

TAX PLANNING CHECKLIST FOR YEAR ENDING 31 MARCH 2010

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The end of the financial year is now approaching. This is an appropriate time to consider your tax position for the year ending 31 March 2010 and consequently your 2011 provisional tax.

This checklist will enable you to consider what options are available, as well as informing you of current and future taxation rates.

Year end tax planning checklist

Below is a checklist of matters relevant to all business entities which you should consider before 31 March, some of which may help you reduce the amount of tax you have to pay for 2010.

1. Prepaid expenditure

Certain expenditure can be incurred in advance for the 2010 / 2011 year and, provided they are not capitalised to the balance sheet, may be claimed as a tax deduction in your 2010 financial statements.

Some expenses can be prepaid regardless of the amount or period being prepaid, for example:

- Stationery,
- Subscriptions for papers or journals,
- Vehicle registration and road user charges,
- Postage and courier charges,
- Rates,
- Audit and Accounting fees,

Other expenses can be paid in advance only up to a certain limit, for example:

	Max Amount \$	Max No of Months
Rent (if prepayment more than one month)	23,000	6
Rent (if prepayment less than one month)	Any amount	1
Rent or bailment of livestock	23,000	6
Consumables	58,000	N/A
Insurance (where each premium is no more than \$12,000)	N/A	12
Professional or Trade Association subscriptions (where each subscription is no more than \$6,000)	N/A	12
Accommodation or travel	12,000	6
Advertising	12,000	6
Other periodic charges	12,000	12
Other services	12,000	6

The legislation regarding allowable prepayments is complex and we recommend clients discuss with us any plans for prepaying expenses prior to committing to any expense.

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Other prepaid expenditure

Prepaid expenditure on items other than those covered above is only tax deductible to the extent the services have been performed or goods provided. Therefore a payment for repairs made before balance date will generally not be tax deductible unless the repairs have actually been carried out.

2. Holiday pay and bonuses for employees

Amounts payable to employees, for holidays or bonuses at balance date are deductible in the year to 31 March 2010 if paid to the employee within 63 days of balance date. If they are not paid within 63 days of balance date then the deduction can only be claimed in the income tax year that the payments are made.

3. Discount reserve

A deduction for a discount reserve, such as a prompt payment discount, should be allowed if debtors are customarily entitled to this discount. In the first year a deduction of the discount percentage is allowed and in subsequent years adjustments are made which maintain the discount level at the approved percentage of the debtors. However if the credit period offered to customers is more than 93 days different rules will apply.

4. Guarantee / warranty provisions

The Privy Council held in *CIR v Mitsubishi Motors New Zealand Limited* that a warranty provision was deductible in the year that defective goods are sold provided that a definite commitment is able to be established and the amount of the liability can be calculated as at balance date. Please contact your Lynch Phibbs Ltd advisor who will be able to assist you if you are considering claiming a deduction for guarantee or warranty provisions.

5. Repairs and maintenance

Generally no deductions are allowed for repairs and maintenance reserve. It may be worthwhile undertaking repairs and maintenance prior to 31 March to obtain a full deduction. Deciding whether expenditure on an asset is deductible as repairs and maintenance or should be capitalised is often a difficult decision – your Lynch Phibbs Ltd advisor can assist you.

6. Valuation of trading stock (not including livestock)

Trading stock is required to be valued using a cost valuation method. Market selling value may be used only when it is lower than cost. Formula write downs no longer apply although the market selling value may be used in this case. There is also no provision for the write off of obsolete stock. Therefore, to reduce the value of these items in stock on hand, they should be physically disposed of or, alternatively, valued at market selling value, which will presumably be lower than cost.

Replacement price and discounted selling price may be used to approximate cost if these methods are also used for financial reporting purposes. Please contact your Lynch Phibbs Ltd advisor if you require more information on the valuation methods.

7. Bad debts

To claim a deduction for a bad debt in the year to 31 March, the debt must be bad, and must actually be written off during the year.

Whether a debt is 'bad' is a matter of fact, but there must be no reasonable expectation of recovery.

There must be evidence to verify that a debt has been written off.

8. Retentions

Retentions on building contracts are generally taxable in the year the contractor becomes legally entitled to receive them. Therefore if retentions are outstanding at the year end, they usually do not form part of your income for tax purposes for that year, and are therefore only taxed when they become due. This can result in a significant deferral of income.

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General tips on minimising tax

1. Splitting your income

Depending on your business structure it may be possible to split income between yourself and your spouse or children to obtain the benefit of lower tax rates. For example, in a partnership, the net income of the partnership is split between the partners based on their agreed share of the partnership. Inland Revenue is entitled to revise the split in certain circumstances.

Savings may be achieved by splitting income with your spouse, depending on the other income earned by your spouse.

2. Wages

Wages can be paid to your spouse, your children and relatives who work in your business, but Inland Revenue can make adjustments if payments are considered excessive.

If self employed, before making payments to your spouse you must obtain approval from Inland Revenue and you must be able to show that your spouse will be working and that the wage is commensurate with the work done.

Where your children are working for you or your business, we recommend that you draw cheques in relation to work done on your business account and pay them into your child's account at appropriate times during the year. Remember that if children earn less than \$2,340 in a year (excluding dividends and interest) no PAYE needs to be deducted. However ACC levies are payable in respect of wages paid.

3. Home office expenses

If you use an area in your home principally as an office or storage area for your business, then you may be able to claim part of the overall costs of running your house as a business expense.

Floor area is the most common base used for calculating the portion claimable. For example, if the area you use amounts to 10% of the house's total floor area, then you can claim 10% of expenses such as annual rates, house insurance premium, power, mortgage interest, and house depreciation. It may also be possible to claim a portion of your home telephone rental.

4. Farmer's dwelling expenses

Inland Revenue allows farmers to claim 25% of all of their dwelling expenses, where that dwelling is situated on their farm, because of their need to run their farming business at home. These expenses will include:

- Domestic power
- Dwelling repairs and maintenance
- Dwelling depreciation

Household insurance

5. Tax rebates and tax credits available

Common tax rebates and tax credits available are:

- Child taxpayer rebate – not taxed on first \$2,340 income in certain circumstances
- Housekeeper / childcare rebate
- From 1 April 2008. Individuals can claim a tax rebate of 33 $\frac{1}{3}$ % of all charitable donations made, up to their net taxable income. Companies will be entitled to claim a deduction for charitable donations up to the company's net income.

From January 2010, individuals who make charitable donations by way of Payroll Giving (i.e. deduction direct from salary or wages) will get the benefit of the donation rebate immediately as a net reduction in PAYE deductions.

Claims for the housekeeper / childcare rebate and the donations rebate (on donations other than Payroll Giving) must be made on a separate rebate claim form. Inland Revenue will forward claim forms to every taxpayer (or their agent) who has claimed either of these rebates in the last two years.

As from 01 April 2008 low income earner rebate available to income earners below \$38,000 has been withdrawn. This rebate has been reflected in the new provisional tax rate applying at that time

Working for Family assistant payments for low income families may be available in certain circumstances for:

- Family tax credit
- Minimum family tax credit
- In-work tax credit (or Child tax credit)
- Parental tax credit

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6. Scrapping unused assets

A taxpayer may write-off a depreciable asset where the cost of disposing of an asset is expected to be greater than the proceeds from its sale

7. Tax deductions available to wage earners

Deductions available include:

- Fees paid for the preparation of a tax return
- Premiums for income continuance insurance, where income is a relevant factor in determining the amount insured. Any claims received from such policies are taxable income.

8. Claim your vehicle expenses

If you have a vehicle (not a company vehicle) which is used for business and private purposes, there are several options available for claiming the business portion of expenses:

- If your business running in the vehicle is less than 5,000 km per year, you can use pre-determined Inland Revenue Department rates or the published rates of a reputable independent source (eg Automobile Association) as the basis of your claim. Current IRD rates are 70 c/km up to 3,000 km then 19 c/km thereafter. You must keep a record of all business journeys to substantiate your claim.
- Keep a logbook for 90 consecutive days recording all journeys. Based on the business use percentage from the logbook, you can claim this proportion of all vehicle expenses. You can continue to use this percentage for three years, provided that the actual business use in any month does not vary by 20% or more, than the percentages established by the logbook.

Option (i) can be particularly useful if a private vehicle is only used occasionally for business use. There are also GST implications to be considered.

Note: Similar rules govern the rates at which an employer may make tax free reimbursement to employees (including shareholder-employees) who use their private vehicles for work purposes. These include use of mileage rates published by a reputable independent source (eg Automobile Association)

Help us to process your records efficiently and quickly

By completing the Business Checklist we send to you before your balance date, you can ensure that all the information needed to complete your accounts is provided to us before we begin.

Some further items which may help us are:

- GST returns and worksheets – including these with your annual information ensures that we can follow up any GST issues during the process of completing your accounts.
- Highlighting any repairs and maintenance costs over \$500 and noting on your records what the payment was for e.g. 'repairs to cash register'. Asset purchases and sales must be separately recorded on your Fixed Asset Schedule.
- Identify in your records any entertainment costs. Generally expenses are 50% deductible if they are enjoyed by staff at a staff function, but are subject to Fringe Benefit Tax if available for enjoyment at staff discretion.
- Where a vehicle is not a company vehicle liable for FBT, expenses relating to vehicles used partly for private use should be separately highlighted in your records to enable us to calculate the total expenses for that vehicle, and the respective non-deductible portion.

Another area often overlooked by clients is overseas investments. Investments in foreign superannuation schemes and life insurance policies can be taxable in New Zealand, even if you are no longer contributing to them, or receiving income from them.

Any investment of share capital in a foreign company (or unit trust) can also result in New Zealand tax, even if no dividends are received, although there are significant exemptions.

Please ensure you advise us of any overseas investments, to enable us to confirm their tax status. The penalties for non declaration of overseas income are severe.

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Help yourself – keep your records

To prove your deductions are legitimate you must keep all relevant records for at least seven years and they must be in English. The following records, which are not an exhaustive list, must be kept:

- **All** income received (copies of invoices issued etc)
- **All** tax invoices and receipts for purchases, insurance, power, phone and all other costs incurred
- Bank statements
- Cash books or computerised accounting records
- Wage records for any employees
- Interest and dividend payments
- A list of business assets and liabilities
- Statements of year end trading stock, and stocktake records
- Credit and debit notes
- Motor-vehicle log books

Keeping records in order makes good sense. If you are investigated by Inland Revenue you should be able to justify all your claims with a minimum of time and effort.

Penalties Regime

Under the current penalties regime, tax shortfalls may result in:

- Use of money interest charged from the original due date to date of payment
- Possible penalties depending on the taxpayer's conduct

Penalties are levied if Inland Revenue consider the taxpayer is guilty of:

Type of error	Penalties
Lack of reasonable care	20%
Unacceptable tax position	20%
Gross carelessness	40%
Abusive tax position	100%
Tax evasion	150%

Reduction of these penalties is possible in some circumstances (eg voluntary disclosure to Inland Revenue). These penalties also apply to all other tax types including GST, PAYE and FBT.

We are able to review your systems if you wish to ensure that you are paying the correct amount of tax or wish to reduce any risk of penalties.

It is therefore particularly important for you to ensure that all relevant issues are brought to our attention when we are preparing your financial statements, to reduce any risk of penalties. We are able to review your systems if you wish to ensure that you are paying the correct amount of tax or wish to reduce any risk of penalties. We can provide you with more information about penalties issues, if required.

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Current Taxation Rates

Income Tax

	2009/10	2010/11
Individuals		
\$0 - \$14,000	12.5%	12.5%
\$14,001 - \$48,000	21%	21%
\$48,001 - \$70,000	33%	33%
\$70,001 or more	38%	38%
Other entities		
Companies	30%	30%
Complying Trusts	33%	33%

Resident Withholding Tax

From 01 April 2010:

- The RWT rate on dividends is 33%.
- On interest, individuals can elect to have RWT deducted at 12.5%, 21%, 33% or 38%.
- The company RWT rate on interest is 33% (unless the payer chooses to use a 30% rate).
- The non-declaration rate is 38%.

Provisional Tax Basis – 2011 Provisional Tax

For taxpayers who are not using GST ratio method for calculating provisional tax instalments, the methods for calculating 2011 provisional tax are:

- If the 2010 tax return has not yet been filed and the instalments is the first or second instalment, based on 2009 RIT plus 10%;
- If the 2010 tax return has been filed or if the instalment is the third instalment based on 2010 RIT plus 5%.

RIT = Residual Income Tax: the net amount of tax payable for the year, after deducting source deducted tax (e.g. PAYE or RWT), but not provisional tax.

Provisional tax can be estimated at any time up to the due date of the final instalment. A lack of reasonable care shortfall penalty of 20% could be imposed if Inland Revenue considers that insufficient care was taken in arriving at the estimated figure.

Use of Money Interest (UOMI)

UOMI is payable by:

- All companies and trusts with RIT greater than \$2,500
- All taxpayers who estimate their provisional tax
- Individuals with RIT greater than \$50,000

Depending on your situation, interest will be calculated on any terminal tax due (i.e. after provisional tax payments are taken into account) from the due date of the provisional tax payments to the date the terminal tax is paid – your Lynch Phibbs Ltd advisor can give you further details.

UOMI received is taxable income. UOMI paid taxpayers including businesses is tax deductible in certain circumstances.

Recent UOMI rates applying to tax overpayments (Cr) and underpayments (Dr) are as follows:

Period	Overpayments (Cr)	Underpayments (Dr)
8 March 2007 to 28 February 2009	6.66%	14.24%
1 March 2009 to 28 June 2009	4.23%	9.73%
From 29 Jun 2009 onwards	1.82%	8.91%

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