

NEWSLETTER

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The Partners and Team at Urlich+Kippenberger wish our clients a Merry Christmas and a Happy New Year.

Urlich+Kippenberger will close on Tuesday 22 December and re-open on Monday 11 January 2010.

All information in this newsletter is to the best of the authors' knowledge true and accurate. No liability is assumed by the authors, or publishers, for any losses suffered by any person relying directly or indirectly upon this newsletter. It is recommended that clients should consult a senior representative of the firm before acting upon this information.

Due 15 January 2010 Provisional Tax and GST for October/November 2009

For those filing GST returns 2-monthly, or those not registered for GST, the next Provisional Tax payment date is 15 January 2010. The GST for Oct/November is also due.

If your circumstances indicate that you will be unable to pay the full amount by the due date please let us know. We may be able to make an arrangement with Inland Revenue for you.

Risk Assessments

What happens if.....?

Have you given consideration to those possible events that we do not like to think about? Do you have:

- a suitable range of business and life insurances?
- do you have loss of income cover?
- does your business have key person insurance?
- what will ACC provide if you have an accident – will it be enough?
- should you set up a Family Trust to protect your assets and your family?

If you would like to look further into what you need and what is available, please arrange an appointment to talk with Phillipa Urlich or Jeremy Kippenberger.

Mileage Rate for Business Use of Motor Vehicles

The IRD mileage rate used to calculate motor vehicle expenditure for both self-employed persons and employee reimbursements has increased to 70 cents/km. The previous mileage rates were 62 cents/km for the first 3,000km, then 19 cents for each kilometre thereafter. Even though the new rate was only published in May 2009, it is effective from the 2008/2009 income year, i.e. from 1 April 2008 for taxpayers with a March balance date.

The IRD mileage rate is based on information collected from a survey on the running costs of a range of vehicles with petrol and diesel engines of various sizes. It includes the cost of repairs and maintenance, fuel and other running costs. The IRD has said that changes to petrol prices only have a marginal effect on the overall mileage rate. The rate applies regardless of the size of the engine or whether the vehicle uses petrol or diesel.

Mileage rates are used by employers to calculate reimbursements for employees who use their own vehicle for a business purpose, and by self-employed people to calculate deductible motor vehicle expenditure when a vehicle is used for both business and private purposes.

There are three methods for a self-employed person to calculate the expenditure on a motor vehicle that is deductible for business use of the motor vehicle:

- actual records
- a detailed log book
- mileage rate

Self-employed people can use the mileage rate to calculate their deduction up to a maximum of 5,000km of work related travel each year. If their business travel exceeds 5,000kms then they must use one of the other two methods.

Where an employee incurs expenditure for the benefit of their employer, the expenditure can be



reimbursed to the employee without being subject to PAYE. The employer may base the reimbursement on a reasonable estimate. Employers can use the mileage rate to calculate a reasonable estimate of the cost of using a private vehicle. However, if

reimbursement of high mileage business travel occurs, the amount of the reimbursement may result in a monetary benefit being provided to the employee, on the basis that the reimbursement could be more than a reasonable estimate. If that is the case, the portion which represents a monetary benefit would be subject to PAYE. **Shareholder-employees are not subject to the 5,000km limit if they receive income that is subject to PAYE**, from a company in which they hold shares. However, care must be taken to ensure that the reimbursement is reasonable and to avoid a taxable monetary benefit arising.

Legal Expenditure: Capital v. Revenue

There is no specific provision which governs the deductibility of legal fees. The question of whether legal fees are deductible relies on the general deductibility provisions and limitations on deductibility. Broadly, the deductibility provisions require an expense to be incurred in running a business or deriving gross income and not be capital in nature. A general rule of thumb that is often followed is to determine the purpose for which legal fees were incurred and follow the treatment of that underlying purpose.

For example, if a person acquires a rental property and that rental property represents a

capital asset, the legal fees incurred to acquire the property will be capital in nature and non-deductible (although a portion may be depreciable).

A recent Taxation Review Authority ('TRA') case demonstrates how the distinction between capital and revenue can become very fine. The case involved a group of farmers who incurred legal expenses when they sued the dairy co-operative that they supplied, when it merged with another dairy co-operative.

Dairy farmers supply milk solids to dairy co-operatives in proportion to their shareholding in

the co-operative. Farmers who supplied to one of the co-ops ('co-op A') were dissatisfied with a clause in the merger agreement that stipulated that they would receive a lower payout for their milk solids compared to the farmers in the other co-operative ('co-op B') for a period of 4 years after the merger. The reduced payout by the merged co-op to the former shareholders of co-op A was to reflect the fact that co-op B had a higher share value and its suppliers had historically received higher payouts.



The farmers challenged the differential payment through the High Court and the Court of Appeal. The farmers did not succeed in either Court. The farmers claimed a deduction for the legal fees incurred, which the IRD disputed. The farmers argued that as they were attempting to recover a dairy payout that would have been assessable on receipt, the expense was incurred to derive income and therefore should be deductible. The IRD argued that the reduced payout was a cost incurred by the farmers to acquire shares in the merged co-operative. As the legal fees related to disputing the cost of a capital asset, the legal expenses incurred were non-deductible.

The TRA held that the legal expenses were capital in nature. The Judge noted that the farmers did not couch their submissions to the High Court and the Court of Appeal in terms of 'loss of profit' but rather, focussed on considerations of capital structure and capital cost, i.e. the difference between what they paid and what they received. The fact that the capital asset (the shares) were paid for by way of reduced income made no difference to the fact that the asset acquired was a capital asset. The legal action taken against the co-operative was not designed to increase income but to reduce the amount they paid for the shares.

This case highlights the uncertainty that surrounds the deductibility of legal expenses. Notwithstanding that the farmers lost their case at the TRA, the view adopted by the TRA was reasonable. Recognising that the deductibility of legal fees can be a complex issue, **legislation has recently been enacted, providing that where a taxpayer incurs legal fees of less than \$10,000, the legal fees will be deductible irrespective of whether they are capital in nature.**

Tax Working Group

Due to concerns about falling government revenue, an independent 'Tax Working Group' has been established to consider New Zealand's current tax system and identify the key issues that the Government should address in the medium-term. The issues being discussed have

been widely covered in the media in recent times. Rental losses is one issue being reviewed. Be wary of buying rental property, either through LAQC or personal ownership, in order to offset losses against personal income. This may not continue.

IRD told it can hold back GST refunds

Under the Goods and Services Tax Act, the IRD can request further information and hold up repayments, provided proper notice is given within 15 working days after receipt of the return. However, there is no time limit on any further requests for information or on payment of a refund.

This seems to indicate that, so long as notice is issued by IRD, they can carry on an investigation as long as they like if they think a refund is questionable. In a recent case the Court of Appeal has upheld the Department's position. We hope that this decision will be appealed by the taxpayer.

Snippets

FBT on Car Parks

The IRD has updated previously released Rulings on the application of FBT to car parks provided to employees by employers, to reflect

changes in legislation due to the enactment of the Income Tax Act 2007. The rulings have been issued in draft to enable public consultation.

This latest draft ruling reaches the same conclusions as the previous ruling. Car parks provided by an employer, or a company within the same group as the employer, will be exempt from FBT only if the park is on land owned or leased by the employer or group company. If the

car park is on land that is subject to a licence agreement, then FBT will apply. A licence agreement is normally created where a person is granted the right to use premises without becoming entitled to exclusive possession of the premises.

Tax Pooling Changes

"Tax pooling" is a mechanism that taxpayers can use to minimise their liability to "use of money interest" and in some cases eliminate late payment penalties charged by the IRD. By using a Tax Pooling intermediary a taxpayer who has paid insufficient tax to the IRD and is incurring interest and penalties, can "purchase" tax (and have it credited to their tax account) through a tax pooling intermediary, from other taxpayers who have overpaid their tax. Depending on the matching of underpayment and overpayment transaction dates, the IRD charges can either be eliminated or reduced. A cost is still incurred when tax credits are purchased, i.e., the tax pooling intermediary will charge interest on the tax purchased; however, that cost is less than what would have otherwise been payable to the IRD.



Since its introduction in 2003, there has been some confusion in relation to the tax purchases as the legislation was originally unclear and tax purchases were completed for other tax types, such as GST. After some time the IRD stopped allowing transfers to other taxes.

Legislation passed recently has expanded the use of tax pooling beyond income tax to other tax types. However, transfers to other tax types can only occur if requested within 60 days of an IRD reassessment (for example, due to an IRD audit), and only for the amount of the increased assessment. This means that if a taxpayer faces a reassessment of GST, RWT, PAYE or other tax types, they can utilise tax pooling. This should lower the cost of IRD audits and voluntary disclosures for taxpayers.

PAYE Tables for Employers

IRD will no longer be issuing a hard copy of the PAYE tax tables. Information will only be available online. If you are using a payroll computer programme this



information should be updated by your software provider. If not, you may wish to discuss this with our office so that you deduct tax etc at the correct rate.

If you have any questions about the newsletter items, please contact the team at Ulrich+Kippenberger