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The information contained in this report is not advice. We recommend that before readers decide to proceed with any of the matters raised below, that they contact their professional advisors.

TRUST REFORMS

Trusts are a popular way of protecting property and managing assets in New Zealand. The number of trusts we have in New Zealand is unknown, but estimates put the figure between 300,000 and 500,000.

The legislation governing NZ trusts has remained unchanged for decades as it has been predominantly governed by the Trustee Act 1956. The Act has been criticised for allowing the mismanagement of trusts with no easy legal redress for beneficiaries, however this is set to change. The legal framework has been subject to an in-depth review by the Law Commission, with the Trusts Act 2017 released in draft late last year, followed by ongoing consultation.

The draft bill seeks to clarify core trust concepts, resulting in a more useful piece of legislation that can be applied to fix practical problems and reduce the costs associated with trust administration. This will effectively impose 'minimum standards' for the governance of trusts so that trustees and beneficiaries are clear on their precise obligations, duties and rights.

The draft Bill features seven key proposed reforms that vary in nature from clarifying the key features of a trust, to detailing the duties and powers of trustees.

Under the new Act, trustees will be required to know the terms of the trust and act in accordance with them, act honestly and in good faith, to act for the benefit of the beneficiaries and to exercise their powers for a proper purpose. There are a further eleven default duties that apply, unless they are modified or excluded by the terms of an individual trust deed. The default duties cover areas such as the requirement to invest prudently, avoid conflicts of interest and to act for no reward. The formalisation of Trustee duties will provide protection to beneficiaries that assets will be dealt with in their best interests, and provide legal remedies if trustees fail to meet these standards. The Act also requires trustees to disclose certain information to beneficiaries who are reasonably likely to receive property under a trust.
How the above impacts on professional advisors being independent Trustees of client Trusts remains to be seen.

It will be important for all trustees to understand the new law and their individual trust deeds, to ensure they discharge their duties with the appropriate standard of skill and care.

No changes to the tax treatment of trusts are proposed. However, there is additional focus on trusts from a tax perspective following the recent "Panama Papers" scandal and the alleged misuse of NZ foreign trusts, which has resulted in a Government led investigation into whether existing disclosure rules are adequate. In response, the Government is beefing up the requirements for foreign trusts in three key areas; registration, disclosure, and annual filing. The proposed changes will require all foreign trusts to formally register with the IRD and be subject to an increased number of disclosure requirements, with sanctions for non-compliance with the new rules.

To some degree, the new Act serves to codify existing case law and current best practice, bringing a degree of consistency to New Zealand's trust regime. Ideally, this will reduce the frequency with which disputes end up before the courts and benefit all beneficiaries, which is ultimately what a trust is designed for.

TAX PLANNING BEFORE 1 APRIL '17

For most taxpayers, 31 March represents the end of the financial year. In the lead up to 'year-end' there are a number of actions that business owners may want to take to avoid missing the boat on simple tax planning opportunities.

Trading stock: stock can be valued at the lower of cost and market selling value ("MSV"), and generally it will be beneficial to use a lower MSV where possible. But to use MSV you must have evidence that this represents the market value of the specific stock items at or about balance date. The IRD have indicated that suitable evidence includes independent or internal valuations by suitably qualified persons of the price of goods and actual sales for a reasonable period before and/or after balance date.

Accruals and provisions: a tax deduction should be available if you are definitively committed to an expense at year end and can reliably estimate the amount. Ensure all expenditure is captured and accrued to minimise the amount of taxable income. One exception is employee related accruals that are tax deductible if they are incurred and are paid within 63 days after balance date (so by 6 June); consider paying any staff bonuses by then to gain a current year tax deduction.

Bad debts: to be tax deductible bad debts must be actually written off before year end – it's no good booking the journals after balance date as part of your year-end accounts preparation. There also needs to be evidence that the debt was considered "bad" (e.g. review of accounts receivable, debt-enforcement notices and other actions taken).

Assets: if you are planning on buying any depreciable assets (e.g. plant and equipment), a full month's depreciation can be claimed in the month of purchase, so it may be worth buying replacement assets just before 31 March.

Relevant to companies only:

Charitable donations: in order to claim a donation deduction, it needs to be paid in cash before 31 March. The amount of the donation is limited to the amount of a company's net income in the absence of the donation. Hence, if a company has made a loss it might be beneficial to push the payment into the next year.

Shareholder current accounts: if a company is owed money by shareholders, consider paying commercially justifiable shareholder-employee salaries or paying a dividend to settle the debts. If not done, there may be fringe benefit tax or deemed dividend issues.

Imputation Credit Account (ICA) balance: ensure the imputation credit account does not have a debit balance at 31 March, otherwise penalties will be incurred. If the ICA may be in debit, consider a making a voluntary provisional tax payment before 31 March.

FBT CHANGES ON THE HORIZON

Currently, companies that provide a motor vehicle for the private use of their employees must register for and pay FBT. Draft legislation has been introduced which will enable some small businesses to avoid having to pay FBT.

The proposed amendment will allow close companies (where 5 or fewer natural persons own 50% or more of the shares) that only provide one or two vehicles to shareholder employees (and no other benefits) to apply the rules currently available to sole traders and partnerships. Using these rules, the company will claim a deduction for the use of a vehicle to the extent it is used in the business and not pay FBT in respect of the private use.

In order to apply the treatment to a particular vehicle, it needs to be adopted from the time a vehicle is acquired, or first used in the business. Hence, the method won't be available for company vehicles currently held. Once a particular vehicle is subject to the new treatment, it must continue to be applied until the vehicle is either sold or is no longer used in the business.

The Bill introducing the change is currently going through its second reading in Parliament and will apply from the 2017- 2018 year. With the new rules coming into play soon, it may be the right time to think about your current business vehicle usage and whether or not it is a good excuse to splash out on a new vehicle.

CHANGES TO COMBAT INTERNATIONAL TAX STRUCTURING

Perceived tax avoidance by multinational companies has been attracting significant media and public attention. There is widespread concern that corporate structures and financing arrangements are being used to minimise worldwide tax bills.

A common example to illustrate the problem is where a business operates through companies in both New Zealand and Australia, and there is a loan between the two. By using certain type of debt instruments, interest payments can be structured as tax deductible in New Zealand, but non-assessable in Australia. This results in a mismatch between the two companies / countries and a net reduction in their total tax payable.

The Organisation for Economic Cooperation and Development (the 'OECD') has released a series of recommendations designed to close such tax loopholes and make tax more equitable across the globe.

The New Zealand Government intend to adopt the recommendations, however they recognise that our domestic policies will only be effective if the OECD recommendations are implemented worldwide. The Government is therefore closely following the changes adopted by the UK, EU and Australia before the new rules are passed into legislation here. However, the US and other Asian countries are currently reluctant to adopt the OECD recommendations, so it will be interesting to see how the international markets react.

The proposed changes to NZ's tax rules are complex, however they aren't just relevant for global giants. The rules will need to be understood by all New Zealand businesses that engage in cross-border transactions, even relatively small New Zealand businesses operating outside New Zealand.

Some of the key changes proposed to be implemented in New Zealand include:

- Denial of a tax deduction for a payment to an overseas related entity, where the payment is not treated as taxable income in the foreign country.
- Where foreign dividends received by a NZ company are normally non-taxable, they will become taxable if there has been a tax deduction for the dividend payment in the overseas country.

On a practical level, this is most likely to affect:

- NZ businesses with loan or share arrangements with businesses in other countries;
- NZ branches of foreign companies, or NZ companies with overseas branches;
- NZ companies, partnerships and trusts with overseas owners or investors, or with foreign investments.

The proposed changes are not simple and have the potential to cause major headaches for New Zealand businesses looking to overcome the technical and practical difficulties of doing business on the international stage.

MORE ON FBT

In the vast majority of cases, fringe benefit tax (FBT) on vehicles is paid based on the GST inclusive cost price of a vehicle. But it is worth considering application of the depreciated tax value (TV) method if you have older vehicles on which FBT is being paid.

Under the TV method, the value of the benefit for FBT purposes is calculated based on the depreciated value of a vehicle. It is typically not used from acquisition because it front loads the FBT cost into the first years of ownership and the benefit of its use doesn't come until later.

The method chosen in the first FBT return for a specific vehicle must continue to be used for that vehicle for 5 years. Hence use of the TV method can only be considered after that initial 5 year period has finished. However, if FBT is being paid on vehicles that have been owned for more than 5 years, a comparison to the TV method should be made—it is likely to give rise to a lower FBT cost.

The fringe benefit value is calculated based on 9% of a vehicle's TV (at the beginning of the year). The 9% rate is based on a GST inclusive value. If GST was deducted on the cost of a vehicle and you wish to use your fixed asset register, the rate of 10.35% applies. The minimum TV value that can be used for a vehicle is $8,333.

It is worth checking your vehicle register and if the TV method is an option, run the numbers, the greater the original cost of the vehicle, the greater the potential saving.

IRD RULINGS

Over the past few years, there has been a pronounced improvement in the manner in which the Inland Revenue Department selects and conducts its investigations.

There has been an increased focus on data analysis, comparisons to statistical norms, and use of external information such as land transfer data. As a result there is an increasing need to consider how IRD might approach a particular transaction or issue.

In cases where the position is unclear or the dollars involved are material, consideration needs to be given to approaching the IRD beforehand to seek their approval or view to treat something in a particular way. This can occur by approaching IRD for a 'private binding ruling' or a 'non– binding indicative view.'

Both processes are positive and collaborative, as IRD generally are focused on determining the correct position under the law. In contrast, if IRD approach the matter 'after the fact' through the course of an investigation, there may be more focus on proving a tax shortfall exists; and their view of the law can feel as though it is bending to accommodate that outcome. It can become emotional as each party becomes increasingly entrenched in their view, giving rise to significant cost to defend a position and if the taxpayer is unsuccessful, penalties could apply, Too often the incremental cost will exceed what it would have cost to approach before-hand.

A private binding ruling provides the highest degree of comfort, because if successful, the outcome is binding on IRD. This provides peace of mind that a different individual from the IRD won't take a different view on the future. The binding ruling process is not subject to a legislated timeframe within which one must be provided, however IRD work to a timeframe of 3 months and are very good at meeting that timeframe. They are also willing to provide early indications of their expected view if required for the purpose of a particular transaction that may be occurring. IRD do charge a fee to provide a binding ruling; it does so at an hourly rate of approximately $160 an hour. The total IRD cost for a ruling is generally about $15,000 to $20,000. This cost must be considered in light of the tax involved and the comfort otherwise associated with taking a particular position. When this is balanced with the down side risk of IRD disputing the treatment in the future, it quickly becomes reasonable.

A further option is to acquire an indicative view. We understand IRD will consider issues through this process if it will take 20 hours or less. IRD don't charge for providing an indicative view, however, the outcome is not binding. irrespective of the fact that the IRD is not bound by the outcome, from a practical point of view it should provide a high degree of comfort. It should be unusual for an alternative view to later be taken by the IRD, and if this did occur, the fact that an indicative view was acquired should provide a strong negotiating position when asserting no penalties should be charged,

IRD AUDIT INSURANCE

Your tax invoice for the IRD audit insurance is currently being processed for the year beginning 1 March 2017. You should receive this before 20 February. In view of the IRD's increased activity in tis area, we recommend that you take up the cover. Note that the cover kicks in once payment is made only. If notification of an audit is received before payment is made, you will not be covered. If you will not take it up, please sign the decline option and return to us so we do not continually send out reminders.

WE ARE MOVING...

After 29 years (Oct) at 100 Mayoral Drive, we will be moving.

We were advised a few years ago that the building was sold to a developer who was going to turn the building together with the carpark behind us into a high rise apartment. Quick action by our client, Paul Dyson of Colliers, secured our new office on the ground floor at 3 City Road across from the Langham Hotel, at the corner with Symonds Street.

The move is scheduled for 1 April. Our office is currently being fitted out and we have been assured that it will be ready for the move, but please call us first, if you are popping in, to confirm if we have re-located.

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