

Newsletter

June - August 2008

FISHER

CHARTERED ACCOUNTANTS

HEASLIP LTD

SYSTEMS & SOLUTIONS FOR SUCCESS

Welcome to our mid-year newsletter, we hope you enjoy reading this issue in the warmth of your home or office.

Budget 2008

PriceWaterHouse Coopers have put together a Budget 2008 Tax Analysis, which we would like to share with you.

Budget 2008 delivers a three year programme of tax cuts. The lowest marginal tax rate falls from 15% to 12.5% from 1 October 2008. The thresholds at which each of the marginal rates applies will be raised progressively over the next three years until the tax cuts are implemented fully on 1 April 2011. Disappointingly the middle and top marginal tax rates will remain at 33% and 39% and Finance Minister Michael Cullen has given no indication of when those rates could be reduced. It seems fair to conclude that these rates will remain as a permanent feature of the tax landscape.

The tax cuts are targeted primarily at low income earners and will provide some relief from the rising cost of living when they are delivered. A single person earning \$45,000 will benefit by \$860 a year from 1 October 2008 and by \$1,670 a year from 1 April 2011. A person earning \$80,000 or more will benefit by \$1,460 a year from 1 October 2008 and by \$2,870 a year from 1 April 2011.

The threshold at which the 33% rate kicks in moves only modestly from \$38,000 to \$42,500 by 1 April 2011, which is far less than the \$12,000 uplift required to reflect the movement in the CPI since 1999.

From a design perspective the new package further widens the gap between the top rate of 39% and the bottom rate, now 12.5%. This 26.5% margin is likely to incentivise people to spread income into the names of family members on the lower rate. The other design consequences of delivering the tax relief primarily on the first \$20,000 of income is that it does not reduce a worker's marginal rate, being the rate they pay on the next \$100 of income. This means that there is no additional incentive to work harder as the tax relief will occur automatically on the first \$20,000 of income.

Families with children receive additional Tax rates and thresholds relief from Budget 2008. Dr Cullen has brought forward the inflation adjustment to Working for Families that would have taken effect on 1 April 2009 to 1 October 2008. This will put a further \$14 a week in the pocket of a family of two on the average wage from 1 October 2008. He has forecast a further increase from 1 April 2011. In recent weeks options including reducing the GST rate and removing GST from food and petrol have been floated by other politicians and commentators. Dr Cullen deserves credit for throwing these tools out of his toolbox. GST is an efficient tax that is easy to administer and difficult to avoid. There would be no sense in reducing the GST base.

The Government has also not opted to introduce a tax free threshold (below which income would be exempt from tax) or to pay a social dividend - sensible decisions in our view. A tax free zone poorly targets those most in need and would open up the tax system to avoidance and evasion. A social dividend (a one-off payment or tax rebate) would provide no incentive for people to work and could be inflationary.

The Budget does little to address a fundamental issue - the fact that New Zealand is a low wage economy. While responsibility for this rests with the entire community, it would have been useful to see the Government advocate measures aimed at increasing productivity - a key step on the road to higher wages. Our judgment is that lower tax rates and a flatter scale would be sensible policy options in pursuing that goal.

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IN BRIEF

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Tax payable by single person

Single person's income	\$50,000	\$75,000	\$100,000	\$150,000	\$200,000
Tax payable currently	\$11,370	\$20,520	\$30,270	\$49,770	\$69,270
Tax payable from 1 October 2008	\$10,510	\$19,060	\$28,810	\$48,310	\$67,810
Tax payable from 1 April 2010	\$10,213	\$18,463	\$28,213	\$47,713	\$67,213
Tax payable from 1 April 2011	\$9,700	\$17,950	\$27,400	\$46,900	\$66,400

Budget 2008 contd.

Working for Families and effective marginal tax rates

Budget 2008 delivers an early inflation adjusted rise for people receiving working for families (WFF) tax credits.

The WFF tax credit delivers targeted income support to families with children. While it achieves this objective, it does so at the cost of imposing very high effective marginal tax rates on the recipient families. The high effective marginal tax rate comes from adding the tax on an extra dollar of income together with the loss of the WFF tax credit as a result of that extra income - plus the loss of other assistance such as the accommodation supplement.

High effective marginal tax rates are a significant policy concern. They reduce the relative incentive for people to increase their incomes by work and investment. WFF in particular creates broad bands of income where families will experience high effective marginal rates of taxation. Our calculations show that, for a family with two children under 13 and earning \$75,000 a year - 80% by one spouse and 20% by the other, the family's effective marginal tax rate is 55% (and this ignores any abatement of accommodation supplements or other assistance). This means they take home only 45 cents for every extra dollar of income earned.

Budget 2008 has increased the thresholds and reduced the bottom tax rate. This delivers a modest reduction to some families' effective marginal tax rates including our family above. It reduces their effective marginal tax rate to 49%. However, at the same time the range of incomes that WFF applies to is being expanded, thereby widening the range of family incomes that are exposed to high marginal tax rates.

It is fair to acknowledge that there are no easy solutions to this dilemma. If the Government chooses to provide targeted income assistance to families, then it needs to abate that assistance and this creates the high effective marginal tax rates. The solution is to reduce tax rates generally and at the same time reduce the rate of the WFF tax credit. This lessens the targeting of the income assistance (as those without children benefit from the tax rate reductions) but reduces the negative impact of high effective marginal tax rates on families. However, with the design of the tax relief package in Budget 2008, the Government has essentially embedded high marginal tax rates in the tax system by retaining a steeply progressive income tax scale and expanding the WFF support levels.

Tax Simplification

The Government will introduce new rules to reduce compliance costs for businesses by raising a number of tax thresholds. The signalled changes will be part of the June 2008 Bill.

The main threshold changes are:

The new rules will also:

- increasing PAYE once a month filing and payment threshold from \$100,000 to \$250,000;
- increasing the FBT annual return filing threshold from \$100,000 to \$250,000;
- increasing the provisional tax use of money interest safe harbour threshold from \$35,000 to \$50,000;
- increasing low value trading stock from \$5,000 to \$10,000
- increasing GST registration threshold from \$40,000 to \$50,000; and
- increasing the GST six monthly return filing threshold from \$250,000 to \$500,000.
- allow non individuals (subject to certain thresholds) to return income tax for financial arrangements on a cash accounting basis; and
- increase the threshold for allowing financial arrangements to be accounted for on a straight line basis from \$1.5 million to \$1.85 million (based on the total level of financial arrangements).

The Government also announced that it is working on a second phase of initiatives that include:

- simplifying the rules for deducting legal and entertainment expenditure;
- introducing a single category of restricted private use vehicle for small and medium sized entities for FBT purposes;
- simplifying the rules for record keeping requirements for private use of motor vehicles by businesses;
- simplifying the GST invoice disclosure requirements; and
- allowing taxpayers to correct minor errors in subsequent returns.

Tax rates and thresholds

Current

\$1 - \$9,500	15%
\$9,501 - \$38,000	21%
\$38,001 - \$60,000	33%
\$60,001 and over	39%

From 1 October 2008

\$1 - \$14,000	12.5%
\$14,001 - \$40,000	21%
\$40,001 - \$70,000	33%
\$70,001 and over	39%

From 1 April 2010

\$1 - \$17,500	12.5%
\$17,501 - \$40,000	21%
\$40,001 - \$75,000	33%
\$75,001 and over	39%

From 1 April 2011

\$1 - \$20,000	12.5%
\$20,001 - \$42,500	21%
\$42,501 - \$80,000	33%
\$80,001 and over	39%

Ensure you sign your GST return

THE new GST 103H form does not provide for signing on the front. This is because the back of the form has parts two and three, which for some clients will not be applicable.

Be careful to sign the back of the form even if parts two and three do not apply to you.

An unsigned form can be treated as not having been received and leave you exposed to future risks. Sometimes mistakes are made and perpetuated.

The Inland Revenue Department is entitled to recover unpaid tax, in these circumstances, for a little over four years.

Anything beyond that time cannot be recovered as long as you have been honest with the IRD.

Tax Dates

May 28

1st Installment 2009 Provisional Tax (December balance date) -
1 or 2 monthly GST payers only

June 7

3rd installment 2008 Provisional Tax (June balance date)

June 28

1st installment 2009 Provisional Tax (March balance date) -
GST ratio option only

August 28

1st installment 2009 Provisional Tax (March balance date) -
1 or 2 monthly GST payers only

September 28

1st installment 2009 Provisional Tax (March balance date) -
6 monthly GST payers only

Monitor those Yellow Pages ads

DO YOU measure your responses from Yellow Page ads? How many of those responses turn into sales? Yellow Page advertising is expensive. Some people advertise, get responses and never follow up. They have more business than they can handle! So why do they pay for advertising? Examine your return on your Yellow Page advertising. Keep records. If your advertising works, that's fine. If it doesn't, save your money.

An opportunity to be a specialist?

IF YOU find a difficult task and no one likes doing it, you have an opportunity. Learn to do difficult jobs others won't tackle and you can command a premium for your skills. You'll become a specialist with the ability to charge extra for your unique abilities.

Learn the art of saying 'no'

FOR most of us in business, there never seems to be enough time in the day. We are often asked to serve on committees or help in some other way and are reluctant to say "no". Sometimes the invitation is made by an organisation with an inferred reward of being offered some business. These rewards rarely materialise. Perhaps we need to break the "yes" habit and say "no" more often. Be more selective about when you say "yes".

Are storm clouds on the horizon?

IF YOU see black clouds on the business horizon, now is the time to prepare for a storm. Hopefully, it will never come, but there is no better time than now to prepare for the possibility.

How should you prepare?

Borrowing

A major cause of financial distress is too much borrowing. Calculate the percentage of your borrowed money to the true or slightly reduced worth of what you own. Be like the punter on the sharemarket and knock something off the calculated value of your assets, just in case. If bad times come and revenue falls, consider how you would be placed.

Control

To steer your business through rough seas, it helps to know where you are going. Some costs vary with sales. An accountant's biggest variable cost is wages, but many tradesmen with a small business, for example, will find it is mostly materials. You can monitor your business by adding up your sales, deducting your variable costs and arriving at, what we term, gross profit.

You will find most of the costs of running your business are pretty well out of your control. Examples include rent, telephone costs, insurance and so on. We call these the fixed costs of the business.

If the fixed costs of your business are going to be \$20,000 per year, add what you need to take out of the business for living costs, then you'll know how much gross profit you will have to make.

You can also calculate the cost of the materials you use as a percentage of your sales. If you are running a shop you will need to take account of the change in your stock level. In difficult times you will be under pressure to cut your profit margin in an attempt to increase sales. This means the amount of gross profit expressed as a percentage of sales falls. We call this the gross profit percentage.

Monitor your gross profit percentage regularly and set yourself realistic targets, so you can discipline yourself not to give too much away.

Conclusion

This article has been written not because we are pessimists, but to alert you to the power of accountancy. We have many measures of business performance and we can help you to keep control of your business and its profitability. Implement your systems and get used to using them - and if the storm never breaks you will still be better off.

Remember, when politicians talk of a technical recession, there is a fair chance the outcome will be more than merely "technical". When the 1918 flu epidemic was rampant, the authorities deliberately understated the true situation.

Source deduction payment means FBT as an employee

ANYONE who receives source deduction payments is an employee for Fringe Benefit Tax purposes. This can possibly include self-employed people from whom your firm is deducting withholding tax.

Providing a vehicle to contractors can be the same, for FBT purposes, as it would be if they were employees.

When the employee is also an owner of the company, it is wise to have a directors' minute agreeing to prohibit the private use of a vehicle, in addition to the standard letter from the firm to the employee as recommended by the IRD. Get the minute signed by the employee confirming acceptance.

The quarterly check to see the employee is not using the motor vehicle is an idea generated by the IRD. It is not backed by case law. Nevertheless, you should document enough evidence to show you have confirmed the employee is following the instructions. You could check on petrol consumption, for example.

Employee contribution

You can have a vehicle partly owned by an employee and partly owned by the employer.

Based on a quarterly adjustment of 5 percent of vehicle cost, if the employee has paid for a third of the vehicle, the fringe benefit liability is reduced by one-third of 2.5 percent of the cost of the vehicle. So a vehicle costing \$12,000 is subject to FBT for the quarter on only two-thirds of 2.5 percent of the cost of the vehicle (to account for the employee contribution), plus 2.5 percent of the cost of the vehicle.

Deposit can help cash flow

AS A builder, plumber, electrician or any other skilled trades person who buys large amounts of material, are you in the habit of asking your clients for a deposit?

Hopefully, the answer is “yes”, because a deposit can help your cashflow. In our experience most trades people get deposits ranging up to 50 percent.

If your business is in any trouble, be careful about accepting a deposit and then using some of it for your personal costs. If your business fails, you will be liable for the debts to your customers.

If you are a limited liability company, you have protection only if you had first checked, before accepting any deposit (each time), to make sure your business was technically solvent. If you do not keep documentation to show the company was solvent at the time you received a deposit, the directors of the company can be personally liable for the debt to the customer, regardless of limited liability.

If you are wearing the hat of a customer, avoid giving a deposit. Some suggested points to raise with the trades person are:

1. Why should I take the risk of your business failing?
2. You can check out my credit worthiness.
3. Here is a list of references. Please feel free to ring any of them.
4. I do not wish to pay you directly, but I would be happy to lodge the money in your solicitor's trust account on the basis it would be paid to you when I have confirmed the job is complete.
5. If you are getting some building done and, for example, your kitchen joinery supplier wants a deposit, try getting the bill charged through the builder's account. This often works as the builder is known to the supplier.
6. Try a token deposit as a compromise, with the balance of the deposit payable when goods are delivered to the site.

Important

If you pay a deposit and the supplier goes broke, you rank as an ordinary creditor and might never see your money again.

Pitfalls in Starting a Business

If you are contemplating starting a business, either by buying an existing business, or starting from scratch, you will need to avoid the pitfalls. This can be done by seeking advice from an accountant before signing any contracts. Sitting down with an accountant in the early planning stages can help you to not only avoid the pitfalls, but can also help set realistic goals, plus an objective, experienced voice at the outset will minimise teething problems.

The key items to help avoid pitfalls are:

- Get good advice from Accountant, Solicitor and Bank
- Market analysis and verification
- A realistic Business Plan
- Honestly review your management skills
- Undertake training to overcome management deficiencies
- Prompt and regular financial accounts
- Regular monitoring of stock and work in progress
- Chase up debtors
- Staff training, motivation and leadership
- Some knowledge of the trade or business
- A clear understanding of the hours you will have to work

We can assist you in all of these areas.

IN BRIEF

Check your KiwiSaver statements

The KiwiSaver scheme is new and the IRD had trouble coping with the task of sending contributors' money to the KiwiSaver fund managers. Most changes like this take a while to settle down and for mistakes to be fixed. We suggest you tell your staff to check their statements from fund managers, when they receive them, and make sure all the money they and their employer have contributed has been paid in. KiwiSaver's year-end is 30 June, so fund managers should be accounting to contributors after that date.

Contribution rate

The KiwiSaver CEC (compulsory employer contribution) rate for a year applies only if the whole pay period is in the year specified. For example, if a pay period for an employee spans 1 April 2009, the 1 percent rate will apply for the employer contributions for the whole period starting before midnight on 31 March 2009 and the 2 percent rate will apply to the next pay period.

First home buyers

If a couple want to buy their first home and claim the KiwiSaver incentives, both should be enrolled in KiwiSaver for a minimum of three years. To get the maximum benefit it may pay to stay longer as it is \$1000 per annum with a maximum of \$5000 per person.

Contractor employee

What happens if a contractor is subsequently ruled to be an employee, but the employer has not taken KiwiSaver contributions? Answer: The employer will be liable for KiwiSaver contributions as well as PAYE, holidays, etc.

Office News

We would like to introduce two new people to the Fisher Heaslip Ltd team.

Firstly Roopam Verma, has joined us as an Accounting Technician.

Secondly Kere McKinnon has joined us on a part-time basis as our Trust Administrator. Kere is currently working on updating our trust administration system which will allow us to keep a better track of our clients trusts. We will highlight in our next newsletter how trusts with incomplete records and documentation are highly likely to be deemed useless for asset protection if your trust is “attacked” by a third party and highlight how our Trust administration can minimise these risks.

If you have any questions or comments, please don't hesitate to get in touch with us at any time, call 827 6006 or email us at: admin@fisherheaslip.co.nz or visit our website: www.fisherheaslip.co.nz. We'd love to hear from you!

If you have received the hard copy of this newsletter and wish to receive as electronic format please let us know.

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