NOBILO & CO. LTD

CHARTERED
ACCOUNTANTS

JOHN NOBILO, B.Com., CA (PP)

Member of the Institute of Chartered
Accountants of New Zealand

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Reduced financial reporting requirements for SMEs

Recent changes to the Financial Reporting Act 2013 (FRA 2013) have changed the requirements for entities that are not "large" by definition.

Broadly, this means that most NZ businesses will no longer have to prepare financial statements that comply with New Zealand Generally Accepted Accounting Practice (NZ GAAP). Recognising that this could lead to a reduction in the disclosure of financial information by a business, the IRD has introduced its own minimum standards. The standards are aimed at providing the IRD with a basic level of information so that it can adequately assess a business's performance.

From 1 April 2014, the IRD requires companies (including look-through companies) that have annual revenue of $30 million or less, and assets of $60 million or less (or subsidiaries of multinational companies with less than $10 million of annual revenue and assets of less than $20 million) to prepare financial statements that meet its stated minimum requirements.

Entities that exceed these thresholds are required to prepare more extensive financial statements as per the standards set out by the External Reporting Board.

Some extremely small companies will be exempt from the IRD's minimum requirements, as follows:

- Companies that:
  - are not part of a group of companies, and
  - have not derived income of more than $30,000, and
  - have not incurred expenditure of more than $30,000 in an income year.

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- Non-active companies who are not required to file a return.

Minimum Requirements
Under the IRD's minimum requirements, the financial statements must contain:

- a balance sheet setting out the assets, liabilities and net assets of the company at the end of the financial year,
- a profit and loss statement showing income derived and expenditure incurred for the year,
- a statement of accounting policies describing the basis on which the accounts have been prepared, and a description of any material changes in accounting policies used since the previous income year.

The statements must be prepared using double entry and accrual accounting principles. There are also certain valuation principles that may be applied. Tax values may be used where they are consistent with double entry and accrual accounting, or historical cost when tax values are not consistent with the accounting principles used, or when historical cost provides a better basis for valuation. Market values may be used if they provide a better basis of valuation than tax values or historical cost. Interest and dividend income must be grossed up to include resident withholding tax and imputation credits.

There are also presentation requirements that state the accounts must show:

- comparative figures for the prior income year,
- if the accounts are GST inclusive or exclusive,
- tax reconciliation to accounting profit,
- tax fixed asset register,
- reconciliation of shareholders equity for the year,
- relevant amounts from the financial statements summary (IR 10),
- notes to support any amounts disclosed as exception items on the IR 10.

In addition to the above requirements, specific disclosures are required for foresters, livestock owners, and transactions with associated persons.

These are a minimum set of requirements. A higher level of reporting can be adopted if required. The IRD will also accept accounts prepared under NZICA's special purpose framework.

In recent years the IRD has become more adept at collecting and analysing financial information for investigative purposes. Care needs to be taken to disclose the right level of financial information, but always put it through an IRD lens to ensure it is presented in the most favourable light. A misunderstanding by the IRD when reviewing information could lead to unnecessary and costly IRD scrutiny.

Tax Payments – when received in time

Despite our best efforts, many of us are familiar with the consequences of making late tax payments to the IRD. Often, the problem is not just that we forget and leave it to the last minute, but that the payment we make is not processed or received by the IRD in time.

Late payment penalties and use-of-money interest can often be prevented by simply paying tax on time. The IRD has released an updated Standard Practice Statement (SPS 14/01) setting out when different types of tax payments will be accepted as having been paid by the due date. Importantly, it contains several amendments to the previous standards, particularly in relation to payments by post and payments made at Westpac. These changes took effect from 1 October 2014. To ensure your next tax payment is not late and subject to interest and penalties, it is important to familiarise yourself with the standards, as summarised below.

Payments by post – previously, the IRD based the payment date on the post date on the envelope. This is no longer the case. Instead, the IRD will deem the payment date to be the date the envelope is received. As a result, if your routine is to post the cheque on the due date, you may need to put it in the post a day or two earlier.

Electronic payments – payments made electronically or by direct credit into an IRD account must be completed before the end of the bank's online "business hours".

For example, if a GST payment is made on 28 April at 10.30pm but the bank's internet banking cut off is 10.00pm then the payment will not be processed that day and could be treated as late. This also applies to payments made from overseas (bearing in mind the international time difference).

Physical delivery – payments made by cheque must be delivered to an IRD office before it closes, by the due date.

Cash & EFTPOS – all cash and EFTPOS payments must be paid over the counter at a Westpac branch by the due date. It is important to note that returns must still be filed electronically, posted or delivered to the IRD (Westpac will accept the payment but not the actual tax return).

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Post-dated cheques – post-dated cheques will not be banked by the IRD until the specified date. If it is post-dated after the due date then it will be treated as a late payment (even if it was received before the due date).

Take note that from 1 October 2014, Westpac stopped accepting cheque payments so these must now go directly to the IRD.

Weekends & public holidays – if a due date falls on a weekend or a public holiday then electronic payments will be accepted on the next working day. This includes all provincial anniversary days.

Whatever your preferred method of payment, adhering to these updated and clarified standards will enable you to avoid unwanted interest and penalties.

Women in the workforce

Thirty years ago, women would generally leave school at an earlier age than men and with fewer qualifications. The roles women assumed in society were very different and were often paid a much lower wage than what was received by their male counterparts. However, economic development, changing social beliefs and increased education has led to more women obtaining jobs in occupations once reserved for men. Employment opportunities are opening up as more and more females further their education through tertiary institutions. In fact, statistics from leading New Zealand universities put female attendance at almost half their student populations, allowing many to move on to obtain graduate level employment positions.

Despite these recent advances, there continues to be a pay gap between men and women (in 2014 the New Zealand gender pay gap was 9.9%) and many female employees continue to sit at a relatively low rung on the career ladder. At the top, in more senior, executive and board type positions, women continue to be in the minority. This means that their views and opinions are vastly under represented in the decision making processes, which can be problematic given that studies support gender diversity at the top being critical to sustaining performance.

The performance enhancing effects of women working in executive positions goes beyond simply boosting a company's image and reputation. Reports out of Harvard University have shown that entities with women directors deal more effectively with risk and long term priorities, as women tend to be more strategic thinkers with a natural ability to scenario plan and find creative solutions. Having women in top positions can also improve the performance of other female employees who look up to the more senior women as role models.

Another benefit of having females at the top is that they are generally more familiar with consumer needs. Where women tend to drive the majority of consumer purchase decisions, having women involved at the top can enable more successful products and services to be developed. So with that being said, you would think the ratio of females to males would be higher at the top.

A number of factors contribute to women's lack of presence in more senior positions. An obvious one is the implications of childbirth, where taking time away from work often means women do not experience constant levels of progression throughout their career. Other factors that can prevent women from reaching those top positions include a lack of support provided by other women, unconscious bias from males in more senior positions and potentially a lack of self-confidence.

It is important for both males and females to recognise and embrace the differences between each gender. It is not a matter of women trying to act like men. It is about people playing to their own strengths and earning the respect of their peers and subordinates by being themselves.

With studies suggesting that women are making a positive difference to the bottom line, it will be interesting to see whether firms that have a more balanced gender composition enjoy an unbalanced share of the profit.

Easing up on easements

An easement gives a person the right to use another person's land in a particular way, or to prevent that other person from using their land in a particular way. Historically, amounts received by a landowner to grant an easement have been treated as taxable under section CC 1 of the Income Tax Act 2007.

This has been somewhat illogical, because granting an easement typically reduces the value of land and if the sale of land would be non-taxable, it makes sense that a payment for an easement should also be non-taxable.

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The tax treatment of easements is now in a state of change for the following two reasons.

Firstly, looking forward, new legislation has been passed that will treat one-off easement receipts as non-taxable from 1 April 2015. Secondly, looking backward, a recent High Court decision has cast doubt over how CC 1, should be interpreted. The case involved a $3 million payment by Transpower New Zealand Limited (Transpower) to Vector Limited (Vector) for an easement so that Transpower could complete an upgrade by accessing Vector's land.

Vector asserted the easement was non-taxable, however the IRD reviewed the situation and disagreed. Both sides did agree that the payments related to land, and were capital in nature. But Vector took the view that the phrase "other revenues" refers to amounts of a revenue nature. But the IRD argued that it was clear from the legislation that the phrase 'other revenues' was intended to capture both income and capital receipts.

The High Court rejected the IRD's argument and found in favour of Vector, stating that the ordinary meaning of 'revenue' is income, and that capital receipts are not captured under the term "other revenues". They also concluded that the legislation only taxes capital amounts where they are explicitly listed. In addition, the Court also found the nature of the payments to be capital on the basis that the payments were not part of Vector's ordinary income earning process, and their ability to use its assets was permanently impaired.

Emphasis was placed on the importance of the principles of statutory interpretation. This was emphasised by the Court's comment: "if Parliament intends to tax capital it must do so with clear language".

The case represents a significant change of treatment. It also opens the door for taxpayers to request re-assessments (and tax refunds) of past tax returns in which easements have been treated as taxable. How the IRD would view requests like this is uncertain at this stage because it has not commented on the case yet. But if easements have been treated as taxable, there is a potential opportunity for the tax paid to be reassessed.

Snippets

Tax residency case overturned

A recent Taxation Review Authority (TRA) case concluded an individual was a New Zealand tax resident despite being absent from New Zealand for a long period of time. In brief, the decision was a consequence of having an investment property that was 'available' to him in New Zealand and an on-going relationship with his family and ex-wife.

On appeal to the High Court, the TRA's decision has been overturned. The High Court held that the individual was not a New Zealand resident as he had never lived in the New Zealand investment property; therefore it could not be regarded as his 'home'. Although he did have other, on-going, personal connections with New Zealand, in the absence of having a 'home' or 'house' in New Zealand, these connections did not alter the conclusion reached.

This case provides a sigh of relief, as the original TRA decision was of some concern. Although every individual's situation is different, the High Court decision should give New Zealanders living and working overseas with an investment property in New Zealand some peace of mind.

Drones reveal tax evasion

Tax avoidance is a big problem for many governments around the world with some countries going to great lengths to identify and hold tax avoiders accountable. In particular, Argentina has started using drones to catch people who fail to declare certain items of property in their tax returns.

According to news reports, tax authorities have sent drones over wealthy areas of Argentina to investigate the existence of assets that owners may have failed to declare on their tax returns. The unmanned aircraft have taken pictures of at least 200 homes and 100 pools, all of which were sitting on plots registered as vacant. The drones' findings amounted to missing tax payments of more than US$2m (NZ$2.55m) with owners of the properties now expecting heavy fines.

Could New Zealand be next to catch on to this trend?

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

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