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YEAR END TAX IMPLICATIONS

There are a number of issues that need to be considered when preparing year end financial statements. The timing and treatment of certain expense items can have tax implications, and in some cases the accounting treatments applied can result in tax efficiencies.

Typically accountants in conjunction with the business owners, need to consider the treatment of certain expenditure in particular whether it can be brought forward into the current period. The general rule is that business expenditure is deductible in the tax year that it is incurred.

Bad Debts

Have you written off all debts that you consider are 'bad'?

Individual trade debts should be reviewed and actually written off in your debtor ledger prior to balance date for them to be allowed as a deduction in the financial year. A debt is considered bad if a reasonable and prudent business person would be of the view it is unlikely that the debt will be paid. Factors to consider are the length of time the debt is outstanding, and the efforts that you have taken to collect the debt and information on the debtor. A debtor does not need to be insolvent for the debt to be bad, so you can still pursue the debtor for payment.

Loan Accounts & Current Accounts

If your company has loan accounts which have debit balances (including overdrawn current accounts), there could be undesirable tax consequences. Please contact us to find out whether there might be problems, and how they can be avoided.

Donations

Gifts of money

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 net income for the year ("net income" is the year's income after claiming deductions).

Gifts of trading stock

A special rule provides a fairer outcome if trading stock is donated between 17 March 2020 and 31 March 2024 (the end date was 31 March 2023, but has now been extended). Please note that some types of trading stock are not covered by this rule. The application of the rule can depend on whether there is a "business purpose" for the donation, and also on who the recipient is.

Dividends

Imputation credit account debit balances

Irrespective of the company's balance date, it is essential to ensure your company's imputation credit account is in credit at 31 March 2023. Failing this could result in a 10% imputation credit account debit penalty. As a solution you may wish to 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.

Interest Payments

Have you paid more than \$5,000 in interest

(other than to recipients who had RWT-exempt status)?

If you have, you may be required to withhold resident withholding tax.



RESIDENTIAL RENTAL PROPERTIES

Loss ring-fencing rules

Special 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 the beginning of the 2019/20 income year (1 April 2019 if you have a standard balance date).

Interest expenditure limitation rules

Special rules can limit the deductibility of interest expenditure incurred in relation to properties located in NZ. For some loans, there is a deduction phase-out period from 1 October 2021 to 31 March 2025. There are special definitions, exceptions, and exemptions (e.g. for new houses).

Higher Income

Is your income significantly higher than the previous year? If so, you should consider whether an additional voluntary provisional tax payment may be appropriate or alternatively it may be beneficial in aligning your tax payments with turnover. Please discuss with us before balance date. If you have underpaid your provisional tax for the year then it may be possible to use a provisional tax intermediary to save Inland Revenue use of money interest costs.

Purchases and sales

A full month's depreciation can be claimed for any part month that an asset is owned and used. It may be worth buying replacement assets on or just before balance date to obtain one month's worth of depreciation deduction. If you expect to make a loss on sale, consider selling prior to balance date. If you expect to make a gain on sale, consider deferring the sale until after balance date. This will accelerate any available deduction or decelerate the requirement to return taxable income.

Commercial fit-out

The rate of depreciation on buildings for tax purposes is 0% (only residential buildings from the 2020/21 income year). To maximise depreciation deductions it is important to separately identify, where possible, commercial fit-out (depreciation deductions can be claimed).

Fixed Assets

Assets no longer used in the business

For tax purposes fixed assets can be written off if:

- The asset is no longer in use by the business; and
- Is not intended to be used in the future; and
- The cost of disposing the asset would be more than its disposal value.
- We recommend assets be reviewed for use, to determine whether or not a deduction would be available.

Low value assets

Low value assets with a cost below a certain threshold can be written off immediately. The thresholds are :

- For assets purchased before 17 March 2020 : \$500
- For assets purchased on or after 17 March 2020 and before 17 March 2021: \$5,000
- For assets purchased on or after 17 March 2021 : \$1,000

The threshold amounts are GST exclusive if the taxpayer is GST-registered. However, there are two scenarios where an immediate write-off is not permitted :

- If the low-value item becomes part of any other property that is depreciable property, or is an improvement/upgrade of that property
- If more than one low-value asset is purchased from the same supplier at the same time, and if those assets have the same depreciation rate and the total cost exceeds the relevant threshold.



LAND SALES

Sale of taxable land

Taxable income arising from the sale of land is generally derived on settlement. Although dependent on the terms of each contract, if the settlement date is extended beyond balance date (i.e. 1 April and beyond for standard balance dates) any sale would not need to be recognised for income tax until the following year.

Bright-line test for residential properties

This rule can tax certain residential land which is sold within 2, 5 or 10 years of the acquisition date, irrespective of the purpose or intention at the time the property was acquired. The bright-line period is 2 years for land acquired between 1 October 2015 and 28 March 2018, 5 years for land acquired between 29 March 2018 and 26 March 2021, and 10 years for land acquired after 26 March 2021. Special rules apply, and some exemptions are available.

Habitual buying and selling

Although New Zealand does not have a general capital gains tax as such, gains on sales of certain types of land transactions are subject to income tax. If a person is subject to tax under one of the land transaction provisions, they may however be excluded from taxation if they qualify for the main home exclusion, residential exclusion or business premises exclusion.

These three exclusions will not apply if a person has a regular pattern of buying and selling land. The principle underlying these restrictions is that a regular pattern of buying and selling, or developing and selling family homes or business premises is indicative of a profit motive.

There are concerns that the current regular pattern restrictions as they currently stand allow taxpayers who habitually buy and sell land to structure around the rules as they currently apply quite narrowly to the activities of a single person. The current rules can be circumvented by using different people or entities to carry out separate transactions or by varying each transaction so that there is no pattern.

The proposed amendments expand the regular pattern restrictions to apply to regular patterns of buying and selling land by a "group of persons acting together".

Main Home and Residential Exclusions

For the main home and residential exclusions, a group of persons will be treated as undertaking buying and selling activities together when:

- all the people occupy all of the properties together as their residence; and
- where a property is owned by a trustee or other entity, at least one of the people who
- occupy all the properties has significant involvement in, or control of, the trust or other entity.

OVERSEAS INVESTMENTS

Do you have any investments or interests in overseas entities?

The tax treatment of overseas investments is complicated and dependent on the method required to calculate the income.

You should review the tax treatment of your foreign investments such as equities, superannuation or life insurance policies and consider any changes that may have been made within the year. Obtain specific tax advice prior to making changes especially if considering a lump sum withdrawal or transfer from an overseas superannuation or pension fund.

Prepaid Expenditure

Certain types of expenditure can be claimed as a tax deduction in the year in which they are incurred regardless of the fact that the good or service will not be used until a future year, but only if they have also been expensed for financial reporting purposes. Some of these prepayment concessions have a dollar limit and/or a limit on the length of the period after year-end.

The following prepaid expenses could be claimed in the 2022/23 income year:

- Advertising for up to 6 months after the balance date and not exceeding \$14,000 in total;
- Insurance for up to 12 months after the balance date as long as the premiums incurred during the year for the contract do not exceed \$12,000;
- Rates to the extent of the amount invoiced on or before balance date;
- Rent for up to 6 months after the balance date and not exceeding \$26,000 in total. There is no monetary limit for rent that is prepaid not more than one month in advance;
- Subscriptions or fees for membership in any trade or professional association, for up to 12 months after the balance date as long as the expenditure incurred during the year for membership in the association does not exceed \$6,000;
- Advance bookings for travel and accommodation, to be used within 6 months after balance date and not exceeding \$14,000 in total;
- Service or maintenance contract for plant, equipment or machinery, for up to 3 months after balance date, as long as the expenditure incurred during the year for the contract does not exceed \$23,000;
- Use or maintenance of telephone and other communication equipment for up to 2 months after balance date (amount is unlimited);
- Consumable aids (i.e. items that do not become a component of the finished stock, e.g. oil, grinding wheels, chemicals, wrapping and packaging) not exceeding \$58,000 in total;
- Audit fees and mandatory accounting fees (unlimited);
- Stationery, subscriptions for newspapers, journals or other periodicals, and postal and courier services (unlimited);
- Vehicle registration fees, drivers license fees and road user charges (unlimited);
- Other services for up to 6 months after balance date, and not exceeding \$14,000 in total;
- Other periodic charges for up to 12 months after the balance date, and not exceeding \$14,000 in total.

Repairs & Maintenance Expenditure

Generally speaking, repairs and maintenance expenditure is deductible only to the extent it has been incurred during the income year. There can also be a fine line between a deductible repair/maintenance expense and capital expenditure (i.e. non-deductible). You may wish to consider accelerating repair/maintenance expenditure in order to bring forward the deduction.

Trading Stock

Trading stock (excluding livestock) on hand at year end must be valued, subject to meeting the relevant criteria, using one of the prescribed methods: cost; discounted selling price; replacement price or market selling value if lower than cost. Generally, these methods must be applied consistently.

Provisions for obsolete stock or stock write downs are not generally allowed as tax deductions.

Therefore prior to year end it is important to perform a stock take and to ensure that all obsolete stock is physically disposed of or is valued using one of the prescribed methods. Concessional rules can apply to taxpayers with a turnover of \$3 million or less. A further concession is that a taxpayer with a turnover of \$1.3 million or less can value their closing stock at the opening stock value, as long as the closing stock is reasonably estimated to be worth less than \$10,000.

Vehicle Expenses

If you have a vehicle which has not been used 100% for business purposes, have you 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.

Legal Fees

Not all legal fees incurred by a business may be claimed as a deductible expense, for example fees in relation to forming a company or trust and capital asset purchases; these are considered capital in nature for tax purposes ("capital limitation"). Legal fees should be reviewed for deductibility.

The capital limitation can be ignored for qualifying legal expenses if the year's total expenditure on all qualifying legal expenses does not exceed \$10,000 (excluding GST).



Small Business Cash Flow Loan Scheme (SBCS)

Government will provide loans to small businesses, including sole traders and the self-employed, impacted by COVID-19 to support their cash flow needs.

Applications have been extended and are now open until 31 December 2023. You can apply through myIR. The small business cash flow loan scheme will provide assistance of up to \$100,000 to businesses employing 50 or fewer full-time employees. This includes sole traders and self-employed businesses.

Details of the loans include:

- \$10,000 to be provided to eligible businesses
- an additional \$1800 per equivalent full-time employee
- interest free if the loan is paid back within two years
- an interest rate of 3% for a maximum term of five years
- repayments not required for the first two years
- you must show at least a 30% drop in revenue due to Covid-19, measured over a 14-day period in the past 6 months
- maximum amount you can borrow depends on the number of full-time and part-time employees.

TAX CALENDAR - APRIL / MAY 2023

7 April

Terminal tax for 2022 (March, April, May and June balance dates)
For all clients except those who have lost their extension of time privilege

7 May

3rd instalment of 2023 Provisional Tax (March balance date) GST for March 2023

28 May

1st Instalment 2024 Provisional Tax (December balance date)

31 May

Deadline for Fringe Benefits Tax returns

Disclaimer: This publication has been carefully prepared, but it has been written in general terms only. The publication should not be relied upon to provide specific information without also obtaining appropriate professional advice after detailed examination of your particular situation.