

The Low-down on the new contractor withholding tax rules and IRD rolls out new MyIRD for GST

Client Newsletter, July 2017

The low-down on the new contractor withholding tax rules

If you are a contractor, or engage the services of a contractor, are you up to speed with the changes to the withholding tax rules?

From 1 April 2017, contractors can elect their own withholding tax rate. This means they no longer have to have tax deducted from their payments in line with their flat rate under the withholding tax rules (otherwise known as the Schedular Payment rules).

Schedular payments apply to contractors across a broad spectrum of industries; from cleaners, farmworkers and gardeners, to entertainers, sportspeople, labour-only builders and fishing boat workers. The withholding rate can be equally as broad; from 33% for examiners' fees, to 10.5% for personal service rehabilitation payments.

With the new rules however, contractors can choose to elect a lower withholding tax rate, down to a minimum of 10% (15% for non-resident contractors). This is done by the contractor electing a rate on their Tax Rate Notification for Contractors form (IR330C) which they provide to parties they invoice. The idea being that the lower rate will more

accurately reflect the contractor's end of year marginal tax rate.

Non-resident Entertainers

The changes to the withholding tax rules do not however apply to non-resident entertainers who will continue to be subject to withholding tax at the flat rate of 20%, with no ability to reduce this rate.

Labour-Hire Firms

The withholding tax rules have also been extended to apply to contractors that work for 'labour-hire firms'. In addition, the current exemption that applies if a contractor is invoicing through a company does not apply to payments by labour-hire firms. In other words, labour-hire firms will have to deduct withholding tax from payments made to a contractor's company at the standard rate of 20%, unless the contractor elects a lower rate of no less than 10% or applies for a Special Tax Rate, which could be as low as of 0%.

A labour-hire firm has a wide definition and essentially includes "a person which has as one of its main activities the business of arranging for a person

to perform work or services directly for clients of the entity". Essentially, if the labour-hire arrangement is not incidental to the main business of the labour-hire firm, the withholding tax rules will apply.

There is however an exclusion from the new labour-hire rule for transactions with associated persons to prevent overreach of the rules.

The Inland Revenue has allowed for a lead-in time of up to 1 July 2017 for those labour-hire firms that were not able to get their payroll systems in place in time for 1 April 2017.

Special Tax Rate

Contractors subject to the withholding tax rules cannot apply for a Certificate of Exemption, instead they now have the ability to elect a 0% withholding tax rate, which means the contractors will pay their income tax through the provisional tax system. A good option for those contractors who are able to manage three sizeable tax payments throughout the year, with a wash-up in the annual tax return, but perhaps not such a good option for those contractors who will struggle to ensure they have the cash-flow to cover the payments when they fall due.

The election of a 0% withholding tax rate is done by completing an IRD Special Tax Code Application form (IR23BS) and submitting the form to the IRD.

The outcome of having a Special Tax Rate (rather than a Certificate of Exemption) means the payments to the contractor must be recorded on the payer's Employer Monthly Schedule, even though no

withholding tax is deducted. This is an added compliance hassle for payers, however from a tax base protection perspective, this ensures the contractor's income information is still provided to Inland Revenue and therefore reduces the risk of non-compliance.

Voluntary Withholding Agreements

A further change sees those contractors who are not currently subject to the withholding tax rules, able to elect into the rules if they so choose and have payers deduct withholding tax from payments made to them. In order to do this however, the payer has to agree. Therefore, if this was going to cause unnecessary compliance for the payer, the payer could choose not to withhold. The standard rate under a voluntary withholding agreement is 20%, unless the contractor elects a rate no lower than 10%.

Practicalities

The withholding tax changes will be positive for contractors in the long run. However, we foresee there will be a few teething issues to overcome, such as the interplay with the attribution rules; when a contractor's income must be returned in the contractor's individual tax return, yet the withholding tax has been withheld under the contractor's company IRD number.

We note the IRD is aware of this issue and are working on a solution which would potentially allow the company tax credits to be transferred to the individual. Likely there would be a retrospective change to fix the issue so that no one is

disadvantaged by the change to withholding where the attribution rule might apply.

Also, contractors who have been paying tax via the provisional tax system but will now have withholding tax deducted will, in the first year or two, need to consider estimating their provisional tax down which opens them up to IRD's use-of-money interest rules.

Over time, these and other practical issues will be ironed out; it just means in the short term closer attention will need to be paid to contractors and those who make payments to contractors.

IRD rolls out new MyIR for GST

The launch of the first major stage of Inland Revenue's business transformation programme went live in February 2017. This solely dealt with GST and involved the migration of:

- 8.5 million taxpayer records
- 800,000 GST accounts
- 8.1 million GST returns
- \$80 billion of GST payments history
- \$36 billion of disbursements history

Clearly this was a significant task and on a scale that would not often be seen in NZ.

At the user end, the migration appeared to go without a hitch as taxpayers and accountants were able to log on and immediately use the new GST MyIR system.

As it stands however, due to the progressive nature of the rollout onto the new IT systems, there are some inefficiencies now present that are largely caused through a very old and very new system not being

able to integrate. These issues are not ideal from a user's perspective but it seems cannot be avoided given the constraints the Inland Revenue are working with.

The Inland Revenue has acknowledged there are a number of issues that users have identified while using the new system in a real environment. These issues are being prioritised however some of these will not be resolved until Stage 2, when other taxes (i.e. income tax), also transfer onto the new IT platform.

Team News

After 3 years with Biz Solutions **Irene Halim** has decided to go on her big O.E. She has been an amazing member of the team in all aspects and we will miss her very much. We wish Irene all the best with her travels around the world.

Irene's duties will be assumed by **Rahul Singh** as practice manager. Rahul is a certified chartered accountant who joined us this month and have more than 6 years' experience as a BAS accountant.

We are also please to appoint **Ellina Yoo** as an intermediate accountant who has recently joined our expanding team.

Welcome to the team Rahul and Ellina.

We fare welled **Linda Sahiti** as Office Manager in May. She was a great asset to the team and kept us all in check with administration and office outlook. **Francia Tolson** has taken over from Linda as the new Office Manager.