

INTOUCH

with Martin Jarvie PKF

Summer 2004/05

INTRODUCTION

This is the final In Touch newsletter of the year, and being just short of Christmas the partners and staff want to wish all clients and contacts all the very best for the festive season, and for a successful 2005.



Gus Gaskin, Owen Gibson, Robert Elms, Graham Langridge

Whilst the year is coming to an end, the Christmas break provides an opportunity to take stock of what did or did not work during the year, whilst the new-year means a start to business planning for 2005 and putting in place strategies and plans for the future. In making plans for next year it is an opportunity to review structures and explore opportunities, perhaps considering new options, additional capital or borrowing requirements, staff requirements or personal initiatives such as succession planning or retirement.

All of these issues need to be considered and then incorporated into your strategies and your updated business plan for next year. If you have not written down your business plan before, a new-years resolution could be to do so and committing to working more ON your business. The early part of the year often provides the best window for these planning activities, and of course allows the plan to be drafted and in place ready for the start of the new financial year in April.

It should also be considered at this late stage of the year that the final instalment of provisional tax for most tax payers is due 7 March 2005, whilst Terminal Tax (if any) is due 7 April 2005 for most, but still 7 February for those who no longer enjoy extension of time arrangements. This means that cash flow may be difficult, especially for those who will also have GST payments in January and February. Importantly it is also the final chance this year to estimate provisional tax. Being almost at the end of the financial year, realistic estimates of whole year results should be possible, and incorporated into provisional tax planning, either ensuring appropriate estimates are filed if profits have lowered, or additional funds are paid if necessary to reduce exposure to use of money interest.

If you would like to discuss any of the issues above, or any others raised in the newsletter, contact your usual Martin Jarvie PKF partner and we will be happy to discuss further with you.

At this time, and looking towards Christmas we look forward to working with you again next year and we wish yourself and your families the best wishes for the holiday season. **PKF**

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WEBSITE

The Partners are pleased to formally launch the Martin Jarvie PKF website www.martinjarviepkf.co.nz. The site itself has been up and active for a number of months with an increasing amount of content and various pages being added and improved. We invite you to visit, review and comment as you feel, and any and all feed-back would be welcome.

The site contains information about the firm and it's partners, and also details of key staff and service lines such as Audit and Assurance, Business Advisory, Business IT etc.

Importantly the site also has information for clients including copies of our In Touch client and contacts newsletter, our annual client questionnaires, and various checklists on important business topics.

The site also includes a full staff directory with email addresses and phone contact details for all staff so you can reach those assisting in your assignment. We hope all clients and contacts use and enjoy the site, and if there are any additional resources or areas you would like to see added, please contact any one of the partners.

PKF

TRUSTS - A GOOD MOVE ?

Family Trusts have been one of the most talked about topics over the last couple of years. Whilst it should be remembered Trusts are not suitable for all people, they can provide an effective structure for managing risks and taxation, whilst providing a solid base for asset planning purposes.

One of the most often-talked about topics is -
Why establish a trust?

There are a variety of reasons and a number of the most common are listed below. However the most important thing is to take advice and consider your own circumstances. Consideration should also be made not only of the benefits, but of the costs and complexities of establishing and administering a trust.

Trusts are often utilised for;

- Protection of assets from creditors. Claims can come from a variety of sources, especially for self employed professionals, business owners trading as a sole trader or a partnership, and company directors.
- Tax savings, stemming from the ability to split income to beneficiaries that may be on a lower tax rate, e.g. spouse or children (this is now limited in the case of children under the age of 16).
- Protection against means testing for rest home subsidies or other income tested benefits.
- Protection against matrimonial disputes.
- Asset management, where someone is unable to manage their affairs because of age or infirmity. This can be very useful if there may be a child who, due to medical or employment conditions, is disadvantaged compared to other children in the family. A provision can be made for that child and continue after the death of the Settlers without any worry that he or she may miss out or be disadvantaged.

Transferring assets to a Trust during a Settlor's lifetime makes the administration of an Estate much easier, with associated cost savings as well. The death of a Settlor does not affect the running of a trust - it continues as before. A will can be challenged after your death and your Estate may not go where you intended. Setting up a Trust with a corresponding Memorandum of Wishes as to how you wish your assets to be distributed can make it much simpler.

When setting up or considering a trust, we would also recommend you review your will to ensure it contains suitable provision for the new Trust such as forgiveness of debts owed, transfer of residual assets and considers issues such as life interests and bequests previously made.

The new Property Relationships Act has changed the way matrimonial property is split and any clients with an existing Trust should review their Trust structure.

If a Trust is an appropriate structure to manage your affairs Martin Jarvie PKF can assist in working with you and your solicitor to ensure the trust deed meets your requirements, whilst also assisting as necessary in any transfers of assets, for instance in the valuations of business assets or shares. The firm and the partners also often act as independent trustees to assist clients in administering their trusts, and with decision making to ensure the independence of the trust. Remember all decisions must be joint AND unanimous to be valid, so ensure all trustees are consulted and where appropriate, decisions are minuted and signed by all trustees.

To assist in managing your trust Martin Jarvie PKF has authored a guide to trusts which is available to all clients, please contact one of the partners and we can arrange to send you a copy, or you can access it on our website. **PKF**

PROVISIONAL TAX AND USE OF MONEY INTEREST

New Zealand has a comprehensive system of provisional tax, effectively an instalment system, and generally for self employed tax payers. All tax payers who have more than \$2,500 of residual tax to pay in any year become provisional tax payers. (Residual Income Tax (RIT) is the amount after tax deducted at source, such as PAYE, Resident Withholding Tax etc has been accounted for.)

For those tax payers with a 31 March balance date provisional tax is paid 7 July, 7 November and 7 March each year, and is calculated as 105% of the previous years provisional tax liability. Terminal tax is then paid 7 April the following year if extension of time arrangements apply, or 7 February otherwise.

The government have also imposed a system of use of money interest on provisional tax payers, currently charging 11.93 % on underpayments and paying 4.83 % on overpayments. These are not automatic for all provisional tax payers, but they are conditional on other issues. Firstly individuals are not automatically exposed until RIT reaches \$30,000, but for non-individuals (companies, trusts, estates) it applies immediately from \$2,500.

If however an estimate is entered, interest will be charged on any underpayment and hence care needs to be taken when making estimates and reducing payments made.

TAXATION SERVICES



Mike Ruffell

Recently Mike Ruffell joined our team as the manager of Taxation services. Mike joined the firm with over 15 years tax experience, in both corporate environments and chartered accounting firms including 7 years with PricewaterhouseCoopers and experience with a specialist tax consultancy.

Having spent time as the client as well as the advisor, Mike brings a practical, hands-on approach, aiming to provide clients with plain English answers that represent value.

Mike has a wealth of practical tax experience in a range of issues including structuring, due diligence, tax reviews, advice to inbound taxpayers, trans-Tasman tax issues, property transactions and general tax advice to SME's.

Since joining the firm Mike has been assisting the partners in a variety of assignments as well as helping clients through IRD audits and investigations, preparation of responses to IRD queries or formal responses as necessary. Some of the common issues raised in audits and areas of concern are shown below. To discuss any aspect please contact Mike or any of the partners.

Drawing on his previous experience and knowledge Mike is also able to offer a tax health check service that includes meeting with you or your in-house accounting staff and identifying the major areas of tax risk and recommending what can be done to manage or mitigate that risk.

Mike has also been actively providing resource material for the firm and its clients, along with commentary on current tax issues and announcements.

The interest is generally calculated from the first instalment of the year (there are exceptions for first year provisional tax payers), so if profits have increased markedly during the year be conscious that interest may effectively be being incurred on provisional tax payments made the previous 7 July!

For more detailed information or to discuss your particular situation please contact any of the partners or our tax manager Mike Ruffell. mike.ruffell@mjpgkf.co.nz **PKF**

These are on the firm website www.martinjarviepkf.co.nz under the Taxation Services section. If you have any comments or questions, or if any of the matters interest or effect you please contact us.

To discuss your requirements or enquire as to any assistance Mike can provide, please contact any of the partners or Mike on 496 4096.

Common problem issues identified during IRD audits.

Bad Debts not written off at balance date - A deduction is permitted only for bad debts which are actually written off as bad *before balance date* in the income year in which the deduction is claimed. If you maintain a computerised debtors' ledger, the balance for individual debtors has to be reduced by the amount of the bad debt. In other cases, specific actions need to be taken to evidence the belief that the debt is bad. Usually, this will include appropriate book keeping issues.

Entertainment - IRD often finds that entertainment expenses have not been treated correctly. This is particularly so in relation to deductions for food and drink. These types of expenditures are normally 50% deductible for income tax purposes. However, there are exemptions which you should be aware of. It is also important to ensure that appropriate documentation is maintained in support of any claim.

Fringe Benefit tax – all of the following matters can result in a FBT bill. Claiming no private use of your car, and not paying FBT because you have a home office; claiming the full costs of an overseas holiday, where you have a business meeting offshore; Australian firms paying superannuation contributions for NZ based employees; not apportioning the private and business use of phones.

PAYE

Not accounting for PAYE on any housing provided to employees; paying excessive allowances (meals, travel etc).

Cut Off Issues - Often the cut off for revenue and expenditure at balance date has not been accurately completed. Common errors include an omission of cash on hand from sales, income which has been derived but has not been invoiced at balance date (e.g. there is an entitlement to bill) and cutting off prior to the end of month.

Fines and Penalties - IRD's view is that fines and penalties are not deductible for income tax purposes. While there is some basis to the IRD's argument, there is support for the view that some fines and penalties are deductible for income tax purposes, such as fines for trucks exceeding weight restrictions as carting the extra weight could be seen as directly related to earning taxable income. **PKF**

RESIDENTIAL PROPERTY INVESTMENT



Owen Gibson

Investment in residential property has been in the headlines again recently for a number of reasons. Firstly some commentators are predicting a fall in the market and forecasting difficulties for those who have invested heavily in the past few years, and secondly due to the announcement of the governments review of the depreciation regime to reduce some of the tax advantages enjoyed by investors.

As with all investments, residential property has its place if done well, but should always be viewed as part of a portfolio, not the only investment. Currently in New Zealand residential property has enjoyed the combined effect of historically low interest rates, a rising property market, increased immigration, and importantly no capital gains tax.

As some have been saying, the current interest rate outlook is for continued increases for the next year or more. That, along with an increased supply mean rental house prices are also predicted to worsen, by either flattening or reducing prices depending on location and quality.

That being the case is residential property a good investment?

The answer is yes and no. That is, done well with care taken to stick to the fundamentals, property still represents a good opportunity for a long term investor. By that we mean looking at property that is good quality, in a good location, providing an acceptable return, and a good long term opportunity for capital gain.

There are a number of things an investor should consider when looking for opportunities and when purchasing. Before commencing set your conditions, what sort of property you are looking for, set your benchmark return, consider management issues, and the price / debt level you can comfortably service.

In establishing these issues and going forward – take advice. Yes advisors can assist in many ways, setting your goals, considering your investment strategy, assisting in funding decisions, valuing and purchasing the property and setting up for the most advantageous structures. Your team of advisors should include Martin Jarvie PKF, and often one or more of a lawyer, valuer, mortgage broker or bank manager. Each advisor can contribute to the investment decision and increase the chances of a positive result.

Some issues which should be considered once the property has been selected;

- What is an appropriate ownership structure (Personal names, LAQC, Trust),
- How to structure the borrowings to improve or protect interest deductibility,
- Can a chattel valuation be obtained to improve depreciation deductions?

The recent announcement by the IRD of a review of the depreciation regime as it relates to investment property has created some uncertainty, however an independent valuation of the property and the chattels included in the purchase will likely always present an improved depreciation result.

As with many things these issues should be considered **before** committing yourself to a purchase, so always consult with your professional advisors, in particular Martin Jarvie PKF.

MARTIN JARVIE PKF

offer an extensive range of professional services, including:

Business Services

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 Tax Compliance
 Financial and Management Reporting
 Profit and Cash Flow Forecasting

Business Advisory

Strategic Business Planning
 Financial Health Analysis
 Taxation Planning and Advice
 Business and Share Valuations
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Business Recovery and Turnaround Management
 Business and Corporate Restructuring
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 Due Diligence
 Internal Control Reviews
 One-off Investigatory Assignments
 Scrutineering

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Systems Review
 Installation of Accounting Systems
 Training
 Setting Up and Documenting Procedures

Finance

Preparation, Review and Audit of Prospectuses
 Preparation and Presentation of Finance Applications
 Financial Information Memoranda **PKF**

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