



# Newsletter

August 2004

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## TRAVEL BETWEEN HOME AND WORK – DEDUCTIBILITY AND FBT ISSUES

IRD issued a draft interpretation statement setting out guidelines for determining whether travel between home and work is business travel or work related for deductibility or FBT purposes. This ruling may be relevant for many taxpayers.

The general rule is that travel between home and work is private travel and not an allowable deduction for self-employed taxpayers. Similarly where a vehicle is provided to an employee for travel between home and work it is considered available for private use or enjoyment for FBT purposes. In some circumstances, however, travel between home and work is not private. This occurs where such travel is undertaken in the course of performing work rather than in order to commence work or to return home.

In cases relating to deductibility of travel expenditures between home and work (some of which relate to taxpayers who are employees), the following broad factual situations have been identified as circumstances where travel between home and work is "on work" rather than travel to enable the taxpayer to commence work:

- Where a vehicle is essential for transport of goods or equipment necessary for the performance of employment duties at the home and elsewhere;
- Where the taxpayer carries on an "itinerant occupation" (that is, the taxpayer does not work from a fixed work place and the home is the taxpayer's base of operations);
- Where the taxpayer is required to be accessible at the home for employment duties and is required to undertake travel in response to emergency calls; and
- Compliance with FBT rules particularly requires that appropriate administrative procedures and controls exist if an exemption is to be obtained.

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## WHY IS OUR QUESTIONNAIRE SO IMPORTANT?

Recently, a client (of another practice) understated his income. He failed to answer one of the questions in the questionnaire he was given.

He accepted responsibility but this did not save him from IRD penalties.

Be sure to answer the questions carefully. If you don't, we may not know of some tax adjustment we should be making. IF IN DOUBT, PLEASE ASK.

One argument that is often used is that a vehicle is taken home for security reasons. IRD do not accept that as sufficient reason on its own.

Common principles relate to deductibility of motor vehicle expenditure and FBT. IRD consider that for both, the issue is whether the need for the work to be performed partly at the home (and, therefore, the need for the travel) arises from the nature of the work. Travel between home and work would be private travel if the work is performed at the home because of personal circumstances, or personal preferences of the taxpayer.

For travel to be work-related travel, it is not sufficient that the employer and employee have contracted on the basis that employment duties would be performed partly at the home.

You should discuss your particular circumstances with your adviser.



## FINES AND PENALTIES

The general view is that there is no income tax deduction for any fine or penalty paid for a breach of law. Historically the IRD allowed a deduction for some fines, for instance where a fine was imposed on an employee because of a breach of law while the employee was carrying out their employment duties and the employer reimbursed the employee the amount of the fine. A common example is where a sales representative is given a parking ticket or speeding ticket or a truck operator is fined for overloading.

Recently it has been noticeable that IRD auditors are taking a tougher line on the deductibility of fines and penalties. Specifically their view is **“No deduction for fines or penalties for any reason”**. This view is founded on the principle that it is a matter of public policy that there should be no mitigation of the consequence of the fine or penalty.

This view appears harsh and the correct test should be whether there is a connection with the business of the self-employed taxpayer or employer taxpayer who reimburses the employee's fine.

It is accepted that there is limit but that limit can be defined according to whether the fine or penalty is a personal or business structure cost (non deductible), as distinct from having a connection to carrying on the business.

Irrespective of the reasonableness of this view, taxpayers should appreciate that the IRD are currently taking an uncompromising stance.

On the GST front, amending legislation last year indicates that GST does not apply (GST exempt) to the following:

- Penalties or default interest or a charge in the nature of interest that is imposed either under a contract for supply of goods and services or under a statute;
- Late payment penalties imposed by a local authority under the Local Government (Rating) Act for the late payment of rates;
- Finance costs imposed by a local authority under the Local Government (Rating) Act when rates are imposed.

These changes mean that interest and penalties charged by ACC and rates penalties and interest are GST exempt.



## ARE YOU ADMINISTERING YOUR FAMILY TRUST TO KEEP IT SAFE FROM CHALLENGE?

A common belief is that assets held by a family trust are protected from the claims of people who may be able to successfully claim directly against the individuals who are beneficiaries of the trust.

Claimants include business creditors, the taxman, other state agencies, divorced spouses and other family members. Specific provisions are contained in the Relationship Property Act, Companies Act, Family Protection Act and various other statutes. In most cases the use of a trust is effective, as it is the individual who remains exposed, rather than the trust.

However the protection provided is only effective if the trust is administered correctly and established with the correct formalities.

Claimants and their lawyers will seek any opportunity to overturn the trust as a whole, or trustees' decisions, if either the form or administration is deficient.

A trust or trustees' decision can be brushed aside if there is a sham or invalid situation. The trust may be considered a sham if there is no valid trust settlement i.e. the assets remain in the hands of the intended settlor, rather than handed over to the trustees. To be valid a trust requires an intention to create a trust, existence of trust property and identifiable beneficiaries. If any of these do not exist the trust is therefore not created.

If the trustees do not act independently of the settlor, the trust may not in fact exist. If the trustees' decisions are not made in accordance with the trust deed or are made in breach of their duty to the beneficiaries, the decisions may be ineffective. If decisions are contrary to public policy due to illegal

conduct, tax fraud, or as a fraud against creditors, the resulting transactions may be challenged.

On an administrative level there should be:

- a separate bank account;
- a deed of trust;
- decisions substantiated by trust resolutions;
- a proper decision making process undertaken by trustees; and
- evidence that the trustees are acting for the benefit of the beneficiaries and not for the settlor.

If any of these aspects are lacking, your trust could be open to challenge from disaffected or disgruntled parties.



## A ROUGH IDEA IS BETTER THAN NONE

Many businesses should be preparing accounts more than once a year, even if the result is only an approximation. It is better to have a rough idea of how you are going than no idea. From time to time we see a client turn in a poor result for the year and not know it has happened until well into the following year. Often thousands of dollars could have been saved if the business had been monitored regularly. What should you look for in your accounts? Here are two of those things:

### NET PROFIT

This is the most important figure, so it is odd it should appear at the bottom of the accounting report. Ensure owners have been fairly paid for their efforts. The amount left over is the net profit before tax. For many small businesses this is negative and the owners would be financially better to work for someone else.

You now need to have enough profit remaining to provide a reasonable return on your investment in the business. Allowing for risk, 2.5 percent after tax would often not be unreasonable.

### GROSS PROFIT PERCENTAGE

For many businesses the ratio of Gross Profit to Sales should be reasonably constant. What is Gross Profit? It is the amount left over after deducting direct costs (like the food and other goods in a supermarket) from sales. Sometimes, particularly in a manufacturing business, where wages also vary with sales, it is appropriate to deduct these as well.

Constantly monitor your gross profit percentage. To improve this ratio, look for:

- wastage of materials and/or time;
- theft of goods or cash;
- the proportion of high to low profit margin sales (sales mix);
- quoting errors;
- under pricing.



## TAX TRAPS Books giving Tax Advice

Beware books providing tax and trust advice. Some have significant errors. We found this statement in a recent publication: "A LAQC is a company that must allocate its profit or loss for each year in proportion to each shareholders voting rights." Profits are not allocated by LAQCs based on voting rights.

If you buy any of these publications, be sure to check with us before taking any advice from them. Simply because the author claims to have come from a big firm of chartered accountants, does not mean the words he or she writes are accurate.



## NETWORKING - LEARN TO STIMULATE CONVERSATION

SOMEONE asks you "What do you do?" "I am an accountant," I might reply. There's a stifled yawn and conversation dries up.

Instead I could have said "I'm an accountant with a particular interest in helping my clients to save tax."

The extra words present an opportunity for the other person to show an interest. The most likely next question would be "Can you tell me how you do this?"

If you cannot add a "particular interest in" for your work you could add "but when I'm not in the office, I love to go fishing," or whatever. It is important to add something so the conversation can continue.

Networking is about building contacts, not selling. Sales are a by-product.

You do business with people you like. Be ready to stimulate conversation at networking functions and build relationships with people.

## IT'S THE THINKING THAT COUNTS

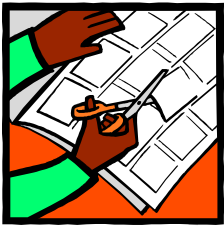


THE two most important parts of a business plan are determining your products and deciding who your customers will be.

A client created a particularly successful business. He said "My business plan was written on one page. This was no reflection on the amount of time and energy put into thinking. I had spent a number of months trying to sort out where I should be focusing my attention. What products should I be selling and to whom should I be selling them? Where were the opportunities and where were the threats? Much of this churned in the back of my mind for months.

"Eventually, I simply wrote down the products I was going to sell, my targets and my strategies for reaching them. The hours of thinking behind this plan were considerable; the number of words were few. Targets were set and a budget added. I focused on a small range of products to a limited market."

As they say, it's the thought that counts!



## SNIPPETS

Coming up in future tax legislation:

- Deductibility of costs relating to patent and resource consent applications that are not granted or are withdrawn – currently such costs are black hole expenditure and non deductible.
- Allowing the IRD to determine amortisation rates for various types of horticultural plants reflecting their estimated useful lives.
- Closing loopholes involving the sale and leaseback of intangibles such as trademarks and newspaper mastheads.
- Providing a 6.7% tax rebate for early payment of tax on self-employment and partnership income in the first year of business – currently not payable until the second year of business.
- Reducing the non-declaration withholding tax rate for non-resident company contractors from the current 15% to 5%.
- Legislating for self-assessment of GST.
- Establishing penalties for NZ employers who do not withhold tax from contract payments for non-resident contractors.

## VANBURWRAY NEWS



Welcome to Michelle Ross who has joined John Angell's Team. Michelle is partway through her studies to qualify as an Accounting Technician.

Michelle Whitmore has been on maternity leave and returns shortly. Initially she will be working just two days per week but will be fulltime from 1 October.

Sandy Jordan has worked in John's Team over the last year but has left us to study fulltime towards her Accounting qualifications.

Catherine Robinson has joined Stephen Eichstaedt's Team. Catherine will be preparing and completing client's Financial Statements, Budgets, Cashflows and Tax Returns. She is also finishing her Business Degree in Accounting at Massey University.

Steven May has joined Ross Whitmore's Team. Steven has completed his Accounting Course at WITT and will be preparing client's Accounts and Tax Returns to draft state.

Julie Winch has returned to Peter Darney's Team as Secretary/Personal Assistant to Peter after the birth of her daughter Amber in October last year. Julie will be job-sharing with Karen Winch. Karen will be in the office in the mornings and Julie will cover the afternoons. If you need an appointment with Peter, please give them a call.

Congratulations to Raewyn and Martin Krutz on the birth of their son Anton.

Congratulations also to Philip Fleming and partner Linda on the birth of their son Aaron.

Birthday Congratulations to Stephen Eichstaedt on turning 50 on 4 July this year!

Roy Grey has retired from our practice. Roy was one of the founding members of Vanburwray. We wish Roy all the best and hope that he enjoys all the extra time with his new grandson!

# The Holidays Act 2003

THE following is a summary of the main points of the new Holidays Act.

## Annual Leave

- Three weeks annual leave is increased to four from 1 April 2007.
- An employee becomes entitled to holidays at the conclusion of one year's service.
- Regular wage payments cannot include holiday pay. Exceptions exist for a fixed term contract of less than 12 months or for those whose work is intermittent.

## Public holidays

An employee may be required to work on a public holiday if:

- it falls on a day which would normally be a working day for the employee; and
- the employment agreement requires the employee to work on the public holiday.

Employees who work on any public holiday are entitled to time and a half for hours worked. They are also entitled to a day in lieu unless they are employed to work only on public holidays.

## Sick Leave

- Minimum annual entitlement is five days a year, after the first six months employment.
- Maximum right to accumulate sick leave is 20 days.
- An employer may call for a medical certificate when the employee has been absent for three consecutive days. Weekends and holidays are included in the calculation of the three days.
- Sick leave is not pro-rated for part time employees - they have the full five days a year.
- It can be used for sick or injured family requiring care.
- An employee can choose to use sick leave for unpaid first week due to a non-work accident, but is not required to use sick leave for this.

## Bereavement Leave

The amount of leave is three days if the relative is a

spouse, parent, child, brother, sister, grandparent, grandchild, or a spouse's parent

It is one day for anyone else having regard to:

- the closeness of the association between the employee and the deceased person;
- whether the employee has to take significant responsibility for all or any of the arrangements for the ceremonies relating to the death; and
- any cultural responsibilities of the employee in relation to the death.



## Laws applicable to both sick and bereavement leave

- Employee has no entitlement until six months have elapsed since starting the job.
- An employer and employee may agree that the employee may take sick leave or bereavement leave in advance.
- In the case of sick leave taken in advance, the amount is to be deducted from the employee's entitlement.
- An employee who intends to take sick or bereavement leave must notify the employer as early as possible before the employee is due to start work or, if that is not practicable, as early as possible after that time.

*If you have any questions about the newsletter items please contact us, we're here to help.*