Tax Information Bulletin

Volume Four, No. 2 September 1992

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Tax Information Bulletin Survey

In the last Tax Information Bulletin, we said that we would be surveying our readers' opinions of this Bulletin with the next issue.

We are using an independent market research firm to run this survey and collate the results. However, because of the size of the TIB mailing list (approximately 13,000, plus IRD staff), it's not practical to get a response from everyone. For this reason, we've only sent a questionnaire to every fifth reader.

If you haven't received a questionnaire, but you have comments that you want to make, we'd like to hear them. Please write to us at:

Tax Information Bulletin
Inland Revenue Department
P O Box 2198
WELLINGTON

or fax your comments to us on (04) 473 3250.

This will help us to adapt the Tax Information Bulletin to meet the needs of you, our readers.

ISSN 0114-7161

Public Service Motor Vehicle Reimbursing Rates

Use for Income Tax Purposes

In TIB Volume 3 No. 2 we set out new rules for using the Public Service “Mileage” Rates (PSMRs) and gave a simplified alternative rate. Comments from our local Inland Revenue offices suggest that there may be some misunderstanding of these rules.

The new rules and rates apply only to the reimbursement of motor vehicle expenses incurred by -

- employees, irrespective of annual distance travelled, and
- shareholder-employees whose total reimbursed travel for the year does not exceed 2,000kms.

If a company wishes to reimburse a shareholder-employee for more than 2,000km of business-related travel in one year, the reimbursement must be on a factual, verifiable basis. The PSMRs or the alternative rates cannot be used.

Self-employed taxpayers, including members of a partnership, can use the PSMRs where their business travel does not exceed 2,000km in a year. If the travel exceeds that figure, claims for travel must be based on actual expenditure apportioned, where appropriate, between the business and private travel of the vehicle concerned.

Reference HO 10.A.8.4

Livestock Valuation Reform Announced

Introduction

The Government is going to reform the way livestock is valued for tax purposes, to give greater flexibility and more accurate results.

Under the present regime, some farmers who use the trading stock scheme pay tax in advance through overvaluation of livestock. This applies especially to farmers who breed their own stock. This is the main reason why the Government capped trading stock values over the last two years.

Please note that this article discusses proposed legislation, which is not law at the time of printing.

Replacement of Trading Scheme

The trading stock scheme will be repealed to overcome the anomaly set out above. It will be replaced by two new cost options, one of which is based on national standard costs.

National Standard Cost Scheme

A National Standard Cost Scheme will replace the trading stock scheme, to more readily reflect the cost of livestock production. Inland Revenue will announce figures each year from which farmers will be able to calculate the value of livestock on hand at year's end.

Self Assessed Cost Scheme

This is a new option for valuing livestock at cost. It will generally follow the same operating rules as the National Standard Cost Scheme. The main difference will be that this method will use a farmer's own costs of production, rather than nationally provided average costs.

Amendments to Herd Scheme

The existing herd scheme will be retained but made more flexible. Differential herd values will be introduced so farmers can value their herd livestock at values other than national average market values. This will allow them to take into account regional, breed and quality variations.

Subject to a supporting valuation, a farmer can set his/her herd values at 90%, 100%, 110%, 120% or 130% of the National Average Market Values. However, the farmer must notify Inland Revenue before changing values, and any change in percentage will be assessable for income tax.

Farmers will also be able to value some stock of a class under the herd scheme, and some under an alternative valuation option. They will then have the discretion to move stock from the alternative valuation scheme to the herd scheme on an animal-by-animal basis. This will help farmers who are increasing livestock numbers or recovering from an adverse event.

Trial of new value setting methods

Because of problems with the current method of setting National Average Market Values, the Government will trial two new methods. These are a year-end “snapshot” of livestock values based on information from livestock valuers, and a survey of stock values over the main sale periods.

Amendments to High-Priced Livestock Scheme

There are several proposed amendments to the high-priced livestock scheme:

- it will now apply only to stock with a purchase price of more than $500, or more than five times the National Average Market Values.
- stock may be depreciated using either the straight line or diminishing value method
- depreciation rates will be based on economic life
- once an animal is depreciated to the national average market value, it will be moved to the scheme being used for other stock of the same class. The requirement to depreciate animals to $1 will be repealed.

Adverse Events

The Government will amend the Income Equalisation Scheme to make it easier for farmers to spread income resulting from the force sale of livestock after an adverse event.

Farmers will be able to "self-assess" an adverse event depending on their own circumstances, rather than having to rely on regionally declared events, as under the present scheme.

More Information

These changes result from recommendations that the Livestock Valuation Consultative Committee made to the Government. If you want a copy of the Committee's report, which contains the Government's decisions, please write to:

Legislative Affairs
Inland Revenue Department
P O Box 2198
WELLINGTON

Legislation not passed yet

Please note that these proposals are not law yet. We will publish full details of the changes as soon as they are passed by Parliament.

Cash Basis Holders and the Application of Determination G24: Straight Line Method

Introduction

We have been asked if cash basis holders can use Determination G24: *Straight Line Method.*

The short answer to this question is no. The straight line method is only available to taxpayers who calculate income or expenditure on an accruals basis. A more detailed explanation is provided below.

Cash Basis Holder Status is Binding

The term "Cash basis holder" is defined in section 64D of the Income Tax Act 1976 ("the Act").

A taxpayer cannot opt out of the cash basis holder status. This is clear from section 64D(1), which states:

> "Subject to this section, a natural person ***shall*** be a cash basis holder in respect of financial arrangements held by that person in any income year ..."
>
> (emphasis added).

Significance of Cash Basis Holder Status

A cash basis holder returns income from financial arrangements on a cash or receivable basis, subject to the calculation of the cash base price adjustment set out in section 64F(3). This means that income during the life of the financial arrangement is not calculated on a yield to maturity basis.

That point is evident from the wording of section 64C(5), which states:

> "Subsections (2) to (4) of this section shall not apply-
>
> (a) To a cash basis holder ...".

This means that a cash basis holder cannot use the straight line method provided for in section 64C(2A).

Determination G24: Straight Line Method

The Commissioner signed Determination G24 on 10 July 1991. It is a simplification measure that relaxes the requirement for taxpayers to calculate income on a yield to maturity basis.

Cash basis holders cannot use Determination G24 as it is the expression of a method provided for in section 64C(2A). As mentioned above, that section does not apply to cash basis holders.

Reference: HO.T.181

Tax Options for Farmers affected by Snowstorms

The Ministers of Agriculture and Revenue recently made an announcement to ensure that farmers hit by the recent snow storms are aware of their tax options.

The tax implications of the devastation caused by the storms emerged as one of the major concerns of the affected farmers. There are several opportunities in the tax system to alleviate these concerns.

To avoid overpaying tax, farmers with significantly reduced incomes should consider estimating their 1992-93 provisional tax. Such estimates should be “fair and reasonable”, although Inland Revenue is aware that many farmers are unsure how badly the snowstorms have affected them.

The Commissioner of Inland Revenue will also use his discretion to extend the period in which farmers can make Income Equalisation deposits. For farmers who cannot yet make deposits for the 1991-92 income year, an extension will be allowed until 30 October. Farmers who have been adversely affected by the snowstorms will also be allowed early withdrawals from the scheme.

Farmers should contact their accountants or tax advisors to ensure they make the best use of the tax options available to them.

Snow Relief Trust - Charitable Status

Inland Revenue recently granted charitable status to the South Island "Snow Relief Trust". This means that individuals who make donations to the Trust will be able to claim a rebate under section 56A(2) of the Income Tax Act, and public companies that make donations will be entitled to a deduction under section 147.

To be eligible, donations to the Trust must be evidenced by a receipt. Receipts will be in the form of a Trust Bank or Bank of New Zealand deposit slip butt, stamped with the name of the Trust.

Under section 56A(2), an individual may only claim a rebate for a donation of $5 or more. For any income year, the total rebate that an individual can claim is limited to the lesser of 33 $^{1}/_{3}$% of all donations s/he makes, or $500.

For public companies, the deduction available under section 147 (for any income year, to any one donee) is limited to the greater of 1% of the company's assessable income, or $4,000. The total deduction to all donees for a single year is limited to the greater of $1,000 or 5% of the company's assessable income.

Reference: HO 10.C.5.1

Extension of Time for Group Companies

Group Companies will be entitled to new tax privileges under a change in Inland Revenue Policy.

Inland Revenue has adopted the Tax Simplification Committee's recommendation that group companies should be able to nominate a company officer to act as tax agent for the group. The nominated agent will have the privileges set out in the existing extension of time arrangements. This will allow group companies to spread their workload for IR 4 company tax returns throughout the financial year.

The extension of time arrangements will be slightly different for group companies. Each arrangement will be separately negotiated between the group and the local District Commissioner or a nominated Inland Revenue representative.

Groups of companies will also have all their statements and returns sent out in one envelope, rather than receiving them separately.

Please contact your local Inland Revenue office if you want more information about this change.

Tax in Dispute - Interest Rate Change

The interest rate on tax in dispute has been lowered from 13.5% to 10%. The new rate applies from 1 April 1992, both for interest paid by and to Inland Revenue.

Where interest is payable for a period that bridges 1 April 1992, it will be calculated at the old rate for the period before 1 April, and the new rate on and after that date.

The new rate will also apply to interest on late GST refunds, and GST in dispute. Two separate rates will also apply, where a calculation bridges 1 April 1992.

Reference: HO 10.T.2.3

IRD Follow-up on Undeclared Income

A new system is making it hard for taxpayers to hide undeclared income from Inland Revenue. Two thousand people who gave incorrect income details in last year's tax returns have already been identified by the system, in its first five months to the end of August.

Together they owe an extra $2.8 million tax.

The new Income Verification system works by checking information that taxpayers supply against income from employers and other sources. All returns that Inland Revenue receives are automatically checked for discrepancies, and taxpayers who have left income out of their returns are identified and followed up.

Most taxpayers are honest and fill in their tax returns correctly. However, there are some who believe they should pay less than their fair share. The new computer system makes it very difficult to hide income, and will help Inland Revenue to make sure that everyone pays the fair amount of tax.

Where Inland Revenue finds that taxpayers have deliberately attempted to hide income, they will be charged a late payment penalty, and could face prosecution and penal tax.

Inland Revenue is sending letters to people who gave incorrect income details, to tell them what they owe before sending them an account for the outstanding tax.

Anyone who disagrees with such an assessment should contact their local Inland Revenue office.

Tax Audits - New Booklet from Inland Revenue

Inland Revenue has recently released “A Guide to Inland Revenue Audits”, a booklet for small business operators and investors. It describes the audit process from start to finish; what happens during the auditor's first visit, what records are checked, and so on.

The booklet then gives a detailed explanation of the individual's rights and obligations during an audit, including how much notice is required, what the person being audited must do, what s/he may do, the role of legal privilege and the right to see IRD records about him/herself.

The book also covers what happens after an audit; assessments, refund or payment of tax, late payment penalties, penal action, and what the taxpayer can do if s/he disagrees with the results of the audit.

Most people who are in business or who receive investment income will be audited by Inland Revenue at some stage, so it is important that they understand the audit process, and their rights and obligations. This new book takes the mystery out of the experience of being audited.

Qualifying Companies winding up

It may be argued that a Qualifying Company which winds up or is formed part way through an income year is unable to maintain Qualifying Company status for that year. This is because section 393B(1) of the Income Tax Act 1976 requires a company to satisfy certain criteria at all times during the income year.

It is not intended that a company lose the benefits of being a Qualifying Company or a Loss Attributing Qualifying Company in any year solely because it winds up or is formed in that year. Inland Revenue will interpret the Qualifying Company legislation accordingly.

We have been asked whether Inland Revenue considers that a company which elects to be a Qualifying Company for the 1992-93 income year, and which pays Qualifying Company Election Tax at the concessional rate, will effectively revoke its election to enter the regime if it winds up in the 1992-93 year. If the answer was “yes”, the company would not be liable to pay Qualifying Company Election Tax, and any distributions it makes would be subject to tax at the normal rate.

Inland Revenue believes that the principles outlined above would apply to this situation. A Qualifying Company that winds up part way through the 1992-93 income year will retain its Qualifying Company status for the part of the year before winding up, provided it meets all the other eligibility criteria during that time.

Due Dates Reminder

October

5 PAYE deductions and IR 66ES for last 15 days of September 1992 due - "large" employers only.

7 First instalment of 1993 provisional tax due for taxpayers with June balance dates.

Second instalment of 1993 provisional tax due for taxpayers with February balance dates.

Third instalment of 1993 provisional tax due for taxpayers with October balance dates.

Annual income tax returns due for non-IR 5 taxpayers with balance dates from 1 to 30 June 1992.

End-of-year tax due for taxpayers with November balance dates.

20 RWT on interest deducted during September 1992 due for monthly payers.

20 RWT on interest deducted from 1 April to 30 September 1992 due for six-monthly payers.

RWT on dividends deducted during September 1992 due.

Non-Resident Withholding Tax (or Approved Issuer Levy) deducted during September 1992 due.

PAYE deductions and IR 66ES for first 15 days of October 1992 due - "large" employers only.

PAYE deductions and IR 66ES for September 1992 due - "small" employers only.

FBT return and payment for quarter ended 30 September 1992 due.

Gaming Machine Duty return and payment for month ended 30 September 1992 due.

30 GST return and payment for period ended 30 September 1992 due.