



## Tax Specialist Joins BVO

A brief stint in the Hawkes Bay with Staples Rodway was followed by a move to Deloitte in Auckland where Marianne was an Associate Director in Tax working predominantly with large multi nationals.

Marianne describes herself as a tax generalist – a person who is becoming increasingly hard to find given the complexities of the various tax regimes.

Marianne has a Bachelor of Commerce (Accounting & Tax) from the University of Auckland. She is also a Chartered Accountant, a registered mentor and holds a Public Practice certificate with NZICA. She is passionate about sharing her knowledge and welcomes the opportunity to facilitate in-house training and seminars for staff and clients alike.

In her spare time, Marianne enjoys the many pleasures of living on Waiheke Island such as the beaches and vineyards. Marianne is also an avid cyclist having participated in many endurance cycling events such as K2 and will be making the trek south to complete the Lake Taupo cycle challenge this month.

***Marianne is available to assist clients and other Chartered Accountancy practices with tax compliance and consulting issues as they arise***



## New Director Appointed

We wish to congratulate Alex Houghton who has been made a director of the firm. Alex works with Dan Virtue and has been with the firm 18 months.

Alex, a Chartered Accountant, has broad experience in accounting and tax gained from working in chartered accounting firms and corporations in New Zealand, Australia and the United Kingdom.

Prior to joining BVO, Alex was a tax manager at Ernst & Young working on a variety of clients from owner-operators to multinational companies and companies listed on the New Zealand stock exchange. While in the United Kingdom Alex held management accounting and systems roles in the European Regional Office of Walt Disney International, a financial analyst at British Sky Broadcasting PLC and an Auditor at one of Ernst & Young's London offices.

Prior to the United Kingdom, Alex worked as an Auditor at Ernst & Young's Auckland office and at Grant Thornton.

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



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### Help! Who isn't Associated!

The new tests of "association" for tax purposes are now in force – The rules are particularly relevant if you hold land. The amendments to the associated persons provisions contained in the Income Tax Act 2007 were designed to close loopholes perceived by the Inland Revenue as being easily manipulated. This is especially in respect to those provisions relating to the land taxing provisions. These changes directly impinge on those in the business as property dealers, developers or builders and those that now find themselves associated to such persons. The direct result will be a welcome addition to the government's coffers as many more land transactions may be subject to income tax. As these specific amendments apply from the date of enactment

### Finally, the July 2008 tax bill

It has been a long time in the making - finally the Taxation (International Taxation, Life Insurance, and Remedial Matters) Bill has been enacted. The Bill, introduced in July 2008, passed its final stages in Parliament on 18 September 2009 and received Royal assent (Governor-General signature) on 6 October 2009.

The Bill included changes to the International Tax regime and a considerable revamp of the Associated Persons provisions.

#### The key application dates are as follows:

- International tax changes – applies to income years beginning on or after 1 July 2009.
- Life insurance – applies generally from 1 July 2010.
- Associated persons rules (other than land) – applies from the 2010/2011 income tax year.
- Associated persons rule (land) – applies from the date of Royal assent; i.e. 6 October 2009.
- Payroll giving – applies three months after the date of Royal assent.
- Relocation payments and meal allowances – changes backdated to 1 October 2001.

(i.e. 6 October 2009), the rest of this article will focus on the impact of these new provisions on the taxing of land sales.

New Zealand currently only taxes amounts from the sale of land in specific circumstances. Land sales will generally only be taxed when the land was acquired with an intention of resale, or a business dealing in, developing, or building on land exists, or when certain subdivisions are undertaken. If you are associated to a person carrying on land dealing or a developing business, the end result is being taxed on any profits derived from the sale of land

if sold within 10 years of acquisition. Further, being associated to a builder at the time you undertake any improvements to a property can also result in being taxed on the proceeds of the sale of that property if it is sold within 10 years of completing the improvements. The reach of these new provisions is quite extensive and, as some commentators have already noted, the outcomes now arising were never contemplated by the legislators.

A major change arising from these new provisions relates to trusts. Trusts have in the past been a common way to “break association”, because the only test applying to trusts associated a person to the trustee of the trust where the person’s spouse, civil union or de facto partner, or an infant child (natural and adopted child under the age of 20) was a beneficiary of the trust. The new trust related provisions that affect land sales, now associate:

- the trustees of two trusts with a common settlor (with spouses, civil union and de facto partners treated as the same settlor);
- the trustee of a trust and the settlor of the trust (excluding charitable trusts); and
- the trustee of a trust and the person who has a power to appoint or remove the trustee.

The other significant change is the introduction of a tripartite test that associates two persons who are associated to a common third person. Whilst there are some restrictions on its application, the provision does widen the range of persons who will now be “associated” with each other.

For example, say a trustee has a 25% shareholding in a land development company and there is a third person, Bob, who has the power to appoint or remove trustees. On applying these new rules the following outcomes results:

- the trustee is associated with the development company as the trustee holds 25% or more interest in the company;
- the trustee is associated to Bob under the new provision that “connects” those who have the power to appoint or remove trustees; and
- Bob will be associated to the developer company via his common association with the trustee under the new tripartite test.

This association will taint any land that Bob acquires which may or may not be an appropriate outcome especially where Bob is merely acting in a professional advisor capacity. This is one example where the new provisions seem to “extend” the intended pool of persons who may associated.

Given the considerable reach of these new provisions, particularly for land transactions, advisors will need to make in depth inquiries as to all the potential relationships that may be caught by the tripartite provision.

Until now, it had been possible to structure an individual’s affairs so that an entity undertaking business as a developer, builder or dealer, was not associated to the individual or other entities owning their private residence and investment properties. The effect of these changes means that most of these structures will no longer be effective. So for existing structures – what does this mean?

Firstly, land acquired before the date of royal assent in structures where no association existed under the old provisions will not be affected. It is only land acquired after this date (i.e. 6 October 2009) that could be caught by the new provisions.

For those involved in the business of building or for those who are associated to such a person, the new provisions apply to improvements which commenced on or after the date of royal assent (i.e. 6 October 2009).

Regardless of when the person acquired the land and whether an association existed at that time, the new provisions could result in a tax liability if the association exists at the time the improvement commenced and the property is sold within 10 years of completing those improvements.

If you are in business as a land dealer, developer or builder or you believe you may now be associated to a person in such a business, you should contact us to discuss the implications of these changes so that any potential future tax liabilities can be more easily managed.

Also note, further remedial changes to these provisions is likely in the future.

## Mortgage Break fees - deductible?

Recently, Inland Revenue published two draft public rulings clarifying its position on the deductibility of mortgage break fees paid by landlords. The two rulings detail the tax treatment of break fees associated with loans entered into to acquire property from which rental income is derived, or to refinance another loan for that purpose.

### Break fee to exit early

When a landlord pays a break fee to the lender to repay in full and terminate a loan earlier than the agreed repayment date, the proposed tax treatment is:

- a base price adjustment is required;
- the borrower includes the break fee in the ‘consideration’ element of the base price adjustment formula;
- the negative amount under the base price adjustment is expenditure incurred under the financial arrangement rules and constitutes interest.
- for companies (other than qualifying companies) a deduction;
- for other taxpayers a deduction is available to the extent the general permission tests have been satisfied.

**Break fee to vary interest rate.** When a landlord pays a break fee to the lender for a variation of a loan to adjust the interest rate, the proposed tax treatment is:

## Snippets

### Christmas Cheers!

As Christmas looms, many businesses will be gearing up to celebrate the festive season and to show their appreciation to staff, colleagues and clients for their support.

Unfortunately, the taxman also wants some of the ‘cheer’ so below is a timely refresher setting out the tax consequences associated with such festive spending; the entertainment tax regime. There are three categories of entertainment: fully deductible, fully deductible but subject to FBT and 50% deductible.

- no base price adjustment;
- In relation to the variation of the terms of the loan Determination G25 applies to taxpayers who are not cash basis persons\* and to taxpayers who are cash basis persons and have elected to adopt a spreading method;
- the break fee is included in the calculation under the Determination and the deduction of the break fee is spread over the remaining term of the loan; and
- a cash basis person can deduct the amount of the break fee when it is incurred under the general permission, provided the money was borrowed to purchase a property from which rental income is derived.

*\* a cash basis person is a natural person whose financial arrangements do not exceed prescribed thresholds, or the trustee of the estate of a deceased person where the deceased person was a cash basis person at death. Contact your BVO representative if you require further clarification.*

The draft rulings will not apply where the loan amount was not used solely for deriving rental income or where the loan is connected with another financial arrangement between the lender and borrower. The proposed tax treatment will also not apply if the taxpayer has adopted the IFRS financial reporting spreading method.

Once finalised it is proposed that these rulings will apply from the end of the 2008/2009 income year to the end of the 2011/2012 income year. *The deadline for comment is 6 November 2009.*

**Fully deductible:** These expenses will be 100% deductible:

- meals while travelling on business
- food / drink at a conference or training course that runs longer than 4 hours
- meal allowance for overtime
- morning and afternoon teas
- promotions open to the public

- if an employee’s salary package includes a taxable allowance for entertaining clients (fully deductible to the employer)
- entertainment consumed overseas

### Fully deductible but subject to FBT:

These expenses will be 100% deductible, however they will attract FBT meaning that an FBT return and payment will be required. Note that where the spending is under the de minimis thresholds of \$200 per quarter per employee or under \$15,000 p.a. per employer, no FBT is incurred. This commonly includes expenditure on gifts or benefits to employees consumed at their leisure.

Some examples are (if the expenditure is over the thresholds mentioned):

- gifts of food or beverages to staff
- t-shirts, caps, jackets provided to staff
- sponsorship of employee’s sports team.

### 50% deductible:

These expenses are only 50% deductible for both income tax and GST:

- entertainment incurred in relation to an existing or potential or prospective business client or contact
- entertainment to staff to maintain goodwill
- entertainment incurred mainly in connection to specific business transactions.

Some examples include:

- Staff Christmas party
- Christmas lunch/dinner for colleagues/clients
- Food and wine provided to colleagues/clients
- Gifts of food or wine to staff (below FBT thresholds)
- Food and drink provided for a function on business premises.

It should also be noted that ‘entertainment’ includes all relevant costs of holding such events including catering, venue hire, crockery, table, glass, on site entertainment.

### Singapore / NZ DTA

New Zealand and Singapore recently signed a new double tax agreement (DTA) replacing the current DTA dating

from 1973. The key changes include amendments to the withholding tax rates on dividends, royalties and interest.

|           | 1973 DTA | New DTA   |
|-----------|----------|---|
| Dividends | 15%      | 0-10% shareholding :15%<br>> 10% shareholding: 5% |
| Interest  | 15%      | 10%   |
| Royalties | 15%      | 5%  |

The current withholding tax rates and the new rates are: The new DTA comes into effect once both parties have given it legal effect, which in New Zealand will occur through an Order in Council.

### Future tax reviews on the horizon

On 25 September 2009, the Revenue Minister, Peter Dunne, released the updated 2009 -10 tax policy work programme. In the next three months, we can expect a new tax bill and several issue papers for consultation.

The next new tax bill is likely to be introduced in December (an early Christmas present for tax advisors!) and it is expected to include the following issues:

- Amendments to the student loan scheme to simplify administration aspects
- Remedial amendments to the binding ruling system which follows consultation on the issues paper released in August 2009
- Further refinements to the KiwiSaver scheme. It includes possible opting out rules.
- Measures to progress the Trans-Tasman retirement savings portability issue which was announced in July 2009.

The following issues papers are expected to be released before the end of the year:

- Disputes – this paper will address concerns about the disputes process and challenge procedures.
- Non portfolio FIF issues – a paper to extend the active income exemption to non portfolio branches and entities
- GST – Business to Business – this paper follows the one released last year and further refines specific proposals aimed at protecting the tax base and improving the GST rules.
- A concept paper to determine the best approach to hybrid financial arrangements.
- Income splitting – the Government intends to release an issues paper, followed by draft legislation in 2010 introducing a voluntary income splitting scheme for parents with dependant children.