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CHARTERED ACCOUNTANTS

What a difference a year makes. The 2010 Budget was announced on 20 May 2010, bringing in far-reaching changes. Outlined below are the more topical changes.

Personal Tax Cuts

The Budget delivered reductions to all personal tax rates, effective from 1 October 2010, with the main surprise being the reduction of the 33% rate to 30%. The reduction to the rates means that someone earning $45,000 p.a. would receive an additional $26 in the pocket each week, while someone earning $70,000 stands to gain $41 a week. These increases do not take into account the effect of the GST increase.

The top personal tax rate was reduced from 38% to 33% to align with the trustee tax rate. This has effectively removed the tax savings that could be achieved for income earned above $70,000 p.a. by having a trust instead of an individual deriving the income. With the tax changes it may be timely to review structures that are in place. The benefits of a trust, such as asset protection and estate planning, still remain and need consideration.

Working For Families Changes

The Budget has made a number of changes to the qualification criteria for Working For Families ('WFF') assistance. The automatic increasing of the Family Tax Credit abatement threshold (to compensate for inflation) has been removed. The abatement threshold will remain at $36,827 unless the Government makes a change to the threshold. One effect of this change is that over time fewer families will qualify for WFF assistance as families' incomes exceed the qualification threshold.
The Government has proposed that from 1 April 2011, investment losses will not be taken into account when determining a family's income for WFF purposes. This will prevent a person from using losses, for example from a rental property, to increase their WFF entitlement. It is also likely that from 1 April 2011 all distributions from trusts will be taken into account, as well as PIE income and the value of fringe benefits received from employment. This will further reduce the amount of entitlement families are eligible to receive.

Loss Attributing Qualifying Companies (LAQCs) & Qualifying Companies (QCs)

The Budget outlined intended changes to both LAQCs and QCs, which will result in them being treated similarly to partnerships. These changes are planned to be effective from 1 April 2011.

Any profit or loss derived by the LAQC/QC will flow through to the shareholders in proportion to their shareholding. The shareholders will then be taxed on the income attributed to them at their marginal tax rates. QCs will be required to file an IR7 partnership tax return instead of an IR4 company tax return.

On transition from an 'old' LAQC/QC to a 'new' QC, the imputation credit balance of the 'old' LAQC/QC will be extinguished. The payment of a dividend to utilise the imputation credits before they are extinguished should be considered keeping in mind how much cash is available in the LAQC/QC. A taxable bonus issue could be considered if cash is a problem.

Any losses currently held in a QC will be 'ring-fenced' from the date the new rules take effect and will only be able to be used to off-set future profits the QC derives. This is not an issue for LAQCs as losses are always attributed to shareholders on an annual basis. Loss limitation rules will apply to limit the losses attributed to a shareholder to the extent of their investment in the 'new' QC.
Once the new rules take effect, any sale of shares in a QC will be a deemed disposition of the underlying property held by the QC. This creates potential tax consequences, such as depreciation recovery for the vendor, as well as having assets at different values for different shareholders.

If an LAQC/QC is expecting to make profits in the future it may be worthwhile exiting the QC regime to prevent the profits flowing directly to the shareholders. It would also be advisable to exit the regime before 1 April 2011 (the likely date of change) otherwise there could be a deemed disposal of the QC's underlying assets if the exit is on 1 April 2011 or later.

Company Tax Rate Change

The company tax rate will drop from 30% to 28% at the start of a company's 2011/2012 income tax year. This could be as early as October 2010 for companies with early balance dates.

The change in the corporate tax rate means the standard uplift rates for provisional tax are on the back-burner once again. If you are basing 2011/2012 provisional tax on last year's tax return there is no uplift (i.e. use 100% of past year's RIT).

If you are basing 2011/2012 provisional tax on your 2009/2010 tax return then use an uplift of 105%.

There will be a two year transitional period during which dividends can be imputed at 30%. Companies will need to track tax paid at 30% and tax paid at 28% to ensure correct imputation of dividends at 30%. Imputing a dividend at 30% when there are insufficient 30% imputation credits will result in an imputation credit penalty being imposed at the end of the transitional period. Resident Witholding Tax (RWT) on dividends paid remains unchanged at 33%. A 'top-up' of RWT to 33% will still be required. For a dividend imputed at 28%, this will mean an additional RWT cost of 5% on the gross dividend.

Depreciation

Depreciation deductions on buildings with an estimated useful life of 50 years or more will be removed from the 2011/2012 income year. The depreciation rate on these buildings will be reduced to 0%.

Other buildings (with a useful life of less than 50 years) will still be able to be depreciated if they have an IRD prescribed depreciation rate e.g. dairy sheds and hot-houses.

Even though many buildings can no longer be depreciated, depreciation recovery will still apply for those buildings when they are sold for greater than their book values. Any asset purchased from 21 May 2010 onwards is not entitled to the 20% depreciation loading. However, if a contract to purchase the asset was entered into prior to 21 May 2010 then that asset can still be depreciated with the loading.

Any asset being depreciated at a rate with loading before 21 May 2010 can continue to be depreciated at that rate for that asset's lifetime. However, if there is a capital improvement to the asset, that improvement will need to be depreciated separately from the original asset without the loading.

GST

The increase in GST from 12.5% to 15% requires a range of systems changes and checks. Whether GST on a sale should be at the old or new rate will depend on whether the time of supply is before, or from 1 October 2010. If you are on the invoice basis, the time of supply is triggered by the earlier of receiving a payment or issuing a tax invoice. This means the old rate can be locked in for a customer purchasing goods to be received after 1 October 2010 by the customer paying a deposit before 1 October 2010.

For those on the payments basis, debtors and creditors existing at the time of the change are subject to a notional 2.5% conversion at their values on the date of transition, with all payments or receipts thereafter being subject to 15%. The notional conversion has the effect of deeming payments or receipts relating to prior to the rate increase to be at a net 12.5%.

If 1 October 2010 comes part way through your GST period, two GST returns must be completed, i.e. one return for supplies made to 30 September 2010 and a second return for supplies from 1 October 2010. The IRD will provide a special form for the additional GST return.

You will need to ensure your systems can deal with two GST rates for a period of time. Credit notes issued post 1 October for purchases made pre 1 October will need to be issued using the old rate. Systems set-up to automatically code repeat transactions will need to be reviewed or switched to manual coding during the transitional period to ensure the correct GST rate is accounted for.

Where goods and services are paid for by progress payments, e.g. insurance or rates, each payment is deemed to be a separate supply. Therefore, the GST on a progress payment made after 1 October 2010 will need to have GST charged at 15%.

ACC Coverplus and Coverplus Extra

We recently heard of a case where a self employed individual was put under financial strain due to the fact they were self employed, had no income protection insurance and were only on the minimum ACC cover, being ACC Coverplus.

We are advocates of CoverPlus Extra, especially for farmers. It allows individuals to choose their own level of cover (within certain limits); it provides certainty of payout for at least six months, farmers do not have to prove loss of earnings and as a general rule premium costs are reasonable.

It is important to understand the impact on you financially if you are self employed should an accident occur. In most cases expenses continue to roll in and you are forced in many cases to employ someone else to come in and cover your job.

Under the basic ACC Coverplus you may be eligible for weekly payments of up to 80% of your liable earnings, starting a week after the injury. The amount of lost earnings compensation paid is dependent on your self-employed status.

Self-employed Status	Lost earnings compensation entitlement for full-time work (2009 levy year) – $ figures subject to annual indexation

Newly self-employed (they have not yet filed a tax return)	Minimum of $384 per week if they are full-time self-employed If they have received any employee earnings within 12 months of going off work due to their injury, ACC may also use those earnings to assess their entitlement.
Recently self employed (they have filed only one tax return)	Based on 80% of earnings in the previous tax year, divided by 52 Weeks. If you have received any employee earnings within 12 months of going off work due to their injury, ACC may also be able to use those earnings to assess your entitlement. If you earned less than the minimum level of lost earnings compensation and you are full-time, ACC will pay you at the minimum entitlement rate of $384 gross per week.
Established in self employment (they have filed two or more tax returns	Up to 80% of your previous year's earnings as declared in the most recently completed tax year, up to a maximum of $1,638.04 per week Minimum of $384 per week if you are full-time self-employed If you have received any employee earnings within 12 months of going off work due to their injury, ACC may also be able to use those earnings to assess their entitlement.

As you can see $384 per week will not cover much when your monthly bills come in and you are paying for a replacement labour unit.

In most circumstances, ACC CoverPlus Extra provides a more appropriate level of cover for self employed individuals, particularly if:

- earnings fluctuate from year to year (eg farmers, real estate agents, contractors)
- earnings status has changed (eg from part-time to full-time)
- you are self-employed and new to business and may otherwise only be entitled to the minimum cover under ACC Cover Plus
- you are a shareholder-employees and new to business and so may have no entitlement to weekly benefits
- your personal income is not an accurate indication of their earnings capacity

Some of the key benefits of ACC CoverPlus Extra are:

- It can give you peace of mind knowing how much lost earnings compensation you are entitled to receive, allowing you to plan ahead with confidence
- Proof of loss of earnings isn't required at claim time
- Cover level can be tailored to suit your personal circumstances
- You can keep your business going by getting replacement labour to help, and can go back to work part-time and still receive you full entitlement

We encourage you to discuss your needs with us to evaluate whether CoverPlus Extra is a more appropriate plan for you. There may still be instances where CoverPlus Extra is still unable to provide the required cover due to the limits ACC has in place around the level of cover. In those circumstances we would recommend you take a top up insurance policy with a private insurer.