The Accounting Income Method

The IRD have recently introduced the Accounting Income Method (AIM) which has been developed for small and medium sized businesses (gross annual income of less than $5 million) to relieve the pressure of the traditional provisional tax system, replacing it with an income/profit aligned provisional tax regime.

Instalment dates are aligned with GST payment dates. For those registered on a monthly basis, provisional tax payments are made monthly. For all others (registered and non-registered) payments are made two-monthly.

Under AIM, use-of-money interest (UOMI) on under-payments of provisional tax will not apply provided that the taxpayer has paid the amount as calculated using the AIM-capable accounting software on the due date. If less than the amount calculated by the system is paid then use-of-money interest applies from the first provisional tax date. No UOMI is paid by the Commissioner on overpayments.

One advantage of AIM is that when losses occur it is possible to receive refunds of overpaid tax immediately rather than waiting until year end. However, since the changes to the UOMI calculations the AIM option currently presents less advantages.

Using the standard uplift method as long as residual income tax (RIT) is less than $60,000 no UOMI is charged on the underpayments of provisional tax. In addition, UOMI has been removed from the first two instalments of provisional tax where the standard method uplift is used and RIT is $60,000 or greater. UOMI will however apply from the third and final instalment however as this instalment occurs subsequent to balance date taxpayers will be in a position to better calculate the last instalment. In addition, tax pooling could be used at a later date to manage the final instalment to mitigate UOMI as rates charged by tax intermediaries are less than the UOMI rate.

With regard to the AIM method, tax Pooling cannot be used for Provisional Tax, but can still be used for terminal tax and reassessments of tax.

AIM is only available on certain Accounting Software approved by IRD. In its current form AIM creates a significant amount of additional compliance work in set up of the reporting system, but also having the accounts up to date for each filing period. In addition, having the correct depreciation deductions claimed, private expenses and non-deductible items calculated, and shareholders salary quantified for the period e.g. a shareholder's salary provision will be necessary.

The taxpayer must take reasonable care when calculating tax liabilities under this method and could still be exposed to penalties for not doing so.

The "aim" of this new regime was to simplify the accounting and tax process and even out cash flow for Taxpayers; it appears that it still has some way to go.

It may be easier and more economically feasible to follow the standard uplift method for now and re-review the AIM methods applicability in the next financial period once any issues have been resolved and people have had a chance to comment on its effectiveness.