Since publishing this article, the COVID-19 situation has evolved significantly. For up-to-date commentary, please visit bakertillysr.nz/news-hub/covid-19/

Cashflow on tap

Provisional tax relief in the wake of COVID-19 and drought

Managing cashflow becomes paramount in an uncertain environment. Right now, a few folks will be trying to keep as much money as possible in their business following droughts, floods and the early impact of the COVID-19 virus.

STORY
Clyden Manikkam
National Business Development Manager
Tax Management NZ

Tax pooling can be an effective tool in helping businesses conserve cash when they need to. It is an IRD-approved service that provides someone with more time to pay their provisional tax, without the risk of facing IRD interest and late payment penalties.

DISCOUNTED RATE FOR FORESTRY AND TOURISM INDUSTRY

Tax Management NZ is offering a highly concessionary rate of 3.95 percent for businesses in the forestry and tourism industries impacted by coronavirus who do not qualify to have IRD interest waived on tax payments. The offer applies for 2020 provisional tax, as well as terminal tax payments relating to the 2019 tax year.

Someone with a provisional tax obligation due on 7 May 2020 would have until mid-June next year to pay if they entered an arrangement with a commercial tax pooling provider such as Tax Management NZ.

Where tax pooling might be useful

For most businesses, provisional tax is generally calculated on an uplift of the preceding year's income tax liability.

However, when something like coronavirus, drought or flooding strikes, profitability can nosedive and cashflow can dry up. As such, paying based on this calculation may no longer be suitable. This is likely the case for those making a living in the forestry, tourism, meat and crayfish industries. The economic ramifications brought upon by the situation in China – one of their key markets – will significantly hurt projected earnings – as well as the regions which rely upon these industries.

Some will simply want to hold onto funds until their financial position improves, while others may need to use that money elsewhere. For instance, businesses impacted by flooding will have repairs and the cost of the clean-up at the forefront of their minds; farmers affected by drought may wish to purchase feed for their cows if the situation worsens.

Although the Government has now come to the table with a package that will assist businesses who qualify, many will still be hurting. Tax pooling can offer some respite from having to meet Inland Revenue's requirement to pay provisional tax during a tough and difficult time.

You only pay what you owe when using the service – not some amount calculated by reference to prior years which may well be in excess of your actual 2020 liability – and can pay once this amount is known.

There is some interest to pay when you settle with the tax pooling provider, but this is cheaper than the 8.35 percent IRD charges if you fail to pay on time or underpay and there is no exposure to late payment penalties.

clyden.manikkam@tmnz.co.nz

Clyden Manikkam is the National Business Development Manager of New Zealand's first and largest tax pooling provider, Tax Management NZ.

HOW TAX POOLING WORKS

Say you have a provisional tax payment of $15,000 due on 7 May 2020. With the uncertainty given recent events, you would rather not pay this right now if it can be avoided.

If you let a tax pooling provider know about your position, they can make a tax deposit of $15,000 into its IRD account on 7 May 2020 on your behalf. This deposit is date stamped as at the date that it is made.

The tax pooling provider will also tell IRD you are using tax pooling to pay your tax and IRD will enter a note in its system telling its debt collection team not to pursue the outstanding payment.

Once you file your tax return and know the liability for the year, you pay the tax pooling provider. This payment must be made no later than mid-June 2021. Your payment includes the core tax of $15,000, plus the provider's interest cost.

The interest cost to pay the $15,000 in mid-June 2021 is $978. That is a saving of $1,140 in interest and late payment penalties if you settled this with IRD at the same date – and ensures your compliance record is not negatively impacted.

If it turns out the actual liability for the year is less than the date-stamped deposit made on your behalf, don't worry. You only pay for the tax you require, and the tax pooling provider's interest will be recalculated to reflect this.

Upon receiving your payment, the tax pooling provider transfers the deposit it is holding on your behalf from its IRD account to your IRD account. IRD will treat it as a $15,000 payment made on 7 May 2020 by you and will wipe any interest and late payment penalties they may have put on your account.