is not permitted.

However, you are allowed to do the following:

1. If you have the larger income, always get it paid into a joint account. It then becomes family money. When you come to invest, the income belongs to both partners and can be split equally. Half a cake is better than no cake.
2. You can enter into a matrimonial settlement. You agree certain of your assets will, in future, belong to the two of you jointly. You now share the income. This could be useful if you own rental properties and you want the rent to be shared.
3. You can sell your investments to a family trust. Your spouse can be a beneficiary of the trust. Trustees, subject to considering the interests of all beneficiaries, may distribute some or all the income to your partner.
4. Form a company, in which the shares are allocated unevenly. This may achieve the result you are wanting. Your decision should not be tax motivated, for example: Matrimonial settlements create a fairer sharing of wealth. Family trusts protect your family assets from:

- Creditors
- The government claiming for your long-term care when you are old
- Children losing their inheritance as a result of a relationship going bad.

World's biggest éclair

THE biggest éclair in the world is made in Ohakune. The owner of the shop where the éclairs are made was in Germany and met a local who seemed to know New Zealand. The German asked where he was from.

“You wouldn't know the place, it is a tiny town called Ohakune.” said the shop owner.

“Oh yes I do, it makes the biggest éclairs in the world,” the German responded.

If you are in Ohakune, try one. In winter, the owner says, he sells about 500 a day. The éclairs are made using a very big old oven and plenty of steam.

The store has something unique. Can you find something different to make your business stand out?

How to pay less FBT

A REMINDER that you are permitted to switch the basis for calculating FBT on a car available for private use, from original cost to tax book value (TBV), once your company has owned it for five years. Our calculations tell us it would be worth making the change. Tax book value is the value shown in your annual accounts. Since we usually prepare them excluding GST, you will need to take the figure in the accounts and add on GST, being 1/8th of the amount shown. That becomes your tax book value. This figure must be at least \$8333. If it is lower, use \$8333 to calculate the fringe benefit.

Don't stint on bank fees

THE easiest way to process your bank account transactions is to have them all identified with codes. The most efficient way of incorporating these transactions into your annual accounts is to put them into our system electronically. The less analysis required by us, the better.

For example, you make a payment to your credit card company. This might involve several different types of expenditure and personal drawings. Why not make a separate payment for each category of expenditure? This is easy if you use electronic banking. By splitting up the payments for us, you eliminate the common error of the total being different from the sum of the parts. You also eliminate the need for us to get the analysis from you and hand adjust these payments; the cost of which is significantly more than the bank fees incurred in making multiple payments of one expense.



● IN BRIEF

Paid parental leave

Application for paid parental leave by a self-employed person must be made before the applicant returns to work or the parental leave ends.

Flu vaccination

Ever thought of offering your staff free flu vaccinations? A \$25 investment could save a week's sick pay, apart from being a way you can look after your staff. Did you know it was the 25-40 age group who were worst hit by the 1918 flu epidemic? One reason suggested is older people had been exposed to flu viruses over the years and had built up some resistance.

Do bad debts go with good business?

MOST bad debt is unnecessary. It arises from being too casual about giving credit.

Occasionally, clients have collection problems because they have too much of their business with one firm. If you are in this situation, plan to get out of it, even if it takes several years. If your customer's business fails, it may take yours with it.

You can minimise your bad debts by:

- Stating your terms of trade clearly and being tough with your follow-up of those who do not stick to them. Be on to them smartly once the deadline has passed. Most bad debts arise because businesses are too busy with their day-to-day work to get on with collecting their debts or don't like to insist on payment.
- Giving credit only when you have to. If you can collect payment on completion, why offer credit?
- Getting progress payments.
- Getting a deposit before you start.

The more materials in your product; the more essential it is to get a progress payment. If you don't get paid, you will still have to pay your supplier. Therefore, the deposit should be at least the cost of materials.

- Better still, get payment in full before you supply.
- If you have to give credit, ask for credit references and follow these through.
- Check credit history through a debt collection company or the *Mercantile Gazette*.
- When you have a problem, be persistent with your follow-up. Write notes of every call made and get a commitment every time. Confront the bad payer with the broken promises.
- If you get a promise to pay, try asking the customer to keep the payment while you get in your car to go around and collect it.
- If the sum is large, you could try getting two or three cheques making up the total. A smaller cheque might get honoured whereas a larger one might not.
- Cash, even if only for part of the total, is better than a cheque which you expect will bounce.
- People who give you bouncy cheques should be asked to get a bank cheque (one drawn on the bank's own account).

Debt collection can take a lot of time, which could be better used developing your business. Therefore, be ready to sack your troublesome customers, particularly if the business you get from them is small. You are probably losing money by having them. Recommend they deal with your least favourite competitor and tell them how to get there!

Keep your retailer fully stocked

PENELOPE manufactures knitted garments which she markets through retailers. They sell well.

“The trouble is,” she said, “when they sell my stuff they never re-order and yet they are always delighted with it.”

I asked Penelope why she didn't send them an order form every month with a message on it: “If you haven't got it you can't sell it; please check your stock level, fill in this form and fax it back to me.” She would probably need to ring the customers, explain what she was doing and get their agreement to complete her order form. She could then follow up when there was no response.

Penelope agreed to try it. We will wait to see the results. Do something different and you get a different (hopefully better) outcome.

How many retailers would make more sales if their re-ordering was better organised? And, how many suppliers need to become more proactive? Wait for the order to come in and it will never happen. If you don't fill the shop's shelves, someone else will.

Supermarkets have re-ordering down to a fine art. Could you copy or adapt their methods?

International reporting standards

A FEW years ago New Zealand agreed to adopt International Financial Reporting Standards for preparing financial statements, so accountants here will abide by similar rules to those being used by the major world economies.

The Financial Reporting Standards Board has just produced some proposed rules for preparing accounts for small and medium sized businesses. Some of the requirements will involve considerable extra work and therefore extra cost. To avoid this, clients may elect to have special purpose financial statements prepared, just for tax purposes.

If clients want accounts to show to their bank or for selling their business, we will be preparing them to comply with these standards. The change is expected to occur some time next year.

Chocolates and champagne

EVER heard of a chocolate lounge? It is a chocolate shop where you can sit down as you would with a coffee shop. You can have chocolate fondue, a choice of chocolate cocktails, truffles and so on. Tea and chocolates replace tea and cakes.

Can you apply some lateral thinking to your business and make it special or different?

Shall I lease or buy the car?

YOU have a choice when your business acquires a car: Lease, hire purchase, borrow or pay cash. Which should you choose?

Leasing

The company leasing you a vehicle (lessor) may be able to buy it at a much better price than you can.

The lessor takes risks including:

- Guessing the residual value.
- If maintenance is included it must estimate the cost.
- Fluctuations of interest rates.

You must pay for these risks.

You can lease the car in two ways:

- An operating lease where each payment is tax deductible.
- A finance lease, which is treated like hire purchase for tax purposes.

Hire purchase

The main difference between a finance lease and hire purchase is the big payment under hire purchase is made at the beginning of the contract, whereas for leases it is often at the end. For those very short of cash flow, leasing might be more attractive than hire purchase.

Borrowing

Bank rates are usually lower than hire purchase or lease. Borrowing from the bank is for those whose business is not short of cash flow.

Pay cash

Choose this option if you do not need to borrow and the benefits of leasing are not sufficient to make that the better choice.



TAX CALENDAR

June 7

3rd instalment 2007
Provisional Tax
(June balance date)

July 7

1st instalment 2008
Provisional Tax
(March balance date)

August 7

2nd instalment of 2008
Provisional Tax
(December balance date)

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