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**FINANCIAL FEATURE  
 FEBRUARY 2008**

**We welcome any input into areas you would like us to cover. If you have any topics you would like covered in a future newsletter, please provide us with some details and we will try and accommodate your request.**

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**COMPANY TAX RATE**

The Income Tax rate for companies will decrease from 33 cents per dollar, to 30 cents. The saving of three cents in tax means that whatever income that can be deferred to next year, should be.

For instance, if you were to sell produce or stock, or a major asset, you may want to defer the sale and date the invoice in the month after your balance date.

Farmers have the ability to pay into an Income Equalisation Account. This is a deposit scheme run by the Inland Revenue where you receive interest on the deposit held by the Inland Revenue. It is in place to help farmers who have abnormally large fluctuations in income as they will in 2008.

This will not suit every company and if you are unsure of the impact on your company, give us a call.

**MINIMUM WAGE RATE INCREASE**

Effective from 1 April 2008, the adult minimum wage will increase to \$12 per hour. This applies to all workers over the age of 18. The youth wage, for 16 and 17 year olds will increase to \$9.60 per hour, which equates to 80% of the adult wage.

Last year the adult minimum increased to \$11.25, an increase of 8%. This year's increase of around 7% is also well above inflation. It means that a minimum gross wage of \$480 is payable for a 40 hour week.

The minimum wage for youth workers has increased from \$9.00 to \$9.60. This equates to a gross wage of \$384 payable for a 40 hour week.

**New Entrant – Youth Wage**

The youth wage system will change on 1 April 2008. It will be replaced by a 'New Entrant' minimum wage rate. This new system will mean that if your new employee is between 16 and 17 you can pay them youth rates for the first 200 hours, or the first three months of employment.

Once the 16 – 17 year old has been at work for more than three months, you are obliged to pay them the full adult wage of \$12. This has taken the shine off employing school leavers.

**END OF FINANCIAL YEAR ADJUSTMENTS**

**Debtors & Creditors**

Certain items need to be included in the end of year accounts even though they may fall outside the return period. For March balance dates, this includes 1st April to 31st March.

Debtors and Creditors are a normal part of every business. Where a transaction date falls within the period of the return, it must be included even though it is paid or received later.

Even Eftpos transactions for the vendor are processed the day after the sale is completed. So even though a retail business that does not normally retain any cash at balance date, may still have debtors in the form of the next business days Eftpos deposits.

**Trading Stock**

The Inland Revenue has in the past looked very hard at the valuation of the closing stock. As the value can dictate the profit of the business, you will need to back up valuations with stock sheets, etc.

If you simply repeat last years figure, you have obviously guessed. The figure needs to be based on a cost based system. You can also use the market value, even if the market value is lower than the cost.

It would be wise to spend some time compiling a list and assessing each stock item as accurately as possible. Then include the cost of the most current items and write down older stock items to a market value. The keyword is consistency. Keep valuing your stock consistently from year to year.

**Repairs & Maintenance**

Remember, any assets purchased for less than \$500 do not need to be capitalized and depreciated.

If you are GST registered, the figure is \$500 exclusive of GST. If you are not registered the figure is \$500 inclusive of GST.

If you are buying 10 chairs for \$100 each (\$1,000) on one invoice, the asset is in excess of \$500 dollars. Yes, even though there a 10 items, the invoice is over \$500 and they have to be capitalised. It may seem pedantic, but ask for two separate invoices where you will be unfairly penalized for bulk purchases.

Repairs are allowed by the Inland Revenue for any value, as long as it is replacing part of an asset that already existed. For instance, you own a rental property with the house listed by itself in the depreciation schedule. You decide to replace the stove for \$1,000. This is a repair.

If the stove was listed separately in the asset schedule, this would be replacing an existing asset. You would write off the old asset and include the new asset on the asset schedule.

Another example would be replacing car tyres and rims with mags or lower profile sets of wheels. If they cost over \$500, you would need to capitalize the new wheels. The key would then be to get them billed separately if they were valued at less than \$500 each.

**Bad Debts**

When you have a debt sitting on your debtors schedule that you are reasonably confident will never be paid, the debt needs to be written off the schedule before the end of the financial year. If you retain these bad debts on your schedule (in the hope they will pay you), they need to be returned as income. You need to physically remove the bad debt.

**BUSINESS SALES & GOING CONCERNS**

Business sale and purchases happen all the time and it is important you know the meaning of a going concern.

A going concern ignores GST when the sale and purchase agreement is drawn up. The Inland Revenue realise that there is no GST on the transaction. The seller does not add it to the sale price and the purchaser does not make a claim. Both the vendor and purchaser need to be GST registered.

Farms and corner dairies are similar in the fact that they both require certain plant and equipment and stock to operate. When the business is sold, it can only be a going concern if all of the assets that are crucial to the running of that business are included in the sale.

For instance, the farmer cannot sell the farm as a going concern without the plant and livestock, as all the assets relate to the business operation. Similarly, the corner dairy operator cannot sell the stock and lease/premises, while keeping the delivery van and office equipment.

Another situation that can trip up contracts is where a landlord cannot sell a commercial property as a going concern if the tenant does not remain in the property.

For instance, two related entities run the corner dairy. The Ma & Pa Trust owns the building (Commercial Landlord) and the Ma & Pa Partnership run the business (Tenant). If the Trust sells the property as a going concern, the Partnership must still be the tenant to be considered a going concern. If the tenancy is vacant, the transaction to sell the property needs to be sold plus GST.

To make the situation even more complicated is where there are multiple activities in the one entity. For instance, the corner dairy also has a dry-cleaning business attached. You would need to sell the dry-cleaning business with all of the necessary assets required to complete the business operations to qualify as a going concern.

**GST & PROVISIONAL TAX ALIGNMENT**

In the August 2007 newsletter we discussed the current Inland Revenue initiative to align the two taxes and file just one payment slip.

This is just a reminder to those who do not have their GST periods aligned with their Income Tax balance date. This will be completed for you by the Inland Revenue in March 2008.

For instance, you have a March balance date and your current GST period is 2 monthly, ending 29 February. To align your GST with your balance date a one monthly return will need to be completed for March.

If you are six monthly, (returning from November to April), your return period will change from November to March and you will complete a five month return.

Keep this in mind if you have a major sale or purchase toward the end of your GST return period.

## PROVISIONAL TAX - RATIO OPTION

The current change to the Provisional Tax regime is the introduction of a new method of calculation. Under the ratio method the Provisional Tax payment is calculated by a percentage of the entity's cash sales. It links your GST to your cashflow.

Certain capital sales are ignored so as not to distort your sales figure. There are some restrictions to who can enter this regime. For instance, your entity must pay GST and Provisional Tax on a single IRD number.

Partnerships won't work, because the GST is paid under the partnership and the Provisional Tax is paid under the individual partner's IRD numbers.

Companies that pay out all the income to the shareholders\ employees won't qualify. The Company will pay the GST, while the Provisional Tax is paid under the shareholder\ employee's IRD number(s).

The ratio method allows the taxpayer to pay their Provisional Tax based on the previous year's tax with the uplift or reduction pinned to total sales. See the below calculation.

### Example

Your residual (total) Income Tax is \$9,500 and your GST taxable supplies were \$160,000.

Your ratio percentage is;

$$\begin{aligned} \$9,500 / \$160,000 &= 0.059375 \\ &= 5.9\% \end{aligned}$$

Your current two monthly GST taxable supplies (total GST income) is \$22,000.

$$\$22,000 \times 5.9\% = \$1,298 \text{ Provisional Tax due}$$

(Example taken from Inland Revenue Booklet IR851)

This payment will be added to your GST payment and paid on the same return.

There are some benefits of this arrangement, as discussed above. However the main benefit of this method is that if you under pay your Provisional Tax you will not be charged Use of Money Interest (UOMI).

Therefore, you may have been more profitable this year and kept your expenses down. Any extra income will be taxed, but you won't be charged UOMI on the shortfall of residual tax that should have been paid through Provisional Tax.

Currently the Inland Revenue charge UOMI at 14.24%.

On the other side of the coin, you will not receive interest on overpaid Provisional Tax. The rate foregone here is 6.66%.

Under the ratio option you will make 6 payments of Provisional Tax, instead of the current 3 payments. Six monthly GST periods are not allowed to use the ratio option. You can still make 3 standard payments as you have in the past, or two if you are six monthly GST registered.

You cannot use the ratio option if your residual Income Tax is above \$150,000. If you would like a leaflet on this topic,

we have some in our office which you can pick up, or we can mail them out to you.

If you would like to use this method, please let us know as we need to contact the Inland Revenue before the start of the tax year in which you would like to participate.

## GST - ACCOUNTING BASIS & PERIODS

Some industry incomes fluctuate from year to year and as other businesses become more established, we need to continually review the accounting basis and the period that each return should cover.

There are three types of accounting basis that you can apply to your GST return.

### Invoice

The first listed in the GST guide is the 'invoice' basis. This method requires you to include any income that you have billed to a customer. You can then claim any invoices due to be paid, even though they may not yet have been paid.

Your GST reconciliation must include all revenue & payments on your bank statement as well as those due to be paid/received. These are called accruals. The accruals are reversed in the next period and the new accruals are added for the subsequent return.

This method is a bit more complicated than the payments basis.

### Payments

The most commonly used is the 'payments', or cash basis. This method is simple to use. You can claim any expense that you have paid during the period that has crystallised on your bank (or other institutions) statement. Similarly, any income on that statement needs to be returned as income.

The fact that you have sent your cheque in the mail does not constitute payment. To use this method your gross turnover (exclusive of GST) needs to be less than \$1.3 million.

There is one main exception. If you have a delayed settlement transaction (eg. the purchase of a property greater than a twelve month period into the future) that exceeds \$225,000 (inclusive of GST). This delayed settlement transaction must be treated as you would on the invoice basis.

For instance, you are in a business partnership and have formed a trust. You have decided to sell your business property to the trust. You invoice the trust in February 2008 for takeover on 1st June 2009. This is a delayed settlement as it is more than 1 year in the future.

The trust is on invoice basis and claims the GST straight away. The partnership is on a payments basis and won't return GST until it gets paid in June 2009. Therefore the trust has the GST refund in the bank for an extended period of time before the partnership has to pay the sale GST to the Inland Revenue.

**Hybrid**

This basis combines the other two, invoice and payments. You return your income on an invoice basis and your payments on a cash basis.

This option ensures the Inland Revenue gets the income GST in as soon as possible. Not many clients know about, or prefer this option.

**Accounting Period**

The length of period of your GST return can be one, two or six monthly. If you don't choose a period you will be given a two monthly return period. You have a choice dependant on the guides outlined below.

You can use 6 monthly if your expected annual gross income is less than \$250,000 (exclusive of GST). You can ignore large one off capital items sold.

Once you breach this you are limited to the one or two monthly options. The only restriction to using a two monthly return period is if your total gross income exclusive of GST exceeds \$24 million.

**KIWISAVER**

In July 2007 the Government launched Kiwisaver, a savings scheme for employees or shareholder/employees who can contribute and gain a contribution from their employer.

The employee can contribute either 4% or 8% of their gross wage. The employer must make contributions on behalf of the employee based on the table below. Any contributions made before 1 April 2008 are not yet matched by the employer.

<b>Compulsory Employer Contribution</b>	<b>Of your gross salary or wage</b>
From 1 April 2008	1%
From 1 April 2009	2%
From 1 April 2010	3%
From 1 April 2011 onwards	4%

The Government will provide the employer with up to \$20 per week (\$1,040 pa) to help pay the employees 1% in 2008. This payment is per employee contributing to the scheme. In the first year the employee could earn \$104,000 and the employer would need to contribute 1%, which equals \$1,040.

You need to be in the scheme for 5 years, or until you are sixty five. Therefore, if you join at 64, you will not receive your contributions until you are 69. Also the employer contributions will stop when you turn 65 but you will retain the \$1,000 kick-start from the Government.

Therefore, shareholder/employees of companies could pay

themselves \$26,000 pa, with a 4% contribution of \$1,040. The employer would match this at 4%, creating a payment of \$2,080. This is an expense to the business and the Government would pay \$1,040 to the company tax free.

The Government will also provide the employee with investment fee subsidies which will lessen the impact of management expenses.

The employee would get the \$1,000 kick-start on top of this for guaranteed saving. The only uncertainty we foresee in the current environment is the volatility in the stock market both domestically and internationally. You may be getting in at the top of the cycle and be faced with troughs in the near future.

However, all investments have peaks and troughs and if you are in for the long haul, you should ignore the volatility of the markets and let the Investment Managers do all the worrying.

Casual employees that have holiday pay included in their wages are not subject to automatic enrolment. Compulsory payments are not made for ACC income or paid parental leave. You must choose to make these yourself.

Remember to do your back ground on your preferred provider and choose carefully. If you aren't bothered over which provider you will end up with, the Inland Revenue will choose for you.

**FINISH WITH A JOKE**

**Callout Reponse (Don't try this at home)**

One night Granddad was going up to bed when Grandma told him that he'd left the light on in the garden shed, which she could see from the bedroom window. Granddad opened the back door to go and turn off the light but saw that there were people in the shed stealing things.

He phoned the police, who asked "Is someone in your house?" And he said "no". Then they said that all patrols were busy, and that he should simply lock his door and an officer would be along when available. Granddad said, "Okay," hung up, counted to 30, and phoned the police again.

"Hello, I just called you a few seconds ago because there were people stealing things from my shed. Well, you don't have to worry about them now because I've just shot them". Then hung up.

Within five minutes three police cars, an Armed Response Unit, and an ambulance showed up at their house and caught the burglars red-handed.

One of the Policemen said to Granddad: "I thought you said that you'd shot them!"

Granddad said, "I thought you said there was nobody available!"

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