Volume Five, No.10 March 1994

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Notes on recent cases heard by the Taxation Review Authority, the High Court, the Court of Appeal and the Privy Council. See page 15 for a list of cases covered in this bulletin.

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## Child Support booklets

**Child Support - a guide for bankers** (CS 66) August 1992
*An explanation of the obligations that banks may have to deal with for Child Support.*

**Child Support - a guide for tax practitioners** (CS 4) March 1992
*A summary (mainly for accountants) of how Child Support works, and the rates for calculating payments.*

**Child Support - a parent's guide** (CS 1) March 1992
*An in-depth explanation of Child Support, both for custodial parents and parents who don't have custody of their children.*

**Child Support - an introduction** (CS 3) March 1992
*A brief introduction to Child Support.*

**Child Support - does it affect you?** (CS 50)
*A brief introduction to Child Support in Maori, Cook Island Maori, Samoan, Tongan and Chinese.*

**Child Support - how to approach the Family Court** (CS 51) June 1992
*Explains what steps people need to take if they want to go to the Family Court about their Child Support.*

**Child Support - the basics - a guide for students**
*A basic explanation of how Child Support works, written for mainly for students.*

# Due dates reminder

## April

5 PAYE deductions and deduction schedules for last 16 March 1994 due - "large" employers only.

7 First instalment of 1995 provisional tax due for taxpayers with December balance dates.

Second instalment of 1994 provisional tax due for taxpayers with August balance dates.

Third instalment of 1994 provisional tax due for taxpayers with April balance dates.

First instalment of 1995 Student Loan interim repayment due for taxpayers with December balance dates.

Second instalment of 1994 Student Loan interim repayment due for taxpayers with August balance dates.

Third instalment of 1994 Student Loan interim repayment due for taxpayers with April balance dates.

20 PAYE deductions and deduction schedules for first 15 days of April 1994 due - "large" employers.

PAYE deductions and deduction schedules for March 1994 due - "small" employers.

Completed PAYE deduction certificates for the year ended 31 March 1994 should have been distributed to all employees.

FBT return and payment for quarter ended 31 March 1994 due.

Annual FBT return for period 1/4/93-31/3/94 due for employers who pay no fringe benefits.

Gaming machine duty return and payment for month ended 31 March 1994 due.

RWT on interest deducted during March 1994 due for monthly payers.

RWT on interest deducted 1/10/93-31/3/94 due for six-monthly payers.

RWT on dividends deducted during March 1994 due.

Non-resident withholding tax (or approved issuer levy) deducted during March 1994 due.

29 GST return and payment for period ended 31 March 1994 due.

## May

5 PAYE deductions and deduction schedules for last 15 days of April 1994 due - "large" employers only.

7 First instalment of 1995 provisional tax due for taxpayers with January balance dates.

Second instalment of 1995 provisional tax due for taxpayers with September balance dates.

Third instalment of 1994 provisional tax due for taxpayers with May balance dates.

First instalment of 1995 Student Loan interim repayment due for taxpayers with January balance dates.

Second instalment of 1995 Student Loan interim repayment due for taxpayers with September balance dates.

Third instalment of 1994 Student Loan interim repayment due for taxpayers with May balance dates.

20 PAYE deductions and deduction schedules for first 15 days of May 1994 due - "large" employers.

PAYE deductions and deduction schedules for April 1994 due - "small" employers.

Gaming machine duty return and payment for month ended 30 April 1994 due.

RWT on interest deducted during April 1994 due for monthly payers.

RWT on dividends deducted during April 1994 due.

Non-resident withholding tax (or approved issuer levy) deducted during April 1994 due.

31 GST return and payment for period ended 30 April 1994 due.

FBT - Annual liable return (1/4/93 - 31/3/94) and payment due for employers who elect to pay FBT on an annual basis.

Annual wage reconciliation and employer premium statement (IR 68A/P) due to be filed, and 1994 employer premium payment due.

RWT on interest - Annual reconciliation statement (IR 15S) due.

RWT on dividends - specified dividend reconciliation (IR 17S or IR 17SA) due.

## For non-profit groups

**Charitable organisations** (IR 255) May 1993

*Explains what tax exemptions are available to approved charities and donee organisations, and the criteria that an organisation must meet to get an exemption.*

**Clubs and societies** (IR 254) July 1992

*Explains the tax obligations that a club, society or other non-profit group must meet.*

**Education centres** (IR 253) April 1993

*Explains the tax obligations of schools and other education centres. Covers everything from kindergartens and kohanga reo to universities and polytechnics.*

**Gaming machine duty** (IR 680A) February 1992

*An explanation of the duty that must be paid by groups that operate gaming machines.*

**GST for non-profit bodies** (GST 605A) September 1992

*Tells non-profit groups whether they'll need to register for GST, and on what activities they must account for GST.*

## For individual taxpayers

**Dealing with Inland Revenue** (IR 256) April 1993

*Introduction to Inland Revenue, written mainly for individual taxpayers. It sets out who to ask for in some common situations, and lists taxpayers' basic rights and obligations when dealing with Inland Revenue.*

**Estate and gift duties** (IR 634) November 1991

*An explanation of estate and gift duties, written for individual people rather than solicitors or legal firms. Estate duty has been repealed since this book was written.*

**Interest earnings and your IRD number** (IR 283L) September 1991

*Explains the requirement for giving to your IRD number to your bank or anyone else who pays you interest.*

**International tax guide** (IR 275) June 1989

*Deals with controlled foreign companies, foreign investment funds, and people who have interests in them.*

**IR 56 taxpayer handbook** (IR 56B) April 1993

*A booklet for part-time private domestic workers, embassy staff, nannies, overseas company reps and Deep Freeze base workers who make their own PAYE payments.*

**Koha** (IR 278) August 1991

*A guide to payments in the Maori community - income tax and GST consequences.*

**New Zealand tax residence** (IR 292) April 1991

*An explanation of who is a New Zealand resident for tax purposes.*

**Objection procedures** (IR 266) April 1993

*Explains how to make a formal objection to a tax assessment, and what further options are available if you disagree with Inland Revenue.*

**Provisional tax** (IR 289) April 1993

*People whose end-of-year tax bill is over $2,500 must generally pay provisional tax for the following year. This booklet explains what provisional tax is, and how and when it must be paid.*

**Putting your tax affairs right** (IR 282) March 1990

*Explains the advantages of telling Inland Revenue if your tax affairs are not in order, before we find out in some other way. This book also sets out what will happen if someone knowingly evades tax, and gets caught.*

**Resident withholding tax on investments** (IR 279) April 1993

*An explanation of RWT for people who receive interest or dividends.*

**Retiring allowances and redundancy payments** (IR 277) April 1993

*An explanation of the tax treatment of these types of payments.*

**Self-employed or an employee?** (IR 186) April 1993

*Sets out Inland Revenue's tests for determining whether a person is a self-employed contractor or an employee. This determines what expenses the person can claim, and whether s/he must pay some ACC premiums.*

**Special tax codes** (IR 23G) January 1994

*Information about getting a special "flat rate" of tax deducted from your income, if the regular deduction rates don't suit your particular circumstances.*

**Stamp duties** (IR 665) June 1992

*Explains what duty is payable on transfers of real estate and some other transactions. Written for individual people rather than solicitors and legal firms.*

**Student Loans and Inland Revenue** (SL 1)

*A guide to your tax obligations if you've taken out a Student Loan.*

**Student Loan repayments - everything you need to know** (SL 2)

*A more in-depth guide to making student loan repayments.*

**Superannuitants and surcharge** (IR 259) January 1994

*A guide to the surcharge for national superannuitants who also have other income.*

**Tax facts for income-tested beneficiaries** (IR 40C) September 1992

*Vital information for anyone who receives an income-tested benefit and also has some other income.*

**Problem Resolution Service** (IR 287) November 1993

*An introduction to Inland Revenue's Problem Resolution Service. You can use this service if you've already used Inland Revenue's usual services to sort out a problem, without success.*

*list continues on page 20*

# List of Inland Revenue booklets

This list shows all of Inland Revenue's information booklets as at the date of this Tax Information Bulletin. There is also a brief explanation of what each booklet is about.

Some booklets could fall into more than one category, so you may wish to skim through the entire list and pick out the booklets that you need. You can get these booklets from any Inland Revenue office.

For production reasons, the TIB is always printed in a multiple of eight pages. We will include an update of this list at the back of the TIB whenever we have enough free pages.

## For people in business

**A guide to Inland Revenue audits** (IR 297) August 1992

*For business people and investors. It explains what is involved if you are audited by Inland Revenue; who is likely to be audited; your rights during and after the audit, and what happens once an audit is completed.*

**ACC premiums** 1993/94

*Explains the ACC employer premium, and gives the premium rates payable by employers and self-employed people. ACC publish this book.*

**Approved issuer levy** (IR 291A) August 1991

*For taxpayers who pay interest to overseas lenders. Explains how you can pay interest to overseas lenders without having to deduct NRWT.*

**Consolidation** (IR 4E) March 1993

*An explanation of the consolidation regime, which allows a group of companies to be treated as a single entity for tax purposes.*

**Employers' guide** (IR 184) 1993

*Explains the tax obligations of anyone who is employing staff, and explains how to meet these obligations. Anyone who registers as an employer with Inland Revenue will receive a copy of this booklet.*

**Entertainment expenses** (IR 268) April 1993

*Covers the tax treatment of business entertainment expenses, under the rules applying from 1 April 1993.*

**Fringe benefit tax guide** (IR 409) June 1992

*Explains fringe benefit tax obligations of anyone who is employing staff, or companies that have shareholder-employees. Anyone who registers as an employer with Inland Revenue will receive a copy of this booklet.*

**GST - do you need to register?** (GST 605) September 1992

*A basic introduction to goods and services tax, which will also tell you if you have to register for GST.*

**GST guide** (GST 600) 1994 Edition

*An in-depth guide which covers almost every aspect of GST. Everyone who registers for GST gets a copy of this booklet. It is quite expensive for us to get printed, so we ask that if you are only considering GST registration, you get the previous booklet on this list instead*

**Imputation** (IR 274) February 1990

*A guide to dividend imputation for New Zealand companies.*

**Inland Revenue employers' tax calendar**
(IR 24E) 1994

*A list of all the more common tax due dates that employers have to remember. If you have a balance date other than 31 March, you may find the full tax calendar (IR 24) more useful.*

**Inland Revenue tax calendar** (IR 24) May 1993

*A complete list of all the tax due dates. It covers everything from filing tax returns to the due dates for non-resident Student Loan repayments.*

**PAYE deduction tables**
- Four-weekly and monthly (IR 184Y) 1993
- Weekly and fortnightly (IR 184X) 1993

*Tables that tell employers the correct amount of PAYE to deduct from their employees' wages.*

**Qualifying companies** (IR 4PB) October 1992

*An explanation of the qualifying company regime, under which a small company with few shareholders can have special tax treatment of dividends, losses and capital gains.*

**Resident withholding tax on interest** (IR 283) March 1993
*A guide to RWT for people and institutions who pay interest.*

**Running a small business?** (IR 257) May 1992

*An introduction to the tax obligations involved in running your own business.*

**Student Loans - a guide for employers** (SL 4)
February 1993

*Tells employers what they'll have to do if any of their employees are repaying a student loan.*

**Surcharge deduction tables** (IR 184NS) 1993

*PAYE deduction tables for employers whose employees are having national super surcharge deducted from their wages.*

**Tax help for sprouting young businesses** (IR 257C)

*A promotional pamphlet for Inland Revenue's Small Business Tax Information Service.*

life. The seismic strengthening was an inseparable part of the expenditure and even if viewed separately, expenditure of $1.28 million on a building (and land) worth only $1.6 million indicated capital investment and not repairs. The expenditure was of a capital nature under section 106 and not the repair of those premises. In terms of the restrictions imposed by the former section 108, the repairs certainly went far beyond what would usually be expended in one year.

Alternatively, if the expenditure was classified as an "alteration" under the second proviso to section 108(1), the expenditure increased the capital value of the asset by more than the sum expended and it was not deductible.

**Comment:** We do not know if the taxpayer will be appealing this decision.

## Upcoming TIB articles

In the next few months we'll be releasing policy statements on these topics in the Tax Information Bulletin:

- When Inland Revenue can grant relief from payment of tax in cases of hardship
- Various statements on the qualifying company regime
- GST second-hand goods credit on property transactions
- National standard cost for livestock determination 1994
- Write-off of low-value assets - GST inclusive or exclusive
- Telephone rental deductions for businesses based at home
- GST and disbursements

We'll publish these statements as soon as we've finished consulting with commentators outside Inland Revenue.

## ACC Premiums booklet - correction about deductibility

On page 9 of the 1994/95 ACC Premiums booklet there is a mistake under the "deductibility" heading. The sentence which reads "Employers have no claims on earner premium as it is paid by their employees." is not entirely accurate.

Employees do bear the cost of earner premiums, because the premiums are deducted from their gross wages. However, employers can claim an income tax deduction for the amount of gross wages they pay.

Employers cannot claim a GST input tax credit for the earner premium because the individual employees bear the cost of the premium.

This correction agrees with the statement about earner premium on page 5 of last month's TIB.

*from page 15*

**Decision:** The TRA found that the partnership was not in the business of money lending. The partnership held a significant interest in each of the businesses to which it made loans. The loans were more in the nature of introduction of capital to those businesses and were not advances made at arm's length as part of a commercial money lending activity. The objectors did not satisfy the test of whether a person is a money lender proposed in *New Zealand Dairy Board v Webby* [1976] 1 NZLR 439. In particular, the number and regularity of the transactions did not point to the existence of a money lending business. Also, there was no suggestion of large inflows of funds and the need to invest those funds. The objectors did not advertise their activities to the general public as being money lenders. The losses claimed were therefore found to be not deductible.

On the second issue, the evidence did not support the objectors' contention that they bought the house for the purpose of development and on-sale at a profit. The TRA held that the purchase was not part of a pattern of trading activity and that the objectors bought the house for use as a private residence.

**Comment:** We do not know if the taxpayers will be appealing this decision.

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## Deduction for seismic strengthening costs

**Rating:** • •

**Case:** Colonial Motor Company Limited v Commissioner of Inland Revenue AP 76/92

**Act:** Income Tax Act 1976, section 106 & former section 108

**Keywords:** *Capital expenditure, alterations of assets*

**Summary:** The High Court found that the costs incurred by the taxpayer in the seismic strengthening of a building were not deductible for tax purposes.

**Facts:** The objector, Colonial Motor Company Limited, owns land and buildings in Courtenay Place, Wellington. The building was an earthquake risk and the City Council required its demolition or strengthening by 1988. The company decided to strengthen it and sought to deduct the costs from its assessable income.

The substantial nature of the undertaking is immediately apparent from comparing the value of the property (about $1.6 million) when the work commenced in 1984 with the sums expended over the next four years (totalling $5.7 million). The $5.7 million has been divided into three categories:

(1) Seismic strengthening

(2) Repairs

(3) Capital

As a result of the $5.7 million spent, the building was transformed from a warehouse, which was an earthquake risk and had to be demolished, into a sound commercial building with a 50 year life.

The objector sought to deduct only the seismic strengthening costs of $1.28 million, incurred over five tax years 1984 to 1988, from its assessable income. The Commissioner disallowed the deduction.

**Decision:** Justice Ellis found that the Commissioner had acted correctly in disallowing the deduction.

He looked at the total work undertaken on the building. While it was not the complete replacement of the building, it was the transformation of an unsound warehouse into a sound commercial building with a substantial revenue earning

# Legal decisions - case notes

This section of the Tax Information Bulletin sets out brief notes of recent tax decisions made by the Taxation Review Authority, the High Court, the Court of Appeal and the Privy Council.

We have given each case a rating as a reader guide to its potential importance.

• • • • • Important decision

• • • • Interesting issues considered

• • • Application of existing law

• • Routine

• Limited interest

We've given full references to each case, including the citation details where it has already been reported. Details of the relevant Act and section will help you to quickly identify the legislation at issue. Short case summaries and keywords deliver the bare essentials for busy readers. The notes also outline the principal facts and grounds for the decision. Where possible, we have indicated if an appeal will be forthcoming.

These case reviews do not set out Inland Revenue policy, nor do they represent our attitude to the decision. These are purely brief factual reviews of decisions for the general interest of our readers.

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## Whether in business of money lending; expenditure on property development

**Case:** TRA No 92/69, decision No 2/94

**Rating:** • •

**Act:** Income Tax Act 1976 - sections 104 and 106

**Keywords:** *Business of money lending, deductibility, property development expenses*

**Summary:** Loans made to businesses in which the lender had an interest were an introduction of capital to those businesses rather than the business of commercial money lending. The objectors purchased a house for use as a private residence and not as part of a trading activity. The objectors could not deduct expenditure relating to either activity.

**Facts:** The objectors were partners who maintained that they were in business as "investors" and that they were entitled to deduct certain items of expenditure. The first item was a loss on a loan to a company. The objectors claimed that they were in the business of money lending and that the loss was deductible.

The second item was expenditure on a property that the objectors claimed they purchased with the intention of developing and reselling at a profit. The objectors lived in the house for about 12 months.

The Commissioner considered that the partnership was not in the business of either money lending or property development and that neither item of expenditure was deductible.

*continued on page 16*

*from page 13*

Under Parts 11A and 11B of the Gaming Duties Act 1971, Internal Affairs and Inland Revenue can exchange the following information:

- The names and addresses of societies licensed under the Gaming and Lotteries Act 1977 to operate gaming machines:
- Details of licences cancelled or not renewed:
- Details of undeclared gaming machine profits identified during random audit activities.

# Estate and Gift Duties Act 1968

## Using government valuation of land for gift duty purposes

**Section 67 - Valuation of Property:** A donor who gifted some land asked what method of valuation is appropriate for gift duty purposes. He expects the government valuation to be greater than the actual value of the land.

Section 67 allows the Commissioner to value any property in any manner he thinks fit. Inland Revenue's policy is that land value must be determined by one of the following methods:

- By agreement between Inland Revenue and the donor. Valuation by agreement may be reached by using either of these values:
  - a private valuer's valuation
  - the gross sale price excluding any chattels, if the property has been sold in an arm's length transaction.
- By government valuation. Generally if the government valuation is more than six months old Inland Revenue will obtain a special valuation.

In this case, the taxpayer could seek an agreement with Inland Revenue to use a valuation other than the government valuation.

# Correction to earlier item

## Gifts qualifying for donation rebate

**Section 56A - Qualifying gifts:** In TIB Volume 5, No.8 (January 1994) we outlined the conditions a receipt for a donation must meet to qualify for the donations rebate. The item could have been misleading.

We failed to mention that a receipt must (of course) show the monetary amount of the donation.

We also said that Inland Revenue must be satisfied that the donation was made either as a gift or *as a payment of fees.* However, in most circumstances fees do not qualify for the donations rebate.

A fee or subscription will qualify for the donations rebate only if its payment does not give any membership rights or any other benefit.

## No input tax deduction after concessionary GST deregistration by associated person

**Section 20(3AB) - Application to associated person transactions:** A taxpayer who was registered for GST bought a car from his brother to use in his taxable activity. His brother had deregistered for GST in 1988 and in doing so had made a supply of goods and services to which section 5(3A) of the Act had applied. The taxpayer's accountant told him that he could not claim an input tax credit if he bought the car within five years of his brother's deregistration. The taxpayer asked if this advice was correct, and how he could find out the date of deregistration.

Section 5(3A) gave a concession to voluntarily registered persons and non-profit bodies which wanted to deregister. They still had to pay output tax on the deemed supply of goods and services that occurred on deregistration (section 5(3) of the Act), but they could claim input tax on the goods and services that they acquired before GST was introduced.

Under section 20(3AB) a registered person cannot claim an input tax credit on any goods or services acquired from an associated person, if the associated person has claimed a concession under section 5(3A) on those goods or services. This prohibition lasts for a period of 5 years after the associated person's deregistration. However, section 5(3A) only relates to goods and services which a registered person acquired before 30 September 1986. This means that:

- If the taxpayer's brother bought the car after 30 September 1986 it will not be within the scope of section 5(3A) and the taxpayer may claim an input tax deduction.
- If the taxpayer's brother bought the car before 30 September 1986 then sections 5(3A) and 20(3AB) will apply to prevent input tax deductions. For this reason the taxpayer should find out when his brother bought the car.

If the brother bought the car before 30 September 1986, the taxpayer will also need to know the date of his brother's deregistration. If the brother is unsure of this date, the taxpayer should give full details of the transaction to Inland Revenue and we will tell him whether he is eligible for an input tax deduction. (We can't tell the taxpayer the actual date of his brother's deregistration because of the secrecy provisions in the Inland Revenue Department Act 1974.)

In practical terms the section 5(3A) restriction will not have much effect from 1993 onwards as the five year periods begin to expire. Section 5(3A) supplies would generally have occurred in the period from 1 April 1988 to 30 September 1988. Registered persons had to request deregistration within that period to receive the concessionary treatment.

# Gaming Duties Act 1971

## Information exchanged between Inland Revenue and Internal Affairs

**Section 14A - Disclosure of information:** A gaming machine operator asked what information about gaming machine duty can be exchanged between Internal Affairs and Inland Revenue.

The Secretary of Internal Affairs and the Commissioner of Inland Revenue can exchange any information about the administration of the Gaming and Lotteries Act 1977, the Casino Control Act 1990, and Parts 11A and 11B of the Gaming Duties Act 1971.

*continued on page 14*

*from page 11*

***Advantages of six-monthly returns:***

- If you normally have to pay GST to Inland Revenue with your GST return, you'll only have to pay it every six months. This can give you a cash flow advantage.
- If it takes you less time to prepare one six-month return than to prepare three two-month returns, you will save time and money by filing returns six-monthly.

***Disadvantages of six-monthly returns:***

- If you normally receive GST refunds, you'll only receive a refund every six months, instead of every two months. This would be a cash flow disadvantage.
- You won't be making up a regular two-monthly summary of inputs and outputs. This summary can help you to monitor the financial position of your business.

Any person who files GST returns six-monthly must do both of these things:

1. As at the last day of every month, calculate whether the total taxable supplies have exceeded $250,000 in the last 12 month period
2. As at the first day of every month, make an estimated calculation of whether the total taxable supplies are likely to exceed $250,000 in the next 12 month period.

If the answer to either of these calculations is more than $250,000, the taxpayer must notify Inland Revenue within 21 days, and change to two-monthly (or one-monthly) return filing.

Note: Don't include sales from scaling down a business, ceasing business, or replacing the business' plant and capital assets in these calculations.

## GST input deduction - private launch later used in taxable activity

**Section 21(5) - Deduction:** A taxpayer built his own launch which took several years to complete. He then decided to use the launch in his taxable activity, and asked how he should treat the incorporation of the launch into the taxable activity for GST purposes.

Section 21(5) allows an input tax deduction for GST paid on the launch. The deduction is calculated at one ninth of the ***lesser*** of the GST inclusive cost, or the market value at the date of change of use.

For example, if the cost of building the launch was $4,567, and the market value was $7,890 at the date of change of use, the input deduction would be calculated on one ninth of the cost of building the launch, as this is less than the market value.

If the taxpayer stops using the launch in his taxable activity at a later date, the output tax adjustment required under sections 5(3) and 10(8) will also be based on the lesser of market value at that time, or cost.

- The compliance costs of section 64C to the issuer
- Whether there is a material difference between the amount calculated under section 64C and the determination.

To date the Commissioner has issued only one determination under section 64C(6). This is Determination G15, which applies to small debtors being issuers who meet all of these conditions:

- They are natural persons or partnerships (not trustees)
- They have total liabilities under certain financial arrangements that are no more than $200,000
- They either hold no financial arrangements at the end of the year, ***or*** are cash basis holders for all financial arrangements held at the end of the income year (except financial arrangements dealt with by the Commissioner under section 64D(2)(b)).

Other taxpayers may apply for determinations under section 64C. Such applications must address the points the Commissioner must consider (as listed above), and be in a form that facilitates a quick response. The applications need not comply with the Income Tax (Determinations) Regulations 1987 because the determinations are not of the same nature as those made under section 64E(1).

## Cheque received but not banked - when assessable

**Section 75 - Income credited in account or otherwise dealt with:** On 27 March 1993 a plumber received a cheque to pay for services he'd provided. However, he did not bank the cheque until 5 April 1994, which is in the following income year. He asked when the income is assessable - in the 1993 year when he performed the services and received the cheque, or in the 1994 year when the cheque was cashed.

The receipt of the cheque constitutes payment of the amount outstanding, regardless of whether the cheque was banked during the same income year. Income is assessable in the year it is derived. This income was derived in the 1993 income year, so it is assessable in that year.

Business taxpayers must include any trade debts which arise during an income year in that year's assessable income, even if those debts aren't paid by the end of that year. The accrual (or earnings) method of tax accounting recognises that business income is represented by trading profits, not simply by receipts. The accrual accounting method treats expenses in a similar manner.

# Goods and Services Tax Act 1985

## Filing GST returns six-monthly

**Section 15 - Taxable periods:** A taxpayer asked about the advantages and disadvantages of filing GST returns every six months, instead of every two months. This taxpayer's taxable supplies did not exceed $250,000 in any 12 month period, so he was eligible to make six-monthly GST Returns.

There are a number of advantages and disadvantages in filing six-monthly returns instead of two-monthly returns. If you're considering changing to or from six-monthly returns, it's important that you weigh up all of the following points:

*continued on page 12*

## Time limit for refund of overpaid tax

**Section 409 - Refund of excess tax:** A taxpayer included non-taxable income in his tax returns over many years. When Inland Revenue discovered this error, we issued amended assessments and refunded most of the overpaid tax. The taxpayer asked why some overpaid tax had not been refunded.

By law, the Commissioner cannot refund excess tax after eight years have expired from the last day in the year in which the assessment was made. This time limit can only be extended when a taxpayer asks for a refund before the eight year period has expired.

Here is the sequence of events in this particular case:

| | |
|---|---|
| 1984 assessment issued on: | 2 August 1984 |
| Last day of that assessment year: | 31 March 1985 |
| Eight years from 31 March 1985: | 31 March 1993 |

The error was discovered in July 1993, so Inland Revenue could not issue refunds for 1984 or earlier years.

## Accrual income and foreign exchange variations

**Section 64B to 64M - Accrual Treatment of Income and Expenditure:** A New Zealand resident individual owned 90 day bills denominated in United States currency. He asked about the tax implications of these bills.

***Example:***

9/5/93 A 90 day bill was purchased for US$20,000.00 (NZ$37,071.36).

7/8/93 The bill matured, and its value was US$20,500.00 (NZ$37,683.82) This is based on a 10 % interest rate, so the interest amounted to US$500.00 or NZ$919.11.

This was the only financial arrangement the taxpayer held during the year, so he was a cash basis holder under section 64D(1) of the Income Tax Act 1976. His assessable income for the year is therefore the amount of the base price adjustment calculated under section 64F(3) of the Act.

The NZ assessable income was NZ$612.46 ($37,683.82 less $37,071.36), not NZ$919.11. The base price adjustment calculation takes into account exchange rate variations between purchase and maturity dates.

## Determinations under section 64C(6)

**Section 64C(6) - Commissioner to determine non-compliance:** A taxpayer asked whether Inland Revenue had made any determinations under section 64C(6).

Section 63C(6) relates to the determination of income or expenditure for a holder or an issuer of a financial arrangement. It permits the Commissioner to make a determination exempting any issuer or class of issuers from complying with the requirements of section 64C of the Act. Issuers are generally debtors under financial arrangements.

The Commissioner must consider all of these things when exercising this discretion under section 64C:

- The nature and amount of expenditure incurred or income derived for financial arrangements of that class

- Copies of all relevant documents. If the documents are lengthy and contain irrelevant parts, the applicant may attach copies of the relevant extracts.
- Written submissions.
- Other details necessary for a ready understanding of the determination.

A fee of $100 plus $90 per hour spent processing the application (Inclusive of GST) applies. Inland Revenue can waive all or part of the hourly fee, if there are exceptional circumstances.

The application for determination should be made to:

The Director
Rulings
Inland Revenue Department
PO Box 2198
Wellington

## Non-profit body - financial gain to members

**Section 61(34) - Non-profit body:** The treasurer of a social club asked for confirmation of the club's non-profit body status.

The club is exempt from tax on income received up to $1,000, but it will lose this exemption if it can distribute its income to club members or to any associated person. To qualify for the exemption, there must be evidence that the club cannot be carried on for the profit or gain of any member. This may include a clause in the club's constitution stating that no benefit be passed to any member.

The club employed a member as a carpenter on several projects. It was concerned that the employment of a club member may be seen to be a distribution of the club's income to that member.

The member was paid a reasonable amount for the carpentry work, so the payment did not jeopardise the club's non-profit status.

Some other acceptable payments to members include:

- A return of subscriptions, e.g. where a social club subsidises a Christmas function.
- Interest paid to a member on a loan at normal commercial rates.

## Access to herd scheme

**Section 86D - Herd scheme for specified livestock:** A farmer asked if he could change his valuation method from the national standard cost scheme to the herd scheme. He intended to have half his dairy cows and breeding bulls valued under the herd scheme.

Where a farmer has elected the herd scheme for any type of livestock, and actually has livestock of that type valued under the scheme, section 86D(6) of the Act requires that all male breeding livestock of that type be valued under the herd scheme.

The farmer in this case may value half of his dairy cows under the herd scheme, but he must also value all of his breeding bulls under that scheme. However, if the bulls are high-priced livestock, their value will be determined under section 86I of the Act, not under section 86D.

# Questions we've been asked

This section of the Tax Information Bulletin sets out the answers to some day-to-day questions that people have asked. We have published these as they may be of general interest to readers.

These items are based on letters we've received. A general similarity to items in this package will not necessarily lead to the same tax result. Each case will depend on its own facts.

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# Income Tax Act 1976

## Applying for an accrual determination under section 64E

**Section 64E - Determinations:** A taxpayer was interested in submitting an application for an accrual determination under section 64E. He asked what initial details the Commissioner required.

The Income Tax (Determinations) Regulations 1987 set out the initial details a taxpayer must include in an application for a determination. These are:

- A draft of the determination. This draft is to include an introduction to explain the purpose of the proposed determination, reference to the sections concerned, the scope of the determination, the principle involved, interpretation of any specialised terms used, the method of applying the principle, and one or more examples.
- The name of the applicant. An applicant who wishes to remain anonymous should notify the Commissioner and provide an anonymous draft version of the determination.

us target our audit activities more effectively. We will be maintaining audit coverage in all sectors as well as focusing our efforts on areas where they are most needed. This will improve Inland Revenue's ability to ensure that all taxpayers pay their fair share of tax.

The modernisation of Taxpayer Audit is part of an extensive programme to review and modernise all of Inland Revenue's core business systems. It follows on from the modernisation of the way we process tax returns and payments, and police return filing and debt collection. Inland Revenue is committed to administering the tax system as effectively and efficiently as possible. All of our recent changes make a major contribution to improving our performance while maintaining a taxpayer-oriented service.

# Maori Purposes Act 1993
# Ngati Rarua-Atiawa Iwi Trust Empowering Act 1993
## Recent legislation with implications for the Inland Revenue Acts

The Maori Purposes Act 1993 and the Ngati Rarua-Atiawa Iwi Trust Empowering Act 1993 (a private Act) were passed by Parliament recently. This article sets out the tax implications of each of these Acts.

### Maori Purposes Act 1993

The Maori Purposes Act 1993 provides for the transfer of certain assets and property from the Crown to mana authorities.

The mana enterprises scheme was set up to provide financial support to enterprises creating employment for Maori. The scheme was administered by mana authorities.

Broadly speaking, under the Maori Purposes Act 1993, all money provided by the Crown to mana authorities under the mana contracts and mana enterprises schemes, and assets purchased with that money (mostly loans), become the property of the mana authorities and not the Crown.

Mana authorities are defined in the Maori Purposes Act 1993 as any person to whom or for whom the Crown has disbursed money under the mana enterprises scheme. It includes any person appointed as an agent of the Crown under any mana contract.

Section 10 of the Maori Purposes Act 1993 provides that, for the purposes of the Inland Revenue Acts, where loans are transferred to mana authorities, the mana authorities are deemed to have acquired the loans for an amount equal to the sum of money owing and repaid under the loans. This means that there will be no accruals rules or gift duty implications on the transfer of the loan assets to mana authorities.

Section 11 of the Maori Purposes Act 1993 provides that there are no GST consequences from this transfer of assets. This means the transfer is not subject to GST.

The Maori Purposes Act 1993 received the Royal assent on 28 September 1993 and came into force on that day.

### Ngati Rarua-Atiawa Iwi Trust Empowering Act 1993 (Private Act)

The Ngati Rarua-Atiawa Iwi Trust Empowering Act 1993 vests assets of the Whakarewa School Trust Board in a trust for the descendants of the original Maori owners of the assets. No GST, conveyance duty or gift duty is payable on this transfer.

In 1853, certain land in the Nelson area was vested by the Crown in the Bishop of New Zealand of the Anglican Church to establish a school. No compensation was paid to the Maori owners of the land.

The Whakarewa School Trust Board administered the original land assets and other assets acquired after the original grant of the land.

The Synod of the Diocese of Nelson resolved to vest the land, and assets acquired from the land, in a charitable trust for the benefit of the descendants of the original Maori owners. The Ngati Rarua-Atiawa Iwi Trust Empowering Act 1993 vests the assets of the Whakarewa School Trust Board in the Ngati Rarua-Atiawa Iwi Trust (a charitable trust).

The Act also provides for the assets held by the Whakarewa School Trust Board that were acquired after the original grant to be vested in the Nelson Diocesan Trust Board for charitable purposes.

Under section 4 of the Ngati Rarua-Atiawa Iwi Trust Empowering Act 1993, the Ngati Rarua-Atiawa Iwi Trust is charitable for all purposes at law. There are therefore no income tax consequences as a result of the transfer of assets to the trust. Similarly, section 11 of the Act deems the assets vested in the Nelson Diocesan Trust Board to be vested for charitable purposes.

Section 7 of the Act provides that no GST, conveyance duty or gift duty is payable on the vesting of the assets of the Whakarewa School Trust Board to the Ngati Rarua-Atiawa Iwi Trust.

Section 13 provides that no GST, conveyance duty or gift duty is payable on the vesting of the assets of the Whakarewa School Trust Board to the Nelson Diocesan Trust Board.

The Ngati Rarua-Atiawa Iwi Trust Empowering Act 1993 came into force on 1 October 1993.

*from page 5*

Casual workers are liable to pay their own ACC earner premium (which provides cover for any non-work related accident) and employer premium (which provides cover for any work related accident) on all withholding income that they receive. These premiums are calculated in the worker's tax return at the end of the year, and are due for payment by the following 7 February.

Like ordinary employees, casual agricultural workers are not entitled to claim a deduction for expenditure incurred in performing their employment duties (section 105(1)(c) of the Income Tax Act 1976).

Any worker who is an employee must complete an IR 12 and have PAYE deducted. The employer is liable for the ACC employer premiums and must deduct earner premiums from payments made to employees.

### Other employer responsibilities

- When employers send in their PAYE deductions to Inland Revenue, they must also send a schedule of all workers whom they start or stop employing. These schedules show each employee's name and IRD number, and the date that he or she started or stopped working for the employer.

  For casual agricultural workers, employers should include starting details when the worker is first taken on. Employers should show a finish date for a casual agricultural worker only when the employer considers that the worker's employment is unlikely to continue.
- At the end of the year employers must file a reconciliation statement to account for all salaries, wages, withholding payments, allowances and other emoluments that they've paid out, and the PAYE or withholding tax deducted from those payments.

### Primary and secondary school children

Primary and secondary school children workers who expect to earn less than $1,040 in a year ($20 a week) do not have to complete an IR 12 or an IR 13 or have PAYE or withholding deductions made. Employers do not need to deduct any ACC premium.

Children who expect to earn more than $1,040 are treated in the same way for tax purposes as other employees and casual workers. Children who earn more than $1,040 and who receive withholding payments will be liable for the ACC premiums on those payments when they file their tax returns.

### University students

Employers should deduct PAYE or withholding tax in the ordinary way from the wages of a tertiary student unless the student produces a special tax code certificate as authority to the employer to make no tax deductions or to deduct tax at less than the normal rate.

***Example***

John owns an orchard in Hastings. He hires a team of university students to pick apples during their two week holiday, and pays them at an hourly rate. None of the students produce a special tax code certificate.

During the two week period the students are unable to work on three days because of rain. John does not pay them for the days that they do not work.

The students are not casual workers because they are employed for more than a week. They should each complete an IR 12 and John should deduct PAYE according to the tax code established. John is liable for the ACC employer premium on those earnings when he files his ACC Employer Premium Calculation Sheet (IR 68A) in May.

When the students' employment has finished, John estimates that there is another two days picking left. He hires a couple of workers to finish the job and pays them at the end of the two days on a per-bushel basis. These workers are casual employees, and John should tax them at the withholding rate. The workers must complete an IR 13. They are liable to pay their own ACC premiums when they file their end-of-year tax return.

This topic is also covered on page 44 of the 1994 edition of Inland Revenue's "Employers' Guide" (IR 184).

# Inland Revenue Audit restructured

The work of Inland Revenue's Taxpayer Audit programme will now be more targeted and co-ordinated, as a result of the programme's modernisation.

The new structure went live on 1 March 1994. It is made up of these four segments, each of which is focused on a specific taxpayer group:

- **Non-Business Audit** - deals with salary and wage earners, and investment income earners
- **Business Audit** - for businesses with an annual turnover of less than $1.5 million
- **Medium Business Audit** - for businesses with an annual turnover between $1.5 million and $100 million
- **Corporates Unit** - deals with businesses and groups whose annual turnover is more than $100 million, also with government departments, state-owned enterprises, local authorities and other specified industries.

This new structure will benefit people who are selected for audit, as they will be less likely to have multiple audits for different tax types.

There is also a new Research and Risk Unit, and a new computerised case selection and management information system. Together with new audit techniques which gather information about the compliance history of a particular industry or profession, we expect these to help

# Distinction between casual agricultural workers and seasonal employees

## Summary

This article restates Inland Revenue's current policy on when a seasonal worker qualifies as a "casual agricultural worker", and when he or she is a salary and wage earner. This is not a new policy.

We have received a number of enquiries about the distinction between seasonal agricultural workers who qualify as casual labour and those who do not. The distinction is important as casual agricultural workers are taxed at 15 cents in the dollar under the Income Tax (Withholding Payments) Regulations 1979, but non-casual workers must have PAYE deducted from their earnings. The distinction also affects whether the responsibility and liability for ACC premiums lies with the employer or the employee.

## Policy

A "casual agricultural worker" is a person hired as a casual seasonal worker solely to perform seasonal agricultural, horticultural, orchard, tobacco farming, market gardening or nursery work, or other similar seasonal work (Income Tax (Withholding Payments) Regulations 1979, regulation 2).

Inland Revenue's policy is that a person is *not* a casual worker if he or she is employed in any of these circumstances:

· for some other purpose in addition to seasonal work of the types listed above

· on a part-time basis by two or more farmers throughout the year

· not on a daily basis, but for a continuous period of more than a week.

An employer can make the distinction between a 'casual' seasonal worker and other seasonal agricultural employees at the time he or she hires the worker:

· If the worker is hired to do work that will last a week or more (or the whole season) he or she is an employee and the employer should deduct PAYE. This will be the case even if the worker only gets paid for the days that he or she works (rather than every day as is the case with a salary earner) or if the worker is employed on a part-time basis for a few days each week. It makes no difference whether the employer pays the worker on a contractual rate (e.g. per box or punnet) or an hourly rate. Like salary and wage earners, these seasonal workers will generally be paid weekly or fortnightly.

· If the worker turns up at the employer's business looking for work (i.e. the employer does not guarantee work in advance), and is employed to do a job that lasts a day or two, he or she will be a casual worker. Casual workers will usually be paid a contract rate and receive payment at the end of the day(s) they work.

Once the casual employee has completed the job, if he or she is kept on to carry out another short-term (less than a week) job, he or she is still a casual worker. The casual status will not change even if the person ends up working for a continuous period of more than a week. The work is still on a day to day basis and is not guaranteed to last more than a few days.

However, if the worker is originally employed to do a job that will last a day or two, but is then kept on on the basis that he or she is employed for a period of longer than a week, he or she ceases to be a casual worker. The worker's status as an employee commences at the beginning of the longer period of employment.

### *Example 1*

A worker is employed to do a job which will last two days. On the afternoon of the second day he agrees with his employer to perform another task for the employer which will last a month. The task will start the next day.

The worker's status changes to that of an employee from the time that he and the employer agree that he will be employed for the month period (i.e. on the afternoon of day two). This is because they share an intention that the worker's employment will last, from that time, for more than a week.

### *Example 2*

In this case the same facts occur as are outlined in Example 1 except that the employer and the worker agree that the task will start three weeks after the end of the worker's current two day job. The worker's status does not change to that of an employee until the time that the second, month-long job commences. He has the status of a "casual worker" during the first two day period, as the intention during this period is that he will not be employed continuously for more than a week.

When the worker's status changes from casual worker to employee he should complete an IR 12, and the employer should start deducting PAYE according to the tax code established.

## Effects of Policy

Casual workers are subject to withholding tax deductions. The rate of withholding deduction on payments made to casual agricultural workers is 15 cents in the dollar. These workers must complete an IR 13 withholding tax declaration form. If an IR 13 is not completed the employer must deduct withholding tax at the no-declaration rate of 30 cents in the dollar.

*continued on page 6*

# Trade-in cars - valuation by franchise motor vehicle dealers

This article explains how franchise motor vehicle dealers or master agents should apply the approved formula for valuing trade-in cars.

Under section 85(4) and (5) of the Income Tax Act 1976, taxpayers can use any of these options to value trading stock (including trade-in cars):

- cost price
- market selling price
- replacement price
- special values approved by the Commissioner because of obsolescence or other special circumstances

## Formula for trade-in cars

In PIB 82 (December 1974) Inland Revenue approved this formula for the valuation of trade-in cars by franchise motor vehicle dealers or master agents:

| Time on the floor | Value |
|---|---|
| less than 1 month | Value at cost plus reconditioning expenses. |
| After 1 month | Value at cost plus reconditioning expenses less 10 percent |
| After 2 months | Value at cost plus reconditioning expenses less 20 percent |
| After 3 months | Value at cost plus reconditioning expenses less 30 percent |
| After 4 months or longer | Value at cost plus reconditioning expenses less 40 percent |

Since publishing this formula, we've found that some franchise motor vehicle dealers or motor agents are incorrectly valuing their stock of trade-in cars. If a dealer considers that a trade-in car has been traded in at too high a figure in order to secure the sale of a new vehicle, the trade in price has been reduced for stock valuation purposes by the amount of the "overtrade". From this reduced figure, some dealers have then made a deduction according to the percentages in the above formula.

## Application of existing policy

If the value of a trade-in car has been reduced by the amount of an overtrade for stock valuation purchases, the resulting value is the replacement price. Dealers may not then deduct the percentages in the above formula from the replacement value so calculated.

Dealers may only deduct the percentages in the above formula from the actual cost price of a trade-in vehicle.

Note that the above formula may only be used by franchise motor vehicle dealers and master agents. It is not available to other motor vehicle dealers.

# Financial service fees

## Deductibility under sections 104 and 106(1)(a), Income Tax Act 1976

Whether financial service fees are deductible has become a topical issue recently. "Financial service fees" are fees that financial advisers charge for reviewing, altering and managing a client's investment portfolio.

There are presently several Cases Stated which are awaiting Taxation Review Authority hearings. However, because of the importance of this issue, Inland Revenue is currently preparing a policy statement which we will publish in the near future. We will consult with recognised industry groups before we publish this policy.

In the meantime, we will maintain our current practice regarding these fees. This position is as follows:

***Review or planning fees*** are paid for an initial review of an investor's existing portfolio. We consider this expenditure to be a "one-off" cost that involves a review of the efficiency of the taxpayer's investment portfolio (which is a capital asset). We consider that these fees are therefore non-deductible under section 106(1)(a).

***Implementation fees*** are paid for services involving the reorganisation of an investor's investment structure so as to ensure that the returns from the investment portfolio are maximised. We consider that these fees are also a capital expense, and therefore non-deductible under section 106(1)(a).

Specifically, this expenditure is incurred in altering the investor's income-earning structure, and has the hallmarks of brokerage. This expense is also a "one-off" capital expense that alters the capital structure from which a taxpayer derives assessable income.

The ***monitoring service*** involves the ongoing management of the investment portfolio so as to ensure that it continues to maximise the investor's return. We consider that these fees are revenue expenses incurred in managing the portfolio, so they are deductible under section 104.

Include as much relevant information as possible with your application. The type of information we will require is set out in the application form for a provisional rate of depreciation (IR 260B). Note that an application for a review of a general rate is not covered by the Income Tax (Depreciation Determinations) Regulations 1993, so no fees are payable.

Taxpayers should apply for a special rate where their particular circumstances warrant setting a rate different from the general rate set by the Commissioner. A provisional rate should be applied for where no applicable general rate has been set.

## Application for a higher maximum pooling value

**Question:** If a taxpayer applies to the Commissioner for a higher pooling value and the Commissioner makes a determination, from which income year can that determination be applied?

**Answer:** In general the Commissioner will apply a determination from the income year in which the application was made. However, Inland Revenue will consider applications for the income year that has immediately finished. In this situation, taxpayers should apply to Inland Revenue for the determination as soon as possible after the end of the financial year. This is to give Inland Revenue time to process the application and to allow the taxpayer time to prepare financial statements and file a tax return by the due date.

# Fences - depreciation

The depreciation rate for fences acquired on or after 1 April 1993 has been amended. The rate is now 9.5% diminishing value, or 6.5% straight line equivalent, and it applies to fences acquired on or after 1 April 1993.

The new rate is set by Determination DEP5: Tax Depreciation Rates General Determination Number 5, which is reproduced below. This determination effectively corrects an error in Determination DEP1 (published in the appendix to TIB Volume Four, No.9 - April 1993), by setting the same rate for fences in the "building fit-out" asset category as in the "building" asset category.

## Determination DEP5

This determination may be cited as "Determination DEP5: Tax Depreciation Rates General Determination Number 5".

### 1. Application

This determination shall apply to the asset class "Fences" under the "Building Fit-out" asset category where the fence is acquired on or after 1 April 1993.

### 2. Determination

Under section 108C of the Income Tax Act 1976 I have determined the following basic economic depreciation rate:

Determination DEP1 (as amended) is further amended by replacing the details in the asset class "Fences" in the asset category "Building Fit-out" with the following details -

| | |
|---|---|
| Estimated Useful Life (years) | 20 |
| DV Banded Depn Rate (%) | 9.5 |
| SL Equiv Banded Depn Rate (%) | 6.5 |

### 3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in section 107A of the Income Tax Act 1976.

This determination is signed by me on the 28th day of February 1994.

Murray McClennan
Manager (Rulings)
Head Office
Inland Revenue Department

## FBT - prescribed interest rate reduced

The prescribed rate of interest used to calculate the fringe benefit value of low interest employment-related loans has been lowered to 7.7% for the quarter starting on 1 January 1994. This rate will apply to all subsequent quarters unless it requires subsequent revision. The new rate is a reflection of the reduced market interest rates during the quarter.

The prescribed rate was previously 7.8% for the quarter starting on 1 October 1993.

*from page 1*
section 428. Taxpayers must keep sufficient information to substantiate their depreciation claims and any loss or depreciation recovered on disposal of the depreciable property. However, there is now no requirement for keeping double entry accounts.

## Two and three shift plant and machinery acquired before 1 April 1993

**Question:** What rates apply to plant and machinery used in two and three shifts, if the machinery was acquired before 1 April 1993?

**Answer:** The rates for plant and machinery operating 16-24 hours per day are set out in the appendix to TIB Volume Four, No.9 (April 1993), on page 19 under the heading "Plant and Machinery - except elsewhere specified". Generally, manufacturing plant and machinery which is operating 16-24 hours per day will qualify for an additional 5% DV. The following note also appears in the TIB appendix:

*"NOTE: Assets other than manufacturing plant and machinery designed and constructed to operate 16-24 hours per day DO NOT qualify for the increased rates".*

The same statement also appears in the depreciation booklet IR 260 (May 1991). However, this statement is not correct. It should read:

***"NOTE: Manufacturing plant and machinery designed and constructed to operate 16-24 hours per day and assets other than manufacturing plant and machinery DO NOT qualify for the increased rates."***

Inland Revenue will not alter any assessment for periods up until the end of the 1992/93 income year where the taxpayer relied on the incorrect statement. Further, we will not alter the 1993/94 assessments of any taxpayers with early balance dates who have already filed their 1994 returns.

## Assets which were previously allowed to be written off

**Question:** Does the Inland Revenue's previous practice of allowing certain taxpayers to write off low-cost assets constitute a "pre-1993 depreciation rate" for the purposes of section 108D of the Income Tax Act 1976?

**Answer:** Inland Revenue previously allowed certain taxpayers to write off the cost of low cost assets in the year of acquisition. The levels of write off varied but they were usually between $200 and $500. We have been asked whether such a practice can be regarded as a "pre-1993 depreciation rate" of 100% for the purposes of section 108D. If it can, taxpayers would have the option of using such a rate for property acquired before the end of the 1994-95 income year.

Inland Revenue does not consider that a "depreciation rate" has been set in these cases. We allowed taxpayers to write off these low cost assets as revenue expenditure. Taxpayers will have these three options:

- Writing the asset off if it cost less than $200
- Pooling the asset if its value is less than $2,000
- Depreciating the asset at the rates specified in the appendix to TIB Volume 4, No.9.

## Taxpayers with non-standard balance dates

**Question:** Do taxpayers who have a 30 June balance date and have acquired assets between 1 April 1993 and 30 June 1993 have the option of using the new rates of depreciation, and how many months depreciation can be claimed?

**Answer:** Taxpayers with late balance dates have the option of depreciating assets acquired after 1 April 1993 at the new economic rates. The economic rate provisions of the regime apply from 1 April 1993 regardless of the taxpayer's balance date.

The other provisions of the regime generally do not apply until the 1993/94 income year, so the depreciation does not have to be claimed on a monthly basis. This means that if a taxpayer acquired an asset after 1 April 1993 but before the end of the 1992/93 income year, the asset can be depreciated using the previous six month rule; assets owned for less than six months are eligible for six months' depreciation.

The opposite applies for early balance date taxpayers. Although the provisions of the regime generally apply from the 1993/94 income year the economic rate provisions do not apply until 1 April 1993. Therefore, assets acquired in a taxpayer's 1993/94 income year but before 1 April 1993 can be depreciated at the old depreciation rates or the interim rates, but depreciation must be claimed on a monthly basis.

## Review of general economic depreciation rates

**Question:** Can a taxpayer or group of taxpayers ask Inland Revenue to review the depreciation rate set for an asset class or asset classes?

**Answer:** Yes. Although there is nothing specific in the depreciation legislation that allows a taxpayer to apply to the Commissioner for a review of a general depreciation rate (as opposed to a special or provisional rate of depreciation) the Commissioner is under an obligation to ensure that the general rates set are correct. Therefore, Inland Revenue will review general rates of depreciation if requested. If you wish to apply for a review of a general rate, write to:

The Manager (Rulings)
Inland Revenue Department
PO Box 2198
Wellington

# Miscellaneous depreciation issues - questions and answers

## Pooling

**Question:** Can an item which was previously depreciated separately be included in the opening value of a "pool" for an income year?

**Answer:** It is arguable whether an item that was previously depreciated separately can be included in the opening value of a pool. If such an item could not be included in the pool's opening value, then it would effectively only obtain six months' depreciation (because the adjusted tax value of the pool is the average of the pool's opening and closing values). This is particularly relevant for the 93/94 income year, when the pooling provisions first applied.

Although this issue is arguable, Inland Revenue takes into account the purpose of pool depreciation, and considers that items previously accounted for separately can be included in the opening value of a pool. The purpose of the pool depreciation provisions was to reduce the compliance costs of maintaining depreciation records for relatively low-value assets. It was not meant to deprive taxpayers of a deduction for depreciation in years where the property is first pooled.

Inland Revenue considers that there is no requirement to make the decision to include an item in a pool at the beginning of the income year. Under section 108B a taxpayer elects to use the pool method of depreciation by applying that pool method to an item of depreciable property in that year's tax return.

***Example***

Corporate Giant Limited has over 500 desks on which it has claimed depreciation in the past. All the desks have individual adjusted tax values of less than $2,000 at the beginning of the 93/94 income year, and their combined value is $14,550.

Corporate Giant Ltd also purchased 40 new desks in October 1993 for $400 each. It decides to create a pool for its desks when it prepares its tax return for the 1993/94 income year, and makes the election in that year's tax return.

Based on the above interpretation the pool depreciation for the 93/94 income year will be

| | |
|---|---|
| Opening value of pool | $14,550 |
| Add purchases | $16,000 |
| Closing value of pool | $30,550 |

$$\text{Pool depreciation} = 12\% \times \frac{14{,}550 + 30{,}550}{2} \times \frac{12}{12}$$

$$= \$2{,}706$$

## Property written off under sec 108K

**Question:** When will the Commissioner exercise his powers under section 108K to allow a deduction for property that can no longer be used, and when should a taxpayer apply for such a deduction?

**Answer:** There is some confusion about when this section applies. Section 108K allows taxpayers to deduct the adjusted tax value of depreciable property where that property is no longer usable. Inland Revenue considers that section 108K will only apply where a deduction for that asset is not allowable under section 117.

Section 117 deals with the tax treatment of a gain or loss from disposing of depreciable property. A deduction is only available under section 117 where the item of depreciable property is disposed of. Section 108K only applies where the depreciable property has not been disposed of. A taxpayer who has retained property that can no longer be used will need to apply to the Commissioner to write the property off.

The legislation does not set a time frame for making the application. Inland Revenue will accept applications at any time after the date from which the property can no longer be used. In normal circumstances, we would expect taxpayers to apply within the period in which a return must be filed for that income year. When we issue the determination, it will be effective in the year that the property is no longer used by the taxpayer.

When considering an application, Inland Revenue must be satisfied about these things:

- that the taxpayer is no longer using the property in a business or to produce assessable income
- that the costs of disposing of the property would exceed any consideration that could be gained from disposing of it.

Inland Revenue will also consider whether the property could still be used in a business or to produce assessable income.

## Record keeping and double entry accounts

**Question:** What records must be kept for the purposes of the new depreciation regime?

**Answer:** The old section 108(2) allowed the Commissioner to refuse to allow any deduction for depreciation if a taxpayer had not kept complete and satisfactory accounts. Under this section Inland Revenue generally required taxpayers to keep double entry accounts.

The new depreciation regime has no specific provision about keeping records to substantiate depreciation claims. Therefore, the records that must be kept come under the general provisions of the Act, namely

*continued on page 2*