

Ross Melville PKF's global ties a powerful resource

News and views from
Ross Melville PKF

The advantages and benefits to Ross Melville PKF and its clients, through the firm's unique global business ties, were clearly evident during two cross-Tasman conferences within the group during this quarter.

The New Zealand and Australian PKF Annual Partners' Conference in Sydney during May and the Business Advisory Services Conference in Auckland in July are a powerful resource for both the firm and its clients.

Ross Melville PKF partner, Jugdis Parbhu, says while New Zealand is often the country chosen to trial new products or services because of the small size of the local market, Australia is often where emerging trends, techniques and technology that will impact New Zealand first show up.

"At both the Sydney and Auckland conferences we are able to share ideas, information, technologies and also strengthen trans-Tasman ties."

The PKF Annual Partners' Conference is focussed on the firm, the specialities of the various partners and also on the organisation – where it is going locally (Australasia), in the Asia Pacific and internationally.

"The conference dealt more with ownership type challenges for us as a business, such as succession planning and getting to understand the nature of the clients our Australian counterparts have.

"By building relationships with our counterparts across the Tasman we facilitate better referrals. If we have a client who needs Australian advice, we can be very specific about referring them to the best person for the job within our group.

"Very often, if one of our clients is expanding to overseas markets they begin with Australia because of our similarities. We are able to assess their offering and together with our counterparts give them the best possible advice – right down to the best place to locate their offices," says Jugdis.

The group also uses common systems and protocols; so transferring confidential information, file notes and records is a smooth and easy process.

The Business Advisory Services (BAS) Conference is more focussed away from audit and high level tax planning and concentrates on such positive business support matters as business structures (including use of trusts), business diagnostics, business plans (including forecasting models), etc – and involves both the partners and managers within the group.

"In addition to being a team building conference between managers and partners, there are many technical sessions on building both Ross Melville PKF's business and client service.

"New Zealand and Australia are increasingly becoming one market for many clients. We have much in common, but the Australian market is four times our size – so it's a good launch pad for global business out of New Zealand," says Jugdis.

Above picture, Jugdis Parbhu of Ross Melville PKF

Short-sighted business predictions in history

■ "I think there is a world market for maybe five computers."

– *Thomas Watson, Chairman of IBM, 1943*

■ "I have travelled the length and breadth of this country and talked with the best people, and I can assure you that data processing is a fad that won't last out the year."

– *The editor in charge of business books for Prentice Hall, 1957*

■ "Who the hell wants to hear actors talk?"

– *H.M. Warner, Warner Brothers, 1927.*

■ "This 'telephone' has too many shortcomings to be seriously considered as a means of communication. The device is inherently of no value to us." – *Western Union internal memo, 1876.*

■ "The concept is interesting and well-formed, but in order to earn better than a 'C,' the idea must be feasible." – *A Yale University management professor in response to Fred Smith's paper proposing reliable overnight delivery service (Smith went on to found Federal Express Corp.)*

Door firmly shut on higher depreciation for rental property components

Residential property owners will no longer be allowed to claim depreciation on components of a building – such as electrical wiring, plumbing and internal walls – under the higher depreciation rates listed under the ‘Building fit out’ asset category.

Deputy Commissioner for Inland Revenue, Naomi Ferguson, says that after consideration by the Adjudication and Rulings business group, IRD still believes this practice is unacceptable.

“Property owners are still able to depreciate chattels such as carpets, drapes, light fittings, whiteware and so on, as separate assets. There is also provision to depreciate separately items such as water heaters, clothes lines and other fittings that are not part of the building.”

However, permanent fittings such as kitchen cupboards, bathroom vanities and built-in wardrobes cannot be claimed under the ‘Building fit out’ asset category.

“Property owners who have been splitting these components out from the cost of the building will have overstated their depreciation claim in the past, but we won’t be asking them to adjust previous years’ income,” says Miss Ferguson. “However they will be required to

add the value of the various ‘components’ they have been depreciating individually into the cost of the building, and combining the depreciation claimed for those individual assets.”

Ross Melville PKF tax partner, John Dillon, says this means depreciation must be applied to the combined asset (i.e. the entire building). The building cannot be broken up into smaller components (i.e. interior walls) to obtain higher depreciation rates under the ‘Building fit out’ asset category.

“The values of these smaller components – previously depreciated individually – must be added into the cost of the building, to also combine the depreciation claimed for those individual assets.

“This will identify the asset to be depreciated; the cost of that asset; the depreciation claimed to date. They should then use the building depreciation rate to claim depreciation for that asset.”



Tax payers will be required to take this approach from the first available income year, but taxpayers will not be required to adjust previous income years.

For cases still under investigation or proceeding through the disputes process, Inland Revenue will consider allowing the taxpayers to take up the Commissioner’s approach to settle the matter.

February 1 2007 - Applications for Charities Act registration

Charities have 17 months from 1 February 2007 to register – or risk losing their tax exempt status – under the new Charities Act.

Ross Melville PKF Partner, Russell Toplis, says anyone involved in a charity should be aware that the organisation must register before the deadline of 1 July 2008 – forms can be downloaded from www.charities.co.nz as can a new guide to the Charities Act.

“For some charities it’s just two forms, so it shouldn’t be too hard. But we do recommend that the charity will benefit from a pre-registration review – bearing in mind that the deadline is not far off.”

In the review, it is advisable to make sure the purposes of the organisation are compatible with its current activities and to consider proposed future activities.

It is important to ensure that the organisation’s

activities comply with the charitable requirements under the Income Tax Act 2004:

- The charity must not be for the private pecuniary profit of any person;
- The charity deriving the income only carries out its charitable purposes in New Zealand;
- No person with control over the charity is able to benefit from the business; and
- The officers of the charity are not disqualified persons, such as undischarged bankrupts or have had a conviction for dishonesty in the last seven years.

For more information (included in a new online guide to the Charities Act) or to download the registration forms, visit www.charities.co.nz.

An end to the modern spam plague?

Spam is one of the plagues of the modern information technology driven age, creating significant costs to business. As a measure of relief, Parliament recently introduced its anti-spam legislation in the form of the Unsolicited Electronic Messages Bill.

The Bill requires:

- All messages with a New Zealand link to identify and provide contact details of the sender, (or person authorising the sending) as well as providing an unsubscribe function;
- It prohibits messages for the sale of products / services that have a New Zealand link unless the people have opted in;
- It prohibits messages with a New Zealand link that promote or market an organisation where people have withdrawn their consent or opted out; and
- It prohibits the use of software to harvest electronic addresses or the use of harvested electronic address lists.

Traps for the unwary in new holiday pay rules

While employees will be entitled to four weeks annual leave from 1 April 2007, there is the probability they may have already started accruing that leave – depending on their anniversary date (the date they started employment).

The Holidays Act states: On and from 1 April 2007, when the employee next becomes entitled to annual holidays, the employee's minimum entitlement is increased from three weeks' annual holiday to four weeks' annual holidays.



This means, says Ross Melville PKF Practice Manager, Michelle Stirrup, that the anniversary date before 1 April 2007 is when the employee starts accruing the four weeks entitlement – so if that anniversary date is the 4th of April, they will have started accruing from the 4th of April 2006. “April 2006 is the kick-off month for employees to be accruing annual leave on the new four week regime – an anniversary date of January, February or March will only begin accruing in January, February or March 2007.”

However, the entitlement must be earned – if an employee resigns before the entitlement becomes law on 1 April 2007, they are only entitled to the equivalent of three weeks holiday pay entitlement.

“We suggest pay slips only show the three week entitlement until it is earned from 1 April 2007,” says Michelle. “If you show the leave entitlement before it becomes law, you may be faced with the problem of staff wanting to take those four weeks before they are entitled.”

Finally, staff who already have an agreement for four weeks leave will not be entitled to five weeks holiday, unless their contract states ‘one week in addition to the minimum entitlement’.

Deductibility of At Risk Pay not so certain

The IRD has signalled that the deductibility of performance pay - paid within 63 days after year end – may not be automatically allowed in future, particularly if the payment is not automatic and depends on an approval procedure.

Ross Melville PKF Partner, Graeme Clark, says performance pay is becoming increasingly popular – bonuses based on performance profitability, production and or sales targets – and IRD is insisting that the taxpayer must be ‘definitively committed to the expenditure on or before year-end’ to be allowed it in that year.

“If it is money you can’t count on – because whether you are paid it or not depends on your performance – then the deduction must be taken in the year of payment. You cannot pre-deduct on your performance pay,” says Graeme.

If however, the bonus is not based on any appraisal criteria – such as to measure performance – and is merely the outcome of calculating a formula, then the bonus is deemed to have arisen by year-end (even if the calculation occurs after balance date), and can be claimed for within 63 days after year end.

“We suggest you refer to your employment contract - or the document which sets out the terms and conditions of the incentive or bonus agreement - to make sure that the payment in question is deducted in the correct income year.”



Graeme Clark of Ross Melville PKF

The things Ross Melville PKF value...

- Being hands on Professionals with a strong business orientation;
- Being Practical, Accountable and Fair;
- Supporting the achievements and accomplishments of our clients;
- Looking for meaningful ways to see our clients grow; and
- For Ross Melville PKF to grow with you



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Inland Revenue briefs

Withholding tax change for fruit growers

Inland Revenue (IRD) has extended Withholding Payment Regulations to all contractors in the fruit growing industry from 1 April 2006.

Concerned about tax evasion in the fruit growing industry, IRD says employers must deduct a withholding tax of 15 per cent if they

hire contractors to 'pick, thin or pack' fruit.

Ross Melville PKF's Christine March says employers may deduct at a 'lower or zero rate' if the contractor has a special rate certificate.

"Previously IRD exempted deductions on payments to companies."

Excess Imputation Credits to be treated differently for individuals

New tax rules are effective from the 2006 year in respect of 'excess imputation credits' received by an individual.

When a dividend is paid by a NZ company, tax credits must be attached equal to 33 per cent of the gross taxable amount. Dividend tax credits are either in the form of imputation credits or withholding tax (or both).

Withholding tax is a straight deduction from a dividend, paid to IRD on behalf of a shareholder (similar to RWT on interest). Imputation credits arise from income tax paid by a company. i.e. a company pays tax on profits and to avoid double taxation of the same profits (that is, when distributed as a dividend) shareholders receive a 'notional' credit for the tax a company has paid.

As imputation credits are 'notional', any excess credits of a shareholder cannot be refunded by IRD. Excess credits arise when imputation credits received by a shareholder exceed the tax he/she has to pay. For example, a person receives a fully imputed dividend but also incurs rental losses that are greater. The person will have no taxable income but has imputation credits to claim. These imputation credits are regarded as excess credits.

In the past when an individual shareholder had excess credits the rules were that they had to be converted to a loss by dividing by .21, for example, a person has excess credits of \$100.

Dividing by .21 converts to a loss of \$476.19.

This loss could then be claimed against future taxable income.

The problem with this approach was that the tax savings on the loss may be more or less than the amount of the excess credits. For example, in the year the loss is claimed the person earns income over \$60,000. Therefore, the person has tax savings on the loss of \$476.19 x 39 per cent (being the tax rate on income over \$60,000), equals \$185.71. As the amount of the excess credits were only \$100 the person was better off by \$85.71.

Similarly, if the person earned less than \$38,000 in the year the loss is claimed, the tax savings on the loss would be \$476.19 x 19.5 per cent (being the tax rate on income to \$38,000), equals savings of \$92.86. As the excess credits were \$100, the person is worse off by \$7.15.

To remedy this disparity the rules have been changed for the 2006 tax year onwards. Now, excess credits are to be carried forward and offset directly against any future tax that may be payable. This ensures a direct one-for-one claim.

A by-product of this change means that individual taxpayers who have excess imputation credits must file an IR3 tax return.

The old rules are unchanged for companies, estates, trusts, Maori authorities and incorporated clubs and societies.

Do you have enough 'Skin in the Game'?

To golfers it means high risk, high reward. In ancient times someone's robe could be put forward as security against a debt or they could be so certain of an outcome they would be willing to bet their shirt on its success. So what does it mean when an investor talks about an entrepreneur having some 'skin in the game'?

In ancient times, wagering your shirt or robe was serious business because to lose it means the unfortunate would be exposed to rain, sun and cold. For golfers, the 'Skins Games' means high risk and high reward, and for a 'Senior Skins Game' it's winner takes all – the golfer has to win the hole outright or the money carries over to the next hole.

As the game progresses, the value of the purse for each hole increases to make each hole a winner takes all scenario - stakes vary from \$20,000 per hole to \$100,000 for the final hole with a total of \$700,000 at stake during a game.

Today, when an investor asks an entrepreneur if he or she has enough 'skin in the game', they're suggesting it's more likely to hurt the entrepreneur than the investor if the idea goes belly up, they're asking if the entrepreneur sees the potential payback as being high enough to tolerate the risk involved.