bakertilly
STAPLES RODWAY

31 March 2020 Tax Planning Checklist

With 31 March approaching, now is the ideal time to consider tax issues and, where available, planning opportunities. Key matters are outlined below.

☐ Accounting & Taxation Services Fee Accrual

Following the decision in TRA Case *Y17*, the accounting and taxation services fees accrual for the current year should be added back in the taxation calculation. This adjustment will reverse in the subsequent year's taxation calculation when the deduction is taken.

☐ Bad Debts

To claim a tax deduction, the debt must be:

- Bad; and
- Physically written off on or before balance date.

The above rules mean you must be able to support that the debt is bad (i.e. you have made reasonable efforts to collect the debt before writing it off).

☐ Companies - Shareholding Continuity & Commonality

The ability to carry forward tax losses is subject to shareholding continuity of 49%. The ability to offset losses against the net income of other group companies requires common shareholding of 66%. The ability to carry forward imputation credits is subject to shareholding continuity of 66%.

Note these tests must always be met and not just at year-end.

If you are anticipating shareholding changes and believe you will breach continuity, forfeited losses can be minimised by accelerating income recognition and minimising deductions where possible. Also, consider the payment of a dividend or making a taxable bonus issue to use imputation credits before they are forfeited.

☐ Controlled Foreign Companies (CFCs)

Except for most Australian shareholdings, ownership of foreign shares has the potential for New Zealand tax to be payable, primarily if the foreign company derives passive income (including, but not limited to, interest, some dividends and royalties). If you have an investment in a CFC, then please contact us for further advice.

☐ Cross Border Transactions

Any transaction with either a related party or that is part of a structured arrangement and results in a taxation mismatch is likely to be subject to new hybrid mismatch rules (known as the BEPS rules). These rules are designed to cancel out the taxation advantage of such transactions and may require a disclosure to Inland Revenue. Similarly, entities which have different tax characteristics between two countries are likely to be subject to these new rules.

These new rules are complex, so if you have cross border transactions of this type, please contact us for further advice.

☐ Employee Allowances

Broadly, employees are exempt from tax when they are reimbursed or provided with an allowance for work-related expenses.

For travel or relocations, employer provided accommodation or accommodation payments will generally be exempt where the employee is temporarily working away from home for a period of up to two years (or three years in the case of capital projects). Employee meal costs or meal allowances will generally be exempt where the employee is working away from home for a period of up to three months.

The subtleties in these rules present both opportunities and pitfalls to employers. Therefore, we recommend you contact us if you are considering providing accommodation or paying a meal allowance to your employees.

☐ Employee Remuneration

Employers have the choice of either treating all accrued employee remuneration (e.g. bonuses, holiday pay and long service leave) as not deductible in the current year or treating amounts of accrued employee remuneration paid in the 63 days following balance date as deductible in the current year.

We note accrued bonuses paid out within 63 days of balance date may not be tax deductible if there is no evidence a commitment was made to pay the bonus on or before balance date.

Redundancy payments must be paid by year-end for the employer to be able to claim a deduction. That is, the 63-day rule does not apply.

☐ Entertainment

A GST adjustment for non-deductible entertainment must be included as an output tax adjustment in the GST return that covers the earlier of the date the return of income is filed

or date the return of income is due. This expense must be added back for income tax purposes.

There is an opportunity available whereby it may not be necessary to make the GST output adjustment. Please contact us if you are interested in finding out more about this.

☐ Fixed Assets

Review the fixed asset register to ensure the assets exist and to identify assets that are no longer used in order to claim a deduction for the remaining adjusted tax value of the asset.

Assets can be written off if they are no longer used but have not been disposed of, provided:

- The asset is no longer used by you in your business or to produce income and;
- Neither you nor an associated person intends to use the asset in a business or in the future to derive gross income; and
- The cost of disposing of the asset would be more than any proceeds from disposing of the asset; and
- The asset is neither a building nor an asset being depreciated using the pooling method.
- Assets costing $500 or less qualify for an immediate write-off provided:
- They do not form part of some other asset; and

They are not purchased from the same supplier at the same time as another asset and the total is more than $500.

☐ Foreign Investment Funds (FIFs)

There are several available methods to calculate the tax position of interests held in FIFs (for instance, shares held in overseas companies, with the exception of some Australian shares). Where a FIF has been held, a change in calculation method may be desirable to improve your tax position. In some cases, it may be necessary to make an election before year-end to be able to use the best method.

If you have a substantial stake in a FIF then please contact us for further advice.

☐ Foreign Superannuation Schemes

Generally, lump sum distributions from Foreign Superannuation Schemes are included as taxable income using either the schedule or the formula methods. Typically, the longer a

taxpayer has been in New Zealand, the higher the amount of the lump sum distribution will be taxable income.

Payments of regular amounts from non-state foreign superannuation are usually subject to tax.

We recommend you contact us for further advice as individual circumstances do vary

□ Fringe Benefit Tax

The end of the year is a good time to review any fringe benefits that might be provided to employees that might not have been identified.

The fourth quarter Fringe Benefit Tax return is different to the other Fringe Benefit Tax returns during the year. An alternate rate calculation is either compulsory (for those who used the 43% alternate rate during the year) or is optional (for those who used the 49.25% single rate). If all employees to whom fringe benefits are provided are on the highest income tax bracket, and this option is available, it may be beneficial to continue using the 49.25% single rate.

A close company calculation option is available for vehicles acquired from 1 April 2017. This applies to close companies providing motor vehicles to a shareholder-employee that is available for private use. A close company can make this election for up to two shareholder-employees in the income year in which they purchase the motor vehicle or first start using the motor vehicle for business use. The effect is no FBT is payable, but income tax deductions and GST inputs related to private use are denied.

We can assist in the preparation of Fringe Benefit Tax returns, the filing of a close company calculation option election, or general Fringe Benefit Tax matters if required.

□ Goods and Services Tax

As part of your year end procedures, a reconciliation between the entity's GST return and the balance of the GST account in its financial statements should be undertaken. This reconciliation can provide a useful warning about any discrepancies and provide an opportunity to rectify any issues. Also, this reconciliation is generally requested by Inland Revenue as part of their audit procedures.

If there are unreconciled differences, we recommend a GST review be performed to identify possible system issues.

□ Imputation Credit Account (ICA)

Your company's imputation year is from 1 April 2019 to 31 March 2020. Please ensure the ICA is not in debit at 31 March 2020. A debit ICA will attract a penalty of 10%.

☐ Individual Taxes

After 1 April, Inland Revenue will be automatically issuing pre-populated income tax returns. Where the individual confirms or Inland Revenue is satisfied the information is correct, a refund or tax bill will be automatically calculated. Due to the risk of error, it would be useful to have any pre-populated income tax returns reviewed by us prior to confirmation.

☐ Inter-Company Charges

We recommend a review of inter-company charges be conducted to ensure documentation is in place to support any deductions and to minimise any potential tax risk.

☐ Mixed Use Assets

The tax treatment of real estate (mainly holiday homes), water craft (with a purchase price of more than $50,000) and aircraft (with a purchase price of more than $50,000) where the asset is used for both private use and income earning use and is unused for 62 days or more per year is subject to the mixed-use asset rules. Under the rules, certain losses will be quarantined, and a deduction may only be claimed when the asset derives positive net income.

If the gross income from the mixed-use asset is less than $4,000 per annum, or if you would otherwise have quarantined deductions, the ability exists to opt out from the mixed-use asset regime for that year. This means that income is not subject to tax, but also means that no deductions can be claimed. This concession does not apply to close companies.

Complex interest deductibility rules exist in instances where mixed use assets are held in companies, as well as additional quarantining rules.

If you own mixed use assets, we recommend contacting us to discuss your options.

☐ Payments to Non-Resident Contractors

If payments have been made to non-residents for services performed in New Zealand the non-resident withholding payment rules may apply. There are exemptions available in specific circumstances. Please contact us if you require further information.

☐ Payroll

All employers with PAYE and ESCT of $50,000 or more per annum need to file employer information returns electronically within two days of payday. Payments continue to need to be made every month or twice a month depending on the size of the employer.

☐ Prepaid Expenditure

Certain prepayments can be claimed as a tax deduction provided they are expensed for financial reporting purposes. Please contact us if you would like further details.

☐ Provisional Tax

The final instalment of 2020 provisional tax for 31 March balance date taxpayers is due for payment on 7 May 2020. Unlike the first and second instalments, if the standard uplift method has been used, use of money interest (**UOMI**) is charged on deemed underpayments of provisional tax with reference to actual residual income tax (**RIT**) only where actual RIT is greater than $60,000.

If actual RIT is less than $60,000 and the standard uplift method has been used, then no UOMI applies until the terminal tax due date (7 April 2021 in most cases).

UOMI will apply from the first instalment if you or any related entity has either used the estimate method for provisional tax or not paid provisional tax on time using the standard uplift method. UOMI can also apply from the first instalment in the first year of business. If this situation applies, you may wish to consider making use of a tax-pooling intermediary, such as Tax Management New Zealand.

Your advisor can help you prepare a draft tax calculation to help determine whether you should make a voluntary payment above the amount due under the standard uplift method. Additionally, they can discuss the advantages and disadvantages of using a tax-pooling intermediary.

☐ Provisions for Warranties & Other Expenses

These accounting provisions are generally non-deductible. However, in accordance with the Privy Council decision in *Mitsubishi Motors*, it is possible to obtain deductions for provisions in limited circumstances, if appropriate records are held.

☐ Research and Development Tax Credit

A research and development tax credit of 15% is available to taxpayers who engage in eligible research and development activities and incur eligible research and development expenditure. Under legislation currently before Parliament, it is proposed that from the 2020/21 year, this credit would be refundable in expanded circumstances. If you think your business may engage in research and development eligible for this tax credit, please contact your advisor. It would also pay to have systems in place to track expenditure in order to maximise the level of credit available.

☐ Residential Property "Bright-Line Test"

Where residential property is held for five years or less (two years or less if the property was acquired before 29 March 2018), it may be subject to the "bright-line test" with any profits on sale subject to income tax. There is an exemption for the family home in most circumstances.

If you are considering selling residential property held for five years or less, or considering transferring ownership as part of a restructure, we recommend seeking advice first as the rules are complex and the consequences can be significant.

☐ Residential Rental Property Loss Ring Fencing

From the 2019/20 year, losses on residential rental property held on capital account (that is, for long term income derivation) will only be able to be offset against income derived from residential rental properties, either from rental income or the application of the "bright-line test".

☐ RWT on Dividends

The RWT rate on dividends generally remains at 33%. This means any dividends with imputation credits attached at 28% will generally require a deduction of 5% RWT. This RWT is payable by the 20th of the month following the date of the dividend. However, no RWT is deductible when the recipient is a company at the election of the payer.

From 1 April 2020, additional information will need to be disclosed to Inland Revenue when paying a dividend. The list of information required is comprehensive and is available at https://www.ird.govt.nz/income-tax/withholding-taxes/resident-withholding-tax-rwt/payers/investment-income-reporting/reporting-requirements-from-1-april-2020/payers-of-dividends---reporting-requirements-from-1-april-2020

☐ Shareholder Salaries

In light of the *Penny and Hooper* decision, it is important to ensure that in closely held businesses commercially realistic salaries are paid to any shareholder-employees. Please contact us if you need further help in this area.

☐ Thin Capitalisation Regime

The regime will apply if a New Zealand company is owned or controlled by non-residents or where a New Zealand owned company owns foreign controlled companies. We recommend you confirm whether your company is subject to the regime and if so, whether its debt level exceeds the applicable safe harbour level. For foreign controlled companies, the safe harbour applies if interest bearing debt does not exceed 60% of the value of assets. The thin capitalisation calculation excludes "non-debt liabilities" from assets. It

may be possible to undertake financial restructuring prior to balance date to maximise interest deductions.

Due to the complexity of the new rules and the increased likelihood of interest deductions being denied, we recommend having your company’s thin capitalisation position reviewed.

□ Trading Stock

Various valuation options are available to you depending on annual turnover and the valuation method used for financial reporting purposes.

In general terms, trading stock, including work in progress, is valued at either cost using a cost valuation method or market selling value when this is lower than cost.

The cost valuation methods include cost, or where permitted, replacement price, or discounted selling price.

To claim a deduction for obsolete or slow-moving stock, it should be physically disposed of on or before 31 March 2020 or valued at market selling value if lower than cost.

□ Transfer Pricing

With the increase in transfer pricing audit activity, we suggest any dealings with offshore related parties be formally documented to support the arm’s length nature of the prices applied.

The onus of proof for transfer pricing matters has also shifted to the taxpayer and Inland Revenue has the power to investigate the last seven years in relation to transfer pricing instead of the usual four years, provided notice of a tax audit or investigation is given within the usual four years.

□ Trusts and Trust Distributions

For trusts on a tax agent’s list, with an extension of time for filing, the distribution date may be the earlier of the date on which the trust income tax return is filed or the date by which the trust tax return is due to be filed. Distributions of current year income by this date allow the income to be taxed in the hands of the beneficiary, rather than in the hands of the trustees.

If the Trust Deed contains a clause requiring the distributions to be made within 6 months of balance date, this can override the above.

More generally, the Trusts Act 2019 comes into force from 30 January 2021 and strengthens the rules around the administration of trusts.

□ Withholding Tax on Interest

If an interest expense on intercompany loans is booked via a journal entry then this triggers an obligation to pay resident withholding tax (RWT) or non-resident withholding tax (NRWT) to Inland Revenue by the 20th of the month following the date of the journal entry.

The above checklist is of a general nature only and does not take into account any specific needs or circumstances. We would be pleased to provide further information on any of the issues highlighted in the checklist.

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