BC'S BUSINESS BRIEFS

TAX ISSUES

When does a business cease?

The issue of when a business ceases is important from the point of view of establishing what expenses are deductible after a business closes down. As an example, it is not uncommon for there to be residual debt in the case of businesses that have been either sold down for a price less than acquisition cost or indeed just closed.

A recent TRA case looked at what constitutes the business closing, and therefore establishing the point at which ongoing expenses become non deductible from a tax perspective.

The case involved a property development company who entered into a contract to acquire land in 2006 which was to be used for the development of retail units and apartments. The purchaser applied for Resource consent but the vendor objected to the consent and in July 2008 the purchaser, through their lawyer, terminated the contract as Resource consent had not been granted.

The dispute as to costs between the vendor and purchaser was finally settled in 2010 with costs incurred by the purchaser up to the time of settlement of the dispute.

The purchaser claimed for all costs incurred up to the time of the settlement of the dispute in 2010. The IR disallowed all costs claimed after July 2008 on the basis that the taxpayer was not in business after the contract was terminated and therefore there was no ability to claim expenses after that point. The purchaser appealed this decision to the TRA who ruled as follows;

1. The business ceased in July 2008;
2. After July 2008, the purchasers sole focus was on trying to minimize its costs of a "deal gone wrong" and this in itself was not indication of the vendor still being in business;
3. The TRA upheld the IR view that the business ceased in July 2008 and as there was no nexus between the property development business and the ongoing expenses (legal costs, planning fees, accounting costs and settlement to the vendor) no deduction was available.

This strict interpretation of time of closure of the business is probably tighter than what most professional observers would have predicted and a shorter timespan than what may have been utilised in the past. If you are in the position of carrying debt forward with the corresponding interest costs after the sale of a business, you can expect deductions available from those interest payments to cease from the point the business ceases.

Tax payments

There have been some recent changes in the way that we all pay our tax. In the past Westpac Bank had been an agent of IR for accepting payments, as were NZ Post. Recent changes have meant that Westpac can only accept payments of tax made by Eftpos or cash and that cheque payments will only be available at IR offices. Cheques must also be received by IR on or before the due date, as opposed to being mailed with a postmark of "on or before due date". These changes really just reflect reality. In 2014 83% of all tax payments made were made electronically. This figure is up from 75% in 2013 and shows the rapid transition to electronic banking by the vast majority of the taxpaying population over the last 5 years or so.

On a practical level, we are aware of instances where clients using the Westpac Bank payment option (either cash or EFTPOS) have had difficulty making their payments. It is important that anyone paying their tax in this manner has all the necessary information required to allow correct identification of the payment by IR. This includes correct IRD number, type of tax and the period to which the payment applies (this could be a month (for PAYE & GST) or a year (for income Tax).

Tax residency

Tax residency is important in establishing a person's tax liability. With the increasingly mobile population that we (and the rest of the world) have, we are being required to consider whether a person is a NZ tax resident or not more and more often.

In simple terms if you are a NZ resident, you are taxable on your worldwide income by NZ, while if you aren't a resident but receive NZ income you are only taxable by NZ on your NZ income.

IR have produced a set of guidelines for determining residency which are useful but not exhaustive. If you are still unsure after considering your own circumstances of your status, IR have a form that can be completed and sent to them seeking their view of your status. This form (IR886) will allow IR to express their opinion. Any opinion IR express in response to the form is just that – an opinion. It is not binding on IR but would rather be a good guide as to the most likely outcome. The only way of getting a ruling that is binding on IR is to make formal application for a Binding ruling and the costs of doing this would most likely preclude the vast majority of people from considering this option.

Tax residency can be a difficult area. The message is that if you consider you have a potential difficulty in this area you seek advice. We are able to help with this as we have significant experience in the area as well as access to other specialist professionals if we feel a second opinion is warranted.

Where is the world going in the short to medium term?

Having been recently involved in interviewing a number of the largest fund managers in NZ on behalf of a client looking to undertake significant investment, it is interesting to note their answers to the question on their views of the state of the world economy and its prospects over the next few years. While everyone has been a little different, there have been a few common themes;

1 Overall World equity markets have perhaps more upside in them at present than the NZ (and to a lesser degree Australian) market as a result of valuations currently being high in this part of the world when compared with historical earnings averages;

2 Interest rates are at all time lows with many central banks involved in "money printing" in some form or other to try and stimulate growth in their economies. Should some form of correction downwards occur the central authorities have very little room to move;

3 The US economy is one current relatively shining light with Interest rate rises in the US forecast for the second half of this year;

4 Chinese growth rates are slowing down to levels not seen in over a decade, the impact of which is currently negatively affecting the Australian and NZ economies with further slowing likely. The impact on NZ & Australia of a further slowing is self evident;

5 The Eurozone is in general depressed and any economic recovery is likely to be a long time coming with low interest rates and "Quantitative Easing" (otherwise known as money printing – poor old Bruce Beetham would turn over in his grave and mention the words "I told you so!") being used to ensure that some growth is encouraged.

6 As a result of the situation in Europe some of the fund managers believe there are good equity market investment opportunities in Europe on a selective basis.

7 The historically low interest rates available at present make it difficult for Bond markets to produce good returns as rates are more likely to go up than down in the medium term. As a result most Bond managers are invested shorter than is normal to take advantage of rising rates when they start to occur.

Everything that this writer has gleaned from discussions with the various fund managers is that the old adage still applies. Diversification is still the best method of protection against volatility in these uncertain times.

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