31 MARCH 2020 YEAR END TAX TIPS AND REMINDERS

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The end of income tax year is fast approaching and will end on 31 March 2020. It's a timely reminder to spend a little time reviewing your financial records and reflect on the past year. It's also an opportunity to remind you of a few steps you may need to take to help minimise your tax bill.

The list is a summary only and isn't intended to be exhaustive or complete. However, I believe there's a reasonable chance that you'll find a couple of tips and strategies to add some extra savings to your tax bill.

Please don't hesitate to contact me if you'd like to discuss your specific needs and circumstances. Regards

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FIXED ASSETS REVIEW

Check your fixed asset register to make sure you're using correct depreciation rates and depreciating new assets for the full month of purchase, not just from the day of purchase.

Likewise, pooled assets can be depreciated for the entire year. Ensure assets you have sold or lost are properly disposed of on the fixed asset register, as this might result in a deduction.

Assets costing less than $500 (GST exclusive) can be written off immediately. This assumes that they aren't an upgrade part of a wider acquisition of the same asset from the same vendor, with the same tax depreciation rate.

You may claim depreciation for a full month for any part of a month that you own and use an asset.

Commercial fit-out [1]

The depreciation rate for buildings is 0%. To maximise taxable deductions identify, where possible, commercial fit-out expenses (so depreciation tax deductions can be claimed) from the building itself.

BAD DEBTS

Write off bad debts. If you don't think that a bill is going to be paid, then write these off before 31 March 2020.

You must be able to demonstrate that you have undertaken a process of determining that the debt is "bad". Individual trade debts should be reviewed. They must be actually written off in your receivables ("debtors") ledger before 31 March 2020 to be allowed.

A debt is generally classified as bad if a reasonable and prudent person would conclude that the debt is likely to be repaid. The length of time that the debt has been outstanding and what you've done to collect it will be key factors in determining if it's a bad debt.

A debtor doesn't have to be insolvent for the debt to be classified as a bad debt. You can still pursue them for the debt.

WAGES, HOLIDAY PAY, ANNUAL LEAVE

Employee remuneration not paid at 31 March 2020 (e.g. holiday pay, bonuses, long-service leave) but made within 63 days after 31 March 2020 may be claimed under certain circumstances.

[1] *Government recently announced it will reintroduce depreciation on commercial and industrial buildings from the 2020-2021 year.*

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Note: accrued bonuses paid out within 63 days of 31 March 2020 date may not be tax deductible if there's no evidence that a commitment was made to pay them. Redundancy payments must be paid by 31 March 2020 to be able to claim a deduction.

CLOSING STOCK

Review inventory: Unsold trading stock (excluding livestock) at 31 March 2020 must be valued, subject to meeting the relevant criteria, using **one** of the following methods: cost; its discounted selling price; replacement price, or market value if it's lower than cost. These methods must be applied consistently.

If your turnover is less than $1.3 million you may value your closing stock at its opening stock value. But only if you can reasonably estimate that your closing stock is valued less than $10,000.

MIXED USE ASSETS

The tax treatment of real estate (mainly holiday homes), water craft 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 these rules, certain losses will be quarantined, and deductions claimed only when the asset derives positive net income.

Complex interest deductibility rules exist when 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.

DIVIDENDS

Imputation credit account debit balances

Irrespective of the company's balance date, it's essential to ensure your company's imputation credit account is in credit at 31 March 2020.

Failing this may result in a 10% imputation credit account debit penalty. Consider accelerating terminal tax or provisional tax payments prior to the due dates.

Dividend timing

If your company wants to declare a dividend with a payment date of 31 March or earlier, please note that the dividend documentation has to be actually signed on or before the payment date.

PREPAID EXPENSES

By pre-paying for tax-deductible expenses before 31 March 2020, you'll be able to minimise your tax bill.

Some categories of business expenses can be pre-paid without any limitations, meaning that you can claim as much as you like. Examples include stationery, vehicle registration, accounting and auditing fees and postal charges. Most other expense categories have caps that limit the amount that can be claimed in a year.

MOTOR VEHICLE EXPENSES

If you have a vehicle which hasn't been used one-hundred percent for business purposes, you must have kept a logbook.

A logbook test period can be used to establish a business use percentage for tax, GST and FBT purposes. A new test period might be needed if there has been a significant change in business usage. However, sometimes a representative period may not even be possible, and a permanent logbook will need to be kept.

COMPANIES

Shareholding Continuity & Commonality

Being able to carry forward tax losses is subject to shareholding continuity of 49%. The ability to offset losses against the net income of other group

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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.

Group loss offset elections and subvention payments

Companies which are part of a "group of companies" (i.e. at least 66% commonly-owned) can choose to offset profits and losses.

This rule includes the option for a profit company to make a "subvention payment" for a loss. Elections and subvention payments generally need to be made by the 31 March that follows the balance date of the loss company.

Please note that companies which are part of a group, but which are not 100% commonly-owned, can now choose to transfer imputation credits when (or after) there is a loss offset.

Consolidated group elections

Consider whether your group of companies should form a Tax Consolidated Group to reduce the number of tax returns that need to be filed and to take advantage of the concessions that are available within a Tax Consolidated group.

Elections to join or form a Tax Consolidated Group can take effect from the start of an income year, providing the election is made within 63 working days of balance date.

LOOK THROUGH COMPANIES (LTC)

LTC elections must be received before the start of the income year from which status is required (with the exception of newly incorporated companies). If you wish to revoke an LTC election it must also be received before the start of the income year in which it is to apply from.

Note there can be significant tax implications of electing into and exiting the LTC regime and advice should be obtained.

Also note that there are restrictions on who can be an owner (directly or indirectly), how many owners are allowed, how much foreign-sourced income can be earned if the LTC is more than 50% owned by non-residents, and what distributions can be made by trust owners.

LOAN AND CURRENT ACCOUNTS

If your company has loan accounts which have debit balances (including overdrawn shareholder current accounts), there could be unwelcome tax consequences.

An overdrawn shareholder account means that the shareholder owes money to the company, typically through regular drawings throughout the year, or via a loan. Please contact us to find out whether there might be problems, and how they can be avoided.

TRANSFER PRICING AND INTER-ENTITY LOANS

IRD has **significantly** increased its focus on transfer pricing and related party transactions and has increased its audit activity in this area.

New Zealand's transfer pricing legislation requires that transactions between related parties (for example: entities with common ownership) are

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carried out on an "arm's length" basis. If they aren't adjustments are required to tax liability calculations. IRD generally places the onus of proof on taxpayers to show that all related party transactions are undertaken at arm's length.

Loans between related parties should incur interest at market rates. If interest isn't charged it could trigger a deemed dividend, unless the loan was for a **short-term** working capital loan.

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 your financial statements should be undertaken.

This reconciliation can highlight 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 unreconciled differences exist, we recommend reviewing your GST to identify possible issues.

DONATIONS

Companies (other than LTC's) are allowed a deduction for gifts of money made during the year to organisations which are approved for donation tax credit purposes. However, donations are deductible only to the extent of the company's taxable income for the year.

INTEREST PAYMENTS

If you have paid or pay $5,000 or more in interest payments to anyone (excluding a bank), you will generally have to withhold Resident Withholding Tax any pay it to IRD.

LAND AND PROPERTY SALES

Selling land and property

Surpluses gained from selling land are generally taxable upon settlement. Although dependent on each contract's settlement terms, if a settlement date is deferred beyond 31 March 2020, the sale wouldn't generally be applicable for income tax until the following income tax year.

Residential Property Bright-Line Test

This rule can tax certain residential land which is sold within 2 or 5 years of the acquisition date, irrespective of the purpose or intention at the time the property was acquired.

Some exemptions are available. The bright-line period is 2 years for land acquired between 1 October 2015 and 28 March 2018, and 5 years for land acquired after 28 March 2018.

RESIDENTIAL RENTAL PROPERTIES

New tax rules can mean that losses from residential rental properties are "quarantined" (i.e. suspended) and carried forward until there is enough "residential property income" to claim them against.

Generally speaking, this means that such losses can no longer be claimed against other types of income (e.g. salary and wages). Some exemptions are available. These rules applied from 1 April 2019.

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.

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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).

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.

We 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.

HIGHER INCOME

If your taxable income is significantly more than the previous year, consider making some extra voluntary provisional tax payments. Alternatively, consider aligning tax payments with income.

If you've not paid enough provisional tax, consider using a provisional tax intermediary to help reduce IRD's expensive use of money interest costs.

OVERSEAS INVESTMENTS

Tax on overseas investments is highly complex and will depend on which method must be used to calculate the relevant income. You should review your foreign investments, such as shares, superannuation and life insurance policies. You should determine how changes to your portfolio will affect your potential tax liability.

We strongly recommend seeking tax advice before making changes, particularly if you're considering making lump sum withdrawals or transferring funds from an overseas pension fund.

PAYMENTS TO CONTRACTORS

PAYE and withholding payment rules apply to most contractors. Because of the penalty and use-of-money interest regimes, it is particularly important that you ensure the rules are complied with. Please note that there were some significant changes made to the withholding payment rules, effective from 1 April 2017.

PAYMENTS TO NON-RESIDENTS

PAYE rules or non-resident contractor tax rules might apply to these payments. There are certain exemptions available, which we can assist you with. The non-resident contractor tax rules can also apply to the use (or right to use) in NZ of property other than land, or the services of another person.

If you've paid interest, dividend, or royalties to a non-resident, non-resident withholding tax (NRWT) might apply to these payments.

Please note that there is a new NRWT rule which can apply to NZ residents (or branches) with interest-bearing loans owing to associated non-residents. This rule targets situations where interest payments lag behind accrued interest deductions; NRWT might now need to be paid earlier, based on the interest deductions

and withholding payment rules apply to a wide range of contractors. Because of the penalty and use-of-money interest regimes, it is particularly important that you ensure the rules are complied with. Please note that there were some significant changes made to the withholding payment rules, effective from 1 April 2017.

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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.

PAYMENTS TO NON-RESIDENTS

PAYE rules or Non-Resident Withholding Tax rules generally apply to payments to non-residents. Some exemptions are available. Non-Resident Withholding Tax will generally apply if you have paid interest, dividend, or royalty payments to a non-resident.

REPAIRS AND MAINTENANCE

Broadly speaking, repairs and maintenance expenses are deductible only to the extent they have been incurred during the income tax year. Tax legislation draws a very thin line between a tax-deductible repairs and maintenance and capital expenses (which are not tax-deductible).

Consider making repairs and maintenance before 31 March 2020 to bring forward the tax-deductible expense especially if your rental property has losses. Losses will be subject to new loss "ring-fencing" rules with effective from 1 April 2020.

VEHICLE EXPENSES

If you own a vehicle which hasn't been used exclusively for business, you must keep a vehicle logbook. The logbook must be used to determine a business use percentage for income tax, GST and fringe benefit tax purposes. If business usage has significantly changed, you'll need to recalculate it.

LEGAL FEES

Some legal fees are not tax deductible. For example professional fees related to forming a new company or a trust and some capital expenditure are not tax-deductible.

WORK IN PROGRESS (WIP)

At 31 March 2020 you need to review any jobs "in-progress", to determine their values and a percentage of completion, income received, and expenses incurred to date, and anticipated profit.

RECORD KEEPING

It's important you keep accurate and complete records. Your business' financial records should include bank and credit card statements, proof of income and expenses, cash books and wages records. You need to be organised, keep your records up-to- date and then hold on to them for a minimum of seven complete tax years.

Please contact us if you have any questions about preparing for the end of the financial year.

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