



# TAX EXPERTS LIMITED

CHARTERED ACCOUNTANTS AND BUSINESS ADVISORS

NEWSLETTER - NINTH EDITION

## Beware terms and conditions

### Special points of interest:

- Beware Terms & Conditions
- What Can I claim
- New rules for mileage rates
- How to reduce bad debts
- How much rent should I charge
- Undeclared Cash Jobs

MANY large suppliers seem to be using their terms and conditions in ingenious ways to take advantage of their customers.

It's been reported that Trust Power advertised unlimited broadband for \$49 a month. However, customers needed to sign up for a minimum of two years and in the small print it stated that the second 12 months was to be charged at \$79 a month. The Commerce Commission has filed charges under the Fair Trading Act.

Magazine publishers sometimes include a clause in their terms and conditions which says if you don't say you do not wish to renew your subscription, the company automatically renews it for a further year.

Be selective in choosing who you are going to allow to direct debit your bank account. If there is a dispute, you might find it hard to get your money back.

Unfortunately, none of us has enough time to read all the terms and conditions. About the best we can do is be aware they can be badly skewed against the customer.

## Go for the shortcuts

IT'S true – most of us only scratch the surface of what's possible when we use our computers.

Underlying all the usual stuff we do daily, are a multitude of smart tricks that can make life easier, improve productivity and ease the pain of OOS.

For the next few newsletters, we're going to give you a few I-Click shortcuts to help avoid the laborious use of the mouse and having to click several times. Do try these shortcuts and get in the habit of using them regularly. It'll save you time. These suggestions are for PCs only. Also, they may not work in older versions of Windows.

If you press the function key, **F9**, at the top of your keyboard, it will automatically magnify the document you are looking at. Press it again to return to normal size.

If you're looking for a keyword, you can find it by **holding down the control key and pressing F**. You then type in the word you are looking for. Each time you press "enter", the cursor will take you to the next place where this word appears in the document. Press the function key **F2** and you will find this is a shortcut for renaming a selected item.

## What can I claim?

A PENSIONER got remarried and decided to rent out her former home. It was one of a group of houses.

A tradesman made an offer to a group of house owners, including hers, to clean all their windows for \$100 each.

"I gave a neighbour \$100 to pass on to the tradesman, but since I didn't get a receipt I assume I can't claim it," she said.

Tax law does not say anything about the need for a receipt. Claiming expenditure is perfectly simple. Generally speaking you can claim any expense which relates directly to deriving income. That's the end of it.

If the IRD ever asks you to prove you spent the money, you need to be ready to do so. So it's always advisable to get some form of written acknowledgement, such as an invoice, to support your expenditure. It's a convenient way to provide proof to satisfy the IRD.

In our example, the house owner could probably get confirmation from the window cleaner or even from her neighbour, if needed. The trouble is they might not be around when the proof is requested.

Incidentally, if you are in business and are registered for GST then you do have to have a "Tax invoice" for any payment you make of \$50 or more, to claim the GST.

## New rules for mileage rates

A BILL is before Parliament which has a section dealing with tax deductions based on mileage.

The calculation at present is easy. The rate is 72c a kilometre and the maximum number of kilometres you can claim for is 5000. The self-employed, only, will be allowed to continue to use this basis for calculating their business mileage.

The new system proposed will be a two-tiered system. You'll have to use a logbook and keep it for three months once every three years. Those who have relatively high business mileage should take advantage of this change.

It's probably easiest to explain the system with an example. X travels 30,000km for both business and personal running in one year. His tier 1 calculation applies to the first 10,000km. Fifty-five percent of his running costs are for business. This means he can base his claim for tier 1 on 5500km. If the rate were 75c a kilometre his claim would be \$4125.

He's still got 20,000km of mileage left. Supposing the tier 2 rate is 25c per kilometre, his claim is based on 11,000km which entitles him to another \$2750. That makes a total claim of \$6875, which is much better than the maximum available under the old rules of \$3600.

The Government plans to bring in these new rules from 1 April 2017. The actual mileage rates are likely to be announced sometime after 31 March 2018.

This new system provides a more accurate way of calculating mileage, but it is going to add to the amount of record-keeping. You're going to need to tell us the total number of kilometres you travel in each year. Therefore, **please start now**. Make a diary note to record your **odometer** reading when you finish work on **31 March 2017**. Then make another diary note to do the same on 31 March 2018 and so on. If you change vehicles, you'll need to get your odometer reading before you trade in your old vehicle and then make a note of the reading on the new vehicle. We hope you've got a good memory for this.

## Don't grab all the money

IF you sell your business, which you run through a company, the money does not belong to you. It belongs to the company.

You can only take it out if you are entitled to do so. If there is money owing to you, according to the balance sheet of the company, then that money can be paid out. However, any more than this becomes a loan to you or may even be an illegal distribution.

A problem often arises when a business is sold. The seller gets paid for "goodwill". This is the value of the customers who have been built up over the years. It is a payment for the potential to get a higher income.

The sale of goodwill in excess of what was paid for it (if anything) is usually a capital gain. This capital belongs to the company.

You can get it out if your company happens to be a Look-through company or one of those old qualifying companies. Otherwise, it must stay there until the company is wound up. If you take the cash out prematurely it has to be treated as a loan from the company to you. There are tax consequences as a result. If you want the capital gain paid out to you, without tax consequences, you must first have a signed special resolution of shareholders resolving to wind up the company.

## Some contractors to choose their own tax

FROM 1 April 2017, the Government is proposing to allow contractors whose income is subject to withholding tax deductions, to choose their own tax rates.

Those who have typically been over-taxed might want to choose a lower rate. The minimum for New Zealand residents has been set at 10%. Others, who have a lot of year-end tax, might be more comfortable having higher deductions.

The maximum number of times you will be entitled to change your rate during the year is twice. After that, the payer will have to agree to your request to make the change.

If you haven't been complying with your tax obligations, you might not be allowed to choose your own tax rate.

## Choose your internet service

A COUPLE of months ago some horrendous stories were published in the daily papers about businesses unable to function because they could not get their internet connection repaired.

One firm in Auckland was without the internet for five weeks. One supplier said: "The average time to fix the fault has increased to more than 60 hours, with some customers waiting considerably longer."

Before selecting your internet service provider, check the firm out as best you can. The internet is a great resource for this purpose as are your friends, particularly on Facebook. If the service provider has a bad reputation, avoid it, even if the price is a bit lower.

If you've got a couple of minutes, try checking out your existing internet service provider. It could be time for a change.

Recently, Ken was approached by a power company with an offer for cheaper power and a free ultrafast broadband connection. He found communicating with the company was very difficult and it was almost impossible to talk to the supplier of the ultrafast broadband connection.

For this reason, he cancelled his arrangement. It later transpired that the broadband supplier was none other than the one who failed the Auckland business described above.

## Trustees need to minute their decisions

IF you have a family trust, be fussy about recording trustees' decisions.

One problem that arises is taking money out of the trust for your own use. This can be:

- a reduction of money owing to you
- a distribution of some of the trust income
- a payment out of the capital of the trust
- reimbursement for trust expenses paid by you
- a beneficiary loan

It's important to clarify these withdrawals. This is done by means of a trustee minute.

If there could be any doubt about the reason for a transaction, be sure to prepare a trustee minute and make sure all trustees sign it **before** it is actioned.

## Computer backups

HERE'S a checklist to help you keep your data safe.

Are you backing up your computer at least daily.

Are you sending data off-site to protect against fire?

How do you know you could retrieve information from your backup? Do you test your backups regularly?

Are the files you keep in your email system also being backed up?

## Get the flight right

BE careful when booking flights on line.

John and his wife were going from Wellington to Christchurch and had booked airfares there and back. It was late at night and John accidentally booked to go on 21 May and back on the 22<sup>nd</sup> instead of going on the 28<sup>th</sup> and back on the 29<sup>th</sup>.

The next day his wife discovered the error and he rang the airline. The extra cost of changing the flights was \$200.

Another way of getting it wrong for overseas flights is to have a different name on your ticket from that which is on your passport. This applies particularly to married women who might have a passport in one name but accidentally book their airfares in their new name. The cost of correcting this is another \$50.

## Contractors to labour hire firms

IF you contract to a firm hiring labour, from 1 April 2017, the withholding tax deducted from your income will be at the rate of 20%. This will mess up your provisional tax payments from 28 August 2017 and the next two payments. Even if you are trading as a company, you will still have withholding tax deductions from income. You will be allowed to choose your own rate so long as it's not less than 10% – see article on page 2 in this newsletter entitled "Some contractors to choose their own tax rate".

# Voluntary withholding agreements

SOME contractors don't have to have withholding tax deducted from their income. As a consequence, they have substantial provisional tax liabilities. Some people prefer to have some tax deducted as they go. It's proposed that from 1 April 2017 they will be entitled to require the payer to deduct withholding tax at a rate they choose, so long as it's at least 10%.

## Gift vouchers

If you are in retailing, do you increase your sales by offering gift vouchers?

Gift vouchers usually have an expiry date. Be generous with the time you allow for redeeming the voucher, or have no expiry date, as this could give you a competitive advantage.

Consumer NZ last year called on all retailers to have no expiry dates on vouchers as it said consumers were losing up to \$10 million a year. Countdown, Kathmandu and Noel Leeming responded positively and now have no expiry date.

It pays to keep a register of your gift vouchers so you know exactly which ones are outstanding.

Customers will often want to use only part of their voucher at any time. Have a system for carrying forward the unused portion of the gift.

The converse applies. If you want to buy some gift vouchers, negotiate the expiry date. Who is going to turn away a sale by limiting you to a niggardly six months?

## How to reduce bad debts

PREVENTION is better than cure when reducing the number of bad debts.

Avoid giving credit to a stranger, without undertaking a credit check.

If you have to give credit without doing a proper check, be sparing.

Giving credit can help you gain customer loyalty, but be careful.

There is no obligation to give credit to anyone. Try to make it a habit, if your type of business will permit, to assume you will be paid on the spot.

If it can't prevent bad debts then:

Jump on new customers who start to abuse your credit arrangement.

Make notes of **every** conversation you have with a debtor.

If you have to make follow up calls, quote back to the customer what he/she undertook to do.

Immediately after you have made a call, make a note in your diary of the day on which you will next call if the money has not been received and keep a record of what was said.

Discontinue giving credit to the chronically bad payers. The time you put into them will destroy your profitability. You could be doing better things with the same time.

What about the big customer who will not pay on time?

Small businesses often find their biggest customer is their worst payer. You feel you can't afford to be too demanding, in spite of the fact you're entitled to your money. What should you do?

The answer is not to have one major customer that dominates your business. You will **always** be vulnerable while you let this continue.

Set a maximum percentage of total sales from any customer and do your utmost to see this is not exceeded. If your big customer goes broke it could take your business with it.

## Write off bad debts

**With 31 March looming as the end of many businesses' financial year, there's always the prospect of paying too much tax, it doesn't need to be this way.**

One of the biggest issues is the importance of writing off bad debts. It seems almost every year we have a client for whom we prepare the annual financial statements, who has a large amount of money owing to them.

When we get the results for the year we find there is a big profit, which has been inflated by an excessive accounts receivable figure. Discussion reveals some of this money is never going to be collected.

Can we fix the problem?

No. The law will not permit us to write off bad debts back-dated to the previous year. The client has to pay the tax and wait until next year to get these bad debts written off.

In the end the result is the same but in the meantime our client has to pay his tax earlier than would have been necessary.

Look at the debts owing to you. Are there some you have been pursuing and who won't pay you? Have you taken every reasonable step to get paid?

If yes, you must physically write off the bad debt before balance date, if you want to reduce your accounts receivable and hence your profit and tax. It depends on the system you are using as to how you go about this. If it's a very basic system like keeping copies of the invoices you have sent out, just write on your copy the words "written off as a bad debt on..." and **insert the date. Do this now.** It is not something you want to overlook.

You should tell us the amount you have written off as Inland Revenue likes us to record this separately.

Can you continue to try to collect a bad debt? Definitely yes. If you're lucky enough to get some money it becomes part of your taxable income.

## Deducting tax from payments to a contractor

Generally, if someone working for you appears to be an employee, they probably are for tax purposes.

There are a whole lot of tests you can apply but if you supply the equipment, premises, agree on hours of work etc you have probably got an employee. Ideally, if the person is a contractor you should have a "contract for service" prepared by an employment law specialist that reflects the actual arrangements. It is important to get this right because if you get it wrong not only would you be liable for the PAYE and penalties etc you could have a claim for holiday pay and/or personal grievance!

Some clients also have problems determining whether they should deduct schedular tax. In this case the rule is simple. If the occupation is listed as being subject to schedular payments, you deduct tax. If it is not listed you don't deduct tax. You can find the list at this URL: <http://www.ird.govt.nz/payroll-employers/make-deductions/withholding-tax/emp-deductions-salaries-wt-activities.html>

If you are reading this and you are a contractor, don't forget if your income exceeds \$60,000 you have to register for GST. Inland Revenue is discovering lots of cases where this is being overlooked.

## Undeclared cash jobs

Recently, Inland Revenue wrote to us to remind us “undeclared cash in the construction sector remains a high priority for us”.

Failing to declare cash jobs is, of course, illegal.

One way Inland Revenue can discover the extent of cash income is to re-construct the taxpayer’s expenditure. Once they have a good idea of the extent of your expenditure, they can deduce your income. The system is surprisingly accurate. If they find a shortfall they then make their estimate of what the income ought to have been and you have to prove them wrong.

It should be obvious, anyone who has a cash business can be targeted by the Department. The simpler the business, the easier the target. Taxis and cafes would have to be sitting ducks. Tips must be included as taxable income.

Inland Revenue has asked us to remind our clients of the consequences of not declaring income. They say it “can include tax penalties, criminal convictions or their ability to contract for work – which could have a considerable impact on their business and personal circumstances. Let them [clients] know that IR is getting smarter at finding people who are not declaring all their income.”

## Get your debtors right at 31 March

**Clients use all sorts of systems for keeping a tally on the money owing to them. From a tax perspective, the figure at balance date needs to be accurate.**

Please note:

Assuming a 31 March balance date, all work done up to 31 March which is capable of being charged must be included as income. For income tax purposes holding some of your invoicing over until April does not necessarily mean you can ignore it. You don’t have to actually send out an invoice but you do have to add the amount into your accounts receivable figure for tax purposes. You won’t be taxed twice because once we have put in a figure for the amount owing to you, we then deduct it in the next year’s accounts. If work cannot be charged because it is not quite complete, it doesn’t get included in your accounts receivable.

Some businesses have work in progress, which is partly completed work. They must value this on the basis of the amount of material which has gone into jobs in progress and the value of the wages they have paid to do that work. Any other direct costs should also be included such as hire of equipment.

### **Cut off**

Don’t deduct money received in April, until you have finalised the total owing to you at the end of March.

### **Professional services**

Professionals, who have supplied partly completed work (not invoiced), do not need to include these services in their annual accounts unless there is a right to make progress claims.

# Beware the debt collector

Inland Revenue now has the power to disclose tax debts to debt collectors.

If the debt is more than 12 months old and greater than 30% of the taxpayer's gross income, the tax department can release the information.

These disclosures are going to be very dangerous. They will damage the credit rating of those who offend. If you are in this situation, be sure to make an **arrangement with the Inland Revenue to catch up and make sure you stick to it.**

Don't agree to anything you are not going to be able to sustain. Obviously, if you are in tax trouble, it might be wise to talk to us first.

## Nowhere to hide

Meanwhile, tax departments around the world are clubbing together to swap information about assets and incomes owned and derived by taxpayers in countries other than their home country. IRD calls this AEOI, an acronym for Automatic Exchange of Information. Soon there'll be nowhere to hide.

## Tax deductions on food and drink

Inland Revenue has informed us it considers the supply of all food and drink, whether in the course of entertainment or not, is tax deductible only to the extent of 50%. Thus, under this new interpretation, if you give your client a bottle of wine or a food hamper you can no longer treat this as a fully tax deductible cost. If you want a 100% deduction, think of something different such as a bunch of flowers or something else which cannot be consumed.

## Charities

Inland Revenue is concerned because some charities do more than just carry out their charitable works. They run businesses. The department has no trouble letting the charity off paying Fringe Benefit Tax when an employee gets a benefit such as a car. It is concerned when the employee is not actually working for the charity so much as working for a business run by the charity. In future, there is to be an apportionment between mileage used for the charity and mileage used for the business. The business arm is to pay FBT. This change to the law has not yet occurred.

## Body corporates

A lawyer's newsletter has drawn our attention to the personal liability of committee members of body corporates registered under the Unit Titles Act 2010. If you are asked to serve on one of these committees, we suggest you require the body corporate to take out insurance to cover your risk.

## Big changes to PAYE on the way

On 3 November 2016, Inland Revenue announced changes to PAYE effective from 1 April 2019.

Monthly schedules are to be abolished.

PAYE information is to be filed on a payday basis.

Dates for payment of PAYE are to remain the same with the option of paying on a payday basis.

All information is to be filed electronically unless total PAYE deductions are less than \$50,000.

Payroll subsidy is to cease from 1 April 2018.



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## Always check your ACC account

YOUR ACC account could easily be wrong. Always check it.

Typical areas where the wrong premium can be charged include:

Selecting the wrong industry for your type of work.

Levying ACC payments in excess of the maximum threshold. Currently, you should not be paying ACC on earnings of more than about \$120,000.

Sometimes, people receive a PAYE salary and then a non-taxed salary on top of this. These are the type of people who can be overcharged.

Some activities are what is known as passive. However, the income from them sometimes sneaks into ACC files and is treated like earnings.

Rental income from a partnership is an example. If it is recorded in the tax return as partnership income, it can get through to ACC and be levied by mistake.

We read in a recent publication by another accounting practice that 30% of clients in a sample were paying too much ACC.

## How much rent should I charge?

IT is always difficult to know, if you own a rental property, how much to charge. Go to [www.tenancy.govt.nz/rent-bond-and-bills/market-rent/](http://www.tenancy.govt.nz/rent-bond-and-bills/market-rent/) you will get some figures of average rents in various areas throughout the country.

We hope this helps.

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