2020 YEAR END - TAX PLANNING CHECKLIST

FOR YEAR ENDING 31 MARCH 2020

Below is a checklist of matters relevant to all business entities which you should consider, some of which may help you reduce the amount of tax you have to pay for 2020 year.

1. Provisional tax elections and Use of Money Interest

If provisional tax has been paid on the basis that you will be a provisional taxpayer for the 2020 year, but it subsequently transpires that this is not the case (because residual tax is below $2,500), an election to be a provisional tax payer for the year is required in order to receive use of money interest on provisional tax overpaid. With Covid-19 situation, Provisional Tax payment threshold has been permanently changed to above $5,000 from the existing $2,500 effective from 2021 financial year.

2. Bad debts

In order to claim a tax deduction for trade related bad debts, the debt must be physically written off in the accounting records before balance date. If a debt is 'bad' there must be no reasonable expectation of recovery. However this does not mean taxpayers can no longer pursue recovery of that debt. You will need to let us know if you and the debtor are associated.

3. Donations

Companies are entitled to a deduction for donations made to approved donee/charitable organisations only limited by the amount of company's net income for the year.

4. Fixed assets and Depreciation

You should do a "stock take" of fixed assets at year end to determine whether the fixed assets listed on the depreciation schedule actually exist. Where assets are no longer being used application can be made to IRD to write off the book value in that year.

Depreciation rates should be checked to ensure they are in agreement with the updated prescribed rates. A check should also be made to ensure that the charge has been calculated including a full month's depreciation for any part of the month the asset is owned and used. No depreciation is claimable in the year the asset (other than buildings) is disposed of.
Please provide details of all assets purchased and/or disposed during the year as noted in the enclosed questionnaire to allow us to work out the depreciation etc.

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5. Prepaid expenditure

The Income Tax Act applies the principles of accrual accounting to the unexpired portion of deductible expenditure at the end of an income year. The effect is to defer the deduction of any unexpired amounts to the following income year.

Some expenses can be prepaid regardless of the amount or period being prepaid, for example:

- Stationery,
- Subscriptions for papers or journals,
- Vehicle registration and road user charges,
- Postage and courier charges,
- Rates,
- Audit and Accounting fees,

Other expenses can be paid in advance only up to a certain limit, for example:

	Max Amount $	Max No of Months
Rent (if prepayment more than one month)	26,000	6
Rent (if prepayment less than one month)	Any amount	1
Rent or bailment of livestock	26,000	6
Consumables	58,000	N/A
Insurance (where each premium is no more than $12,000)	N/A	12
Professional or Trade Association subscriptions (where each subscription is no more than $6,000)	N/A	12
Accommodation or travel	14,000	6
Advertising	14,000	6
Other periodic charges	14,000	12
Other services	14,000	6

The legislation regarding allowable prepayments is complex and we recommend clients discuss with us

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any plans for prepaying expenses prior to committing to any expense.

Prepaid expenditure on items other than those covered above is only tax deductible to the extent the services have been performed or goods provided. Therefore a payment for repairs made before balance date will generally not be tax deductible unless the repairs have actually been carried out.

6. Repairs & Maintenance

Generally no deductions are allowed for a repairs and maintenance reserve. It may be worthwhile undertaking repairs and maintenance prior to 31 March 2020 to obtain a full deduction. Deciding on the nature of the expenses (revenue or capital) is often a difficult decision. Please contact us if you require any assistance in this area. With Covid-19, any asset purchases below $5,000 can be written off in the same financial year, there is no requirement to depreciate this asset (this is from 2021 financial year).

7. Trading Stock

The closing stock value affects the profit or loss of the business. Higher closing stock values result in higher profits whereas lower closing stock value results in lower profits, thus affecting the taxation figure as well. The closing stock value must be true and fair as per IRD's requirements.

Allowable stock on hand valuation methods alter depending on the size of your business:
- For businesses with turnover of less than $1.3m, you can value closing stock the same as opening stock if closing stock can reasonably be estimated at less than $10,000;
- For businesses with turnover of less than $3.0m, you can use market value (even if greater than cost).

8. Shareholding Continuity

Any change in shareholding during the financial year has implications on one or more areas for taxation purposes. These include Imputation credit accounts, losses to carry forward, Qualifying company/Look Through Company status, loss attributions, shareholder salaries, etc.

Shareholding continuity must be maintained in relation to the carry forward and grouping of losses. 49% continuity must be maintained in the loss company from the time the loss is incurred until the time the loss is utilised. For grouping, commonality of 66% is required. That is, the same group of persons must own 66% in both companies at all times during the continuity period.

To rely on the wholly owned group exemptions, 100% common shareholding must be maintained throughout the year.

In order to retain the company ICA balance, 66% shareholding continuity must be maintained throughout the year.

Please consult with one of our accountants first if you intend to and/or are expecting any change in

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shareholding in the company.

9. Subvention payments & loss offsets

You should ensure that any prior year group loss offsets and subvention payments are completed and lodged with the IRD prior to year end. Loss offsets and subvention payments relating to the year ending 31 March 2020 are due on or before 31 March 2021.

10. Qualifying Companies (QC)

For existing QC clients, you need to consider whether it is still appropriate to remain in the regime for various reasons. If you wish to revoke the status by intent you have till end of the year (i.e. by 31 March 2020) to revoke election for that year. It is also important to check number of events (i.e. change in shareholding, change in trustees of trust, dividends paid to trust shareholder not passed out to beneficiaries etc.) to ensure there are no deemed revocation.

11. Look Through Companies (LTC)

If you wish to elect the company to be LTC, you need to elect by 31 March 2020 to become effective from 01 April 2020. Any new companies (including shelf companies if non-active declaration filed) have exceptions whereby they have until the first tax return due date to be filed to make the election. There are various reasons as to why you would want to elect company to be LTC (i.e. if you are planning on restructuring company assets for asset protection purposes etc.). However there are other factors to consider as well such as LTC entry cost arising from not having enough imputation credits for retained earnings and existing associated person gains.

Also note that you can no longer offset rental losses against any other source of income due to ring fencing rule to claim any tax back from IRD. This change is effective from 2020 year.

12. Transitional Resident Exemption

This rule applies to individuals who are becoming new residents or residents returning to NZ after 10 years absence from 01 April 2006 for those arriving on/after that date. It allows exemption on all foreign sourced income from tax other than employment and services income derived while NZ resident for 48 month period. There are times when you are better off to elect out of this exemption (i.e. if offshore losses exist with NZ income) so it is prudent to discuss this with us should you fall under this exemption.

13. Company advances

If you have a company and the company has advanced the funds that result in an overdrawn shareholder current account, loan to associated entities (where not 100% commonly owned),

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associated trust, staff, shareholder-employee/associated person, shareholder then it may trigger tax implications. There are ways to deal with any potential tax implications (salary, dividend or restructuring debt) which can be discussed.

14. Imputation Credit Account (ICA)

Please check your imputation credit balance to ensure that it is either a nil or credit balance at year end. If the ICA is in debit balance this will create a 10% imputation penalty which is not treated as a "tax payment" for income tax purposes.

15. Dividend Resident Withholding Tax (DWT)

If dividends declared and /or paid during the year have been imputed at 28% the DWT return and a payment of 5% will need to be filed and paid to IRD by 20th April 2020. Therefore please advise us if the dividend has been declared and imputed at 28% and forward us dividend statement in order to fully impute the dividends.

16. Accruals

Make a list of all expenses that you owe at balance date i.e. 31 March 2020. These can be claimed as a deduction in the 31 March 2020 income tax return.

17. Home office expense

If you have an office in your home, you may be able to claim a portion of all expenses that relate to all your home expenses. The details of expenses that may be claimed are noted in the enclosed questionnaire. Home office expenses can only be claimed in proportion of the area specifically and exclusively used for business purpose over the total area of house.

During the 2018 tax year IRD introduced an alternative method for calculating home office called the square meter rate option and is calculated based on a rate set by the Inland Revenue Department.

18. Legal Expenses

For the 2010 income year and beyond, legal expenses incurred when buying capital assets used to derive taxable income are tax deductible, provided total legal expenses for an income year are equal to or less than $10,000.

19. Business expenses paid personally

All business expenses which have been paid personally and did not go through the business books or

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bank account can still be claimed as a business expense for taxation purposes. Please provide lists of such expenses.

20. Fringe benefit tax (FBT)

If certain benefits (e.g. motor vehicle) are enjoyed or received by employees as a result of their employment the benefits are liable for FBT. Employers pay tax on benefits provided to employees or shareholder-employees. For motor vehicles however we have new vehicle ownership structure mechanisms available to minimise this FBT exposure. Please contact us for further information on this matter.

Close companies can elect to calculate the deduction for the business use proportion of vehicle expenses as an alternative to FBT. The requirements to use this option are:

1. Employer is a close company
2. Only fringe benefits provided to all employees are 1 or 2 vehicles to shareholder employees
3. Vehicle is acquired or first used for business use on or after 1 April 2017
4. Company give notice to IRD of election by the income tax return due date for the relevant income tax year

21. Land Sales – Zero-rating transactions

The GST registered vendor is to charge GST at the rate of 0% on any supply that involves land or in which land is a component to a registered person who acquires the goods with the intention of using them for making taxable supplies.

22. Working for Family Tax Credits income changes

The definition of family income for Working for Families Tax Credits has been amended. From 1st April 2011 people receiving Working for Families Tax Credits are no longer be able to use investment losses, such as from rental properties, to reduce their family income.

The definition will also include additional income types that could determine your family tax credit eligibility criteria as below:

1. Attributable trustee income - including income of a company controlled by the trust - if you're a settlor of a trust
2. Attributable fringe benefits - when 50% voting is held by shareholder employees or their associates

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3. PIE income - excluding superannuation funds or a retirement savings scheme
4. Passive income of children - includes interest, dividends and rent. Amounts over $500 a year (per child) are included as family income
5. Income of non - resident spouse - worldwide income
6. Tax exempt salary or wages - under specific international agreements in New Zealand (e.g., United Nations)
7. Main income equalisation scheme deposits - made by you, your trust or a company controlled by you or your trust
8. Certain pensions and annuities - includes 50% of payments from life insurance policies or a superannuation fund (excluding NZ Super)
9. Other payments - received from any person or entity and used for the family's day-to-day living expenses. This is only included if the total amount exceeds $5,000 per family
10. Closely held company profits

Hence if you are receiving weekly or fortnightly Working for Families Tax Credits payments, you need to ensure to check those income types and know what you are receiving is the correct amount. If you are receiving Working for Families Tax Credits as a lump sum at the end of the year, we need to know about these types of income before the end of year assessment is completed (year ending 31 March 2018).

23. Shareholder Salaries (Penny Hooper case)

Penny and Hooper Supreme Court decision was released on 24 August 2011. The case considered whether surgeons Penny and Hooper had each entered into a tax avoidance arrangement by restructuring their orthopedic practices to operate as companies (owned by their family trusts) and work as employees of those companies for significantly reduced salaries. The Court found the mischief was in "fixing an artificially low salary".

The Court held that by fixing their salaries and still making use of company profits paid to their family trusts Penny and Hooper entered into a tax avoidance arrangement that altered the incidence of tax. The documentation of salaries and any divergence from a 'commercially realistic salary" is therefore important for those operating through a similar structure to Penny and Hopper.

Subsequent to the Supreme Court's decision, Inland Revenue issued a Revenue Alert RA 11/02 in an attempt to clarify the Commissioner's view on the diversion of personal services income.

The alert states that Inland Revenue is more likely to examine any arrangement where the individual service provider (who is generally the real owner and controller of the business) is not receiving a significant portion of profits derived from the business. The alert also states that the approach is not on market value or comparable industry averages, but rather on the commercial reality of the remuneration paid to the service provider. In adopting this approach, Inland Revenue will consider more than merely the presence of a market salary.

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Please contact us if you require further clarification.

24. Bright Line Test - Property

The legislative measures enacted in this first stage are as follows:

1. The following pieces of information are to be supplied to Land Information New Zealand (LINZ) by any person transferring any property as part of the usual land transfer process:

- Their NZ IRD number; *and*
- Their tax identification number from their home country *if* they are currently [also] tax resident overseas.

2. To ensure that NZ's full anti-money laundering rules apply to non-residents, before buy a property in NZ, offshore persons must have a NZ bank account number before they can get a NZ IRD number.

An offshore person is defined as anyone other than a person who is not an offshore person. A person is *not* an offshore person if:

- They are a NZ citizen and have been in NZ within the last 3 years; or
- They hold a NZ residency class visa and have been in NZ within the past 12 months.

All other individuals will be offshore persons.

A non-individual will be an offshore person if it is:

1. Incorporated outside NZ; or

2. 25% or more owned (legal or beneficial) or controlled by an offshore person.

There is an exemption from supplying the information to LINZ if the property being transferred is the person's main home. This exemption however is *not* available to an offshore person, where the property is to be or was owned by a trust, or if the person is selling their main home for the third time in a two-year period.

For the *main home* exemption to apply to a transferee, the land must be intended to be used predominantly for a dwelling that will be the transferee's main home. For the *main home* exemption to apply to a transferor the land must have been used predominantly, for most of the time the transferor owned the land, as a dwelling that was the transferor's main home. The 'most of the time' requirement is a 50% or greater test. The 'predominantly' requirement is for evaluating the main use of the purchase

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of the property or land. For example, purchase of an industrial building with an adjoining apartment to be used as a main home does not meet the requirement that the land will be used predominantly as the transferee's main home. Therefore the no-notification exemption will not be met.

The second stage introduced a new easy to enforce, objective bright-line test to tax gains from the disposal of residential land acquired and disposed of within two years of acquisition, subject to some exceptions. The rules apply from 1 October 2015. The period that applies has been increased to within 5 years of acquisition; this is started from 1 April 2018.

The start and end dates are specifically defined and may differ depending on the nature of the transaction. The following tables give a summary of the start and end dates for purposes of the bright-line test;

Type of acquisition	**Start date of bright-line test**
Standard purchase of land	Registration under LTA1952
Sales without registration of title	Latest date property acquired (ordinary rules)
Sales "off the plan"	Date of entry into a contract to purchase
Subdivided land	The original date of registration for the undivided land
Converting a lease with a perpetual right of renewal into freehold title	Date the lease with a perpetual right of renewal is acquired
Type of disposal	**End Date of bright line test**
Standard purchase of land	Date of entry into agreement for sale
Gift	Date of gift (generally registration of title)
Compulsory acquisition	Date of compulsory acquisition
Mortgagee sale	Date land disposed of by mortgagee
Other disposals where no contract to sell	Date of disposal according to ordinary rules

Only residential land is caught by the new bright-line test. Residential land is land that either has a dwelling on it, the seller of the land is a party to an arrangement that relates to erecting a dwelling on it, or is bare land that is zoned for residential purposes. However, if the land is used predominantly as business premises or is farmland then the land is *not* residential land.
The bright-line test also has a *main home* exemption whereby a sale of a main home within two years of purchase will not be subject to tax. However, to qualify the land must have *actually* been used

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predominantly, for most of the time the person owns the land, for a dwelling that was the main home of the person or a beneficiary of a trust that owns the property.

A person can only have one main home at a time (some overlap may be permitted in certain situations such as a pending sale of a prior main home when a person has already moved into a new main home) and habitual sellers cannot use the main home exemption. A person is a habitual seller if they have either used the main home exemption twice in the previous two years or have engaged in a regular pattern of buying and selling of residential land.

There is a limitation for trusts selling residential land that want to use the main home exemption. For tax purposes, a settlor of a trust is anyone who has transferred value to the trust for an inadequate consideration. A trust cannot use the main home exemption when a principal settlor of the trust has another main home. This rule is to ensure that people cannot use the main home exemption multiple times through the use of a trust. A principal settlor is the person who has made the greatest transfer of value to the trust. However, if the person providing the most value to the trust has made the provision with no strings attached and is not a beneficiary, trustee, appointor, a person with a contingent interest in the trust property or a decision maker under the trust, then their settlements are disregarded.

Other exemptions from the bright-line test are:

1. Inherited properties - Transfers from the deceased to the estate and from the estate to beneficiaries are deemed to be at cost (no gains arise) and the on-disposal within two years of receipt by the beneficiaries of the inherited property is exempted.

2. Relationship properties – transfers between the parties pursuant to a relationship property agreement are deemed to be at cost and therefore no gain arises. However the on-disposal of the transferred property within two years by the recipient party will be subject to the bright-line test.

3. Resident's restricted amalgamation – the existing rollover relief, where a transfer of property as a result of an amalgamation (held on revenue account by virtue of application of sections CB 9 to 11 and CB 14) is treated as transferred at cost, is extended to include property that is revenue account property of the amalgamating company due to the application of the bright-line test.

Other key aspects of the bright-line test are that:

1. The cost of the property is tax deductible, including expenditure related to the acquisition and cost of capital improvements made after acquisition. Other holding costs may be tax deductible if sufficient nexus exists with income. Interest costs may be automatically deductible if the property is owned by a company.

2. Losses from deductions claimable solely against bright-line income are ring-fenced so they can only be offset against gains on other land sales that are taxable under any of the land sale provisions.

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3. Specific anti-avoidance provisions have been included to defeat the use of land-rich companies and trusts to circumvent the intent and purpose of the bright-line tests, such as disposal of 50% or more of shares in the company that owns residential land, which will be subject to the anti-avoidance provisions.

Offshore property speculators now pay a withholding tax on profits from sales of residential land under the bright-line test which is the lower of:

- 33% of the vendor’s gain on the that property and
- 10% of the total purchase price of that property.

This withholding tax is known as the Residential Land Withholding Tax (“RLWT”).

25. Director requirements from the Companies Office

Effective from 1 May 2015, all New Zealand incorporated companies are required to have at least one director who:

- Is resident in New Zealand, or
- Lives in an enforcement country and is a director of a company registered in that enforcement country.

As noted above, this criteria is an “or” therefore having a New Zealand resident director is not critical provided a director satisfies the alternative criteria. At present only Australia qualifies as an enforcement country.

There may be an option for companies to appoint an ‘alternate director’ who is resident in New Zealand to help satisfy the new requirements.

If a company is found to be in breach of the new resident company requirements, this could result in the company being removed from the register.

In addition to providing the residential address details of each director, companies will also be required to provide the Companies Office with details of the director’s date and place of birth at the time of registration. These details will not be made publically available. Existing companies will be required to provide this information in relation to any changes to directorships or alternate directorships from 1 May 2015.

The board of directors will also be required to advise the Registrar of the name of any ultimate holding company, the country of its registration, the registration number or code (as applicable) and its registered office. This information will need to be provided on registration or within 20 working days of

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any change. These details will be made publically available. Existing companies will need to provide the Registrar with this information in the next annual return that is filed after 1 May 2015.
A further amendment to the Companies Act provides the Registrar with enhanced powers to de-register companies. The Registrar may de-register a company, if there are reasonable grounds to believe that:

- the company is not carrying on business;
- there is no proper reason for the company to continue in existence;
- the company has failed to respond to a request from the Registrar for certain information;
- one or more of the directors or shareholders has intentionally provided the Registrar with inaccurate information; or
- the company, or one or more of the directors, or shareholders has failed, in a persistent or serious way, to comply with the duties relating to the company under the Act or the Financial Reporting Act 1993 ("FRA").

26. IRD's new financial reporting requirements for companies

For income years starting on 1 April 2014 and later companies (including look-through companies) with:

- annual revenue of $30 million or less, and
- assets of $60 million or less

must prepare financial accounts that meet IRD's minimum financial reporting requirements. These thresholds apply to all companies in a group where the parent company is incorporated in New Zealand.

For subsidiaries of multi-national companies the levels are:

- annual revenue of $10 million or less, and
- assets of $20 million or less.

The following companies are required to prepare financial statements to a higher standard of accounting:

- Large companies with income of more than $30 million or assets of more than $60 million.
- New Zealand subsidiaries of multi-nationals with income of more than $10 million or assets of more than $20 million.
- Issuers.
- Companies with ten or more shareholders (unless they opt out).
- Companies with fewer than ten shareholders who opt in.

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These companies must prepare general purpose financial reports using the standards mandated by the External Reporting Board (XRB). Separate financial accounts do not need to be prepared for IRD purposes.

Small company exemption

Small companies are not required to prepare financial accounts if during the income year they:

- are not part of a group of companies, and
- haven't derived income in excess of $30,000, and
- haven't incurred expenditure in excess of $30,000.

Tax records must be kept to calculate taxable income, expenses, and GST (if you're registered). If a small company is also an employer records for employment-related taxes will also need to be kept.

Non-active company exemption

Non-active companies are not required to prepare financial reports.

Minimum financial reporting requirements

The financial statements must consist of:

- a balance sheet setting out the assets, liabilities, and net assets of the company as at the end of the income year.
- a profit and loss statement showing income derived, and expenditure incurred, by the company during the income year.
- a statement of accounting policies setting out:
    - the policies and assumptions that have been applied or changed, and
    - a description of the effect of any material changes in accounting policies used since the previous income year.

The statements must comply with the following accounting principles:

- double-entry method of recording transactions, and
- accrual accounting.

The financial statements may disclose amounts using the following valuation principles:

- tax values, when they are consistent with double-entry and accrual accounting

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- historical cost, when tax values are not consistent with the accounting principles used or when historical cost provides a better basis of valuation, or
- market value, when they provide a better basis of valuation than tax values and historical cost.

The financial reports must show:

- comparable figures for the previous income year.
- whether they have been prepared on a GST inclusive or exclusive basis.
- reconciliation of the company's financial statements and taxable income for the income year.
- taxation-based schedule of fixed assets and depreciable property.
- reconciliation of movements in shareholders' equity for the income year.
- all amounts from the *Financial statements summary (IR10)* form relevant to the company.
- sufficient notes to support amounts required to be disclosed as an exceptional item on the IR10.

The following amounts must be grossed up:

- interest and dividends received - grossed up for resident withholding tax.
- dividends received - grossed up for imputation credits to the extent the dividend is taxable and the credits are available to satisfy the company's income tax liability for that income year.

Certain types of business must provide additional industry-specific information:

- Foresters must show information about the cost of timber as at the end of the income year and a reconciliation of movements.
- Owners of specified livestock must show details of livestock valuation methods, valuations, and calculations for tax purposes.

FURTHER APPLICABLE CHANGES/ DEVELOPMENTS for 2020/2021

With the new tax year fast approaching we cover off some of the major changes that come into effect on 2020/2021 financial year, mainly focusing on stimulus tax package introduced in light of COVID-19 outbreak. These changes are as follows:

- Building depreciation of 2% reintroduced for commercial buildings from 01 April 2020
- Low value asset automatic deduction threshold has increased from $500 to $5,000 for 2021 income year, and permanently reducing down to $1,000 from 2022 income year onwards
- Provisional tax threshold to increase from $2,500 to $5,000; and
- Ability for taxpayers who has affected by COVID-19 to seek remission of Use of Money Interest and late payment penalties for payment due on or after 14 February 2020.

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These are all developing stories as of date of this letter and there may be further tax relief provided by IRD depending on the status of COVID-19 damage, hence we will keep you posted on this news by our e-newsletters as it becomes available.

If you wish to discuss any issues or queries regarding these new changes discussed, please feel free to contact your accountant for assistance.

Regards

TEAM at BIZ SOLUTIONS

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