

NEWSLETTER

Christmas Edition
- December 2010



Another Christmas has rolled around!

All the team here at Hunter Withers wishes you all a Merry Christmas and a Happy New Year!

Office Hours: - Christmas Period

**Closed from 1.00pm 23rd December 2010
Reopening 17th January 2011**



In this Newsletter.....

- ***Changes to the QC/LAQC Regime***
- ***Gift Duty***
- ***More GST Changes Ahead!***
- ***FBT – Motor Vehicles***
- ***Casual Agricultural Workers v Agricultural Contractors***

Changes to the QC / LAQC Regime

In the 2010 Budget the Government announced that changes will be made to the qualifying company ('QC') and loss attributing qualifying company ('LAQC') regimes. The draft legislation outlining these changes has been released, which effectively proposes to eliminate LAQC's, while retaining QC's, and introduces a new vehicle called a look-through company ('LTC').

Similar to a partnership, the shareholders in an LTC are treated as personally deriving the income, incurring the expenses and owning the underlying assets and liabilities of the LTC. When a shareholder disposes of shares in an LTC it is deemed to be a disposal of the underlying assets. For example, if a shareholder in an LTC disposes of shares in an LTC that holds depreciated assets, the shareholder may derive depreciation recovery income.

The look-through aspect applies for income tax purposes only - the company still retains its capacity as a separate legal entity for company law purposes, including limited liability status.

One of the benefits of the QC regime is the ability to distribute capital gains tax-free. By comparison an ordinary company can only distribute capital gains tax-free by liquidating the company. An LTC will provide this same benefit because dividends paid by an LTC will be ignored for tax purposes, as the income is taxed directly in the shareholder's hands when initially derived.

Changes to the QC / LAQC Regime continued...

To cater for situations in an LTC where the profits are generated through the disproportionate efforts of its shareholders, that extra effort can be recognised by a pre-tax payment to a "working owner", i.e. a salary or wage. A working owner is a shareholder who is employed by the LTC under a written contract, and who personally and actively performs the duties of their employment under that contract.

Similar to the existing QC regime, in order to be eligible to be an LTC a company must be a New Zealand tax resident and have 5 or fewer "look-through counted owners". Broadly, the definition of look-through owners includes both individuals and trusts, with individuals who are related to the second-degree of blood relationship being counted as a single owner, as are trustees in a trust.

Existing QC's and LAQC's may transition into the LTC regime by making an election within 6 months of the start of the income year commencing on or after 1 April 2011. If a QC or LAQC does not elect to enter into the new regime, a QC will continue unchanged, while an LAQC will effectively become a QC, i.e. losses will not be able to be attributed to shareholders. When exiting the LTC regime, shareholders are deemed to have sold and re-purchased the underlying assets of the company at market value. The deemed sale could result in a tax cost, such as depreciation recovery.

This change is a chance for shareholders in existing QC's and LAQC's to review their current structure, and look at what would work best for them. Electing the LTC regime is not the only option - a partnership, limited partnership, sole trader or regular company structure may be a better fit.

The legislation has not yet been passed into law, but once this happens, we will be advising our clients of the best option for their LAQC company.

Gift Duty

A new Bill was introduced to parliament recently and is currently awaiting its first reading. Among other things, the Bill will abolish Gift duty from the 1st October 2011.

A review highlighted that Gift duty offered minimal protection to creditors and did not raise revenue significantly enough to justify the compliance costs involved.

The effect of the change is that the Estate and Gift Duties Act 1968 will not apply to gifts of property made on or after 1 October 2011. The Act remains effective for Gifts before this date.



Currently the maximum you could gift annually without attracting Gift Duty was \$27,000 individually and \$54,000 for Couples. Gift Duty was established to prevent people avoid estate duty. Despite estate duty being revoked in 1992, gift duty was retained to help stop people giving away major assets in order to evade tax, avoid exposure to creditors and the rest home subsidy.

It will be interesting to see if the government bring in further rules in respect to these issues.



More GST Changes Ahead!

Recently the focus has been squarely on GST due to the increase from 12.5% to 15%. That focus is set to continue with the release in August 2010 of draft legislation to further change the GST Act with effect from 1 April 2011.

Change-in-use adjustments

A central principle of the current GST Act is the need for a good or service to be principally acquired for the purpose of making taxable supplies (e.g. sales) before GST can be wholly claimed up-front. If a good or service is not acquired for a wholly taxable purpose a change-of-use adjustment may be required. Depending on the situation, the change-of-use provisions can be complicated and expensive to administer. This will apply to cars, homestays and other assets used for business and private use.

It is proposed that the change-of-use provisions are re-written and the principal purpose test is repealed and replaced with a “use” doctrine such that when an asset is acquired for a mixed purpose, a one-off input tax deduction will be made based on its estimated use. This deduction is subject to adjustment at a later date if the actual use varies from the estimate.

Zero-rating of land transactions

Schemes designed to acquire GST refunds from IRD on the purchase of land where the vendor is unable to meet its GST output liability, have caused the Government to propose zero-rating transactions that include land. Zero-rating will apply to the taxable sale of land by a GST registered vendor to a GST registered purchaser who intends to use the land for the purpose of making taxable supplies. Where land is only a component of a transaction, i.e. the sale of land and buildings, the entire transaction will be zero-rated.

This means no more waiting around for large GST refunds on land purchases and purchasers do not have to temporarily fund the GST component of the purchase price. The vendors however will need to be more careful.

As the purchaser’s use of the land will determine whether zero-rating will apply, a vendor will be required to confirm the purchaser’s intentions, and that they are GST registered. If the vendor fails to meet its obligations to gather the required information, it may be liable to pay the applicable GST. If the vendor is unable to gather the required information because of the actions of the purchaser, the purchaser may be held liable for that GST. If an unregistered purchaser provides false information to

avoid paying GST and that is subsequently found out, the purchaser will be deemed to be registered and will be required to pay the applicable GST.

To clarify the boundaries as to what transactions will be zero-rated, a definition of “land” will be inserted into the proposed legislation. As currently drafted, the definition includes an option to acquire land, an estate or interest in land, and rights that give rise to an interest in land. Based on the definition as drafted the commercial leasing of land will be zero-rated. However, it is understood this application to commercial leases is currently being re-considered by Government and is unlikely to be included in the final form of the legislation.

Taking the zero-rating of land and the change-of-use adjustment changes together, if a registered person buys land for a mixed use, the transaction will qualify for zero-rating, however, the purchaser will be required to pay GST based on its estimated non-taxable use.



“Dwelling” definition clarified

The distinction between what is a “commercial dwelling” versus a “dwelling” is important for GST purposes as the supply of accommodation in the former is subject to GST, but supplying accommodation in the latter is not. The current definitions have been the source of uncertainty in the past as activities such as homestays, farmstays and serviced apartments have not fit neatly into either definition. In 2006 the IRD issued a draft interpretation statement that broadly concluded these types of activities would not qualify as the supply of accommodation in a commercial dwelling and therefore are not subject to GST.

The proposed changes will expand the commercial dwelling definition to specifically include homestays, farmstays and serviced apartments. Furthermore, the proposed changes will clarify the law by requiring a dwelling to be a person’s principal place of residence and be subject to their exclusive possession.

FBT – Motor Vehicles



If you or employees are using a Company owned vehicle, the chances are pretty high that the company should be paying FBT on that vehicle.

As a general rule, as long as you've a vehicle available for private usage the company should be paying FBT. FBT taxes are about 10% of the value of the cost of the vehicle payable per year.

However there are General exemptions for "Work Related Vehicles". A Work Related vehicle exemption covers circumstances where employees store the vehicles at home and the employer doesn't allow the vehicles to be available for private use. It must be a condition of that employee's employment to store the vehicle at home.

Not all vehicles are Work Related Vehicles for FBT purposes.

For a Work Related Vehicle exemption all of the following must be met:

1. **The principle design of the vehicle must not be for carrying passengers. (Vehicles that qualify are Utes, including extra and double cabs, light pick up trucks, taxis etc)**
2. **The Company name, logo etc must be prominently and permanently displayed on the exterior of the vehicle.**
3. **The employer must notify the employees in writing that the only private use the vehicle is available for is: Travel between home and work; and travel incidental to business travel.**
4. **The employer must complete at least quarterly record checks to ensure that the restriction is being followed.**

If you have recently purchased a vehicle in the company or are unsure whether the exemption is applicable to you, please phone to discuss.

Casual Agricultural Workers v Agricultural Contractors

What is the difference?

From the IRD's perspective there is a major difference and it pays to get the distinction right!

Casual Agricultural Workers are employees who do casual seasonal work on a day to day basis, or for no more than 3 months. They need to use the "CAE" tax code on the Tax Code Declaration (IR330) form.

Casual Agricultural Workers are taxed under the PAYE regime at a **flat rate of 19.54 cents** in the dollar.

Agricultural Contractors are independent Contractors, not employees and are subject to the Schedular Payment regime (formerly Withholding Payments). The current rate of deduction for Agricultural Contractors who have completed a Tax Code declaration is 15 cents in the dollar. The non declaration rate is 30 cents in the dollar.

The above also applies to all individuals, partnerships, trusts or company who work under contract or arrangement for the supply of labour on land in connection with fruit crops, orchards, vineyards and vegetables.

To remove yourself or entity from the Schedular payments regime a "**Certificate of Exemption**" must be applied for and approved by the Inland Revenue each year. Otherwise, in all instances, the Agricultural Contractor is subject to the Withholding Tax deductions rules.

The requirement to deduct withholding taxes is quite broad. It used to be that if you operated through a company structure that the company was exempted, but not any more, in respect to agricultural, horticultural or viticultural companies.

As a basic rule any employer of labour must deduct taxes from any wages or contracting type payments.