DowseMurray
Chartered Accountants
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Newsletter

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Introduction

Thanks for all your patience over the past few months – it's been a busy time! You may be interested to know we are now a Xero partner - more about this online accounting package later in this newsletter. Important: GST is due 28 October and the second provisional tax payment for 2008 is due on Wednesday 7 November.

Topics in this Newsletter

- GST due 28 October
- Provisional Tax Due 7 November
- Alignment GST and provisional tax
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GST

If you file GST returns one monthly, two monthly or six monthly you will have a return due for the period ended 30 September 2007. Payment is due 28 October, not 31 October as in the past.

This earlier payment date is part of the alignment of GST and provisional tax payment dates which is due to come into force from 1 April 2008. For more information about the alignment please see below.

As 28 October is a Sunday payment will be accepted on Monday 29 October. If you wish to make payment over the internet then you will still need to make your payment by your bank's cut-off on Friday as payments made later than that via internet banking will not be received at IRD until Tuesday 30 October and a 1% late payment penalty will be incurred – that's $150 on a $15,000 GST payment.

Provisional Tax Due

The second instalment of 2008 provisional tax is due on Wednesday 7 November 2007.

Make sure you make payment on time as IRD will charge penalties at 1% for the first day late and this is increased to 5% of the unpaid or underpaid amount by the end of the first week overdue. Remember too that interest may also be charged at 14.24% on any underpayment.

If your 2007 tax return has already been completed then we will have sent you a schedule setting out your provisional tax payments for 2007/8.

If your 2007 tax return hasn't yet been filed with IRD then you will have to base your calculation on your 2006 income. If your income for the 2007 year that hasn't already had PAYE or withholding tax deducted is likely to be less than $112,000 then you can calculate your provisional tax for 7 November at 110% of your 2006 residual income tax, and pay a third of that amount. Your residual income tax is basically the tax you had to pay last year on your self-employed or shareholder employee income.

So, for example if your residual income tax for 2006 was $14,000 then provisional tax for 2007/8 would be $15,400 (ie 110% of $14,000) and the payment on 7 November would be $5,133.33. Remember to pay on time or you may be charged penalties and interest.

If you have not made a payment at 7 July then you should make two payments at 7 November. If this is not your first year of business IRD will charge you late filing penalties and interest until the outstanding amount is paid.

If you pay more than $35,000 a year in tax but you are not paying PAYE then you are probably earning more than $112,000 after all tax-deductible expenses and paying provisional tax. At this tax level you must estimate your income and you will be charged interest on any underpayment of provisional tax on the basis that you have had the use of the money.

If you are in this situation you should monitor your income closely throughout the year. If you are earning more than you had expected when you made your July payment then you may want to increase your November payment and top up the July one. This will reduce any interest payable. If you find by March that your income has tapered off then you can reduce the 7 March payment.

If you wait until your tax return is filed you may end up paying considerably more interest than you expected!

Alignment GST and Provisional Tax

From 1 April 2008 payment of GST and provisional tax are going to be aligned.

For most clients who pay GST two monthly or six monthly and pay provisional tax the payment dates next year will be as follows:

Two monthly GST payers:

	GST	Prov tax
April - May	28 June	
June-July	28 August	28 August
August-September	28 October	
October-November	15 January	15 January
December-January	28 February	
February-March	7 May	7 May

Six monthly GST payers:

	GST	Prov tax
April-September	28 October	28 October
October-March	7 May	7 May

Terminal or final tax for the previous year will continue to be due on 7 April.

The purpose of these changes is to reduce paperwork as only one form, a GST 103, will be required. But as you can see this may cause cashflow issues particularly for those making GST payments six monthly so careful cashflow management may be required.

Ratio method

Concerns have been expressed over many years by those who have to pay provisional tax based on their expected earnings but who do not earn income regularly during the year. This particularly affects contractors, seasonal workers and those in businesses such as the film industry as well as new businesses but it also affects those who have periods of redundancy and those who are on long holidays.

The ratio method is being introduced by IRD from 1 April 2008 and it allows businesses to calculate their provisional tax based on their earnings as shown in their GST return. This only applies to those on one or two monthly GST returns. However if you are preparing six monthly returns and would like to use the ratio method you can change to two monthly GST returns.

You also need to have been in business for more than a year but it doesn't apply to partnerships or those with tax last year of more than $150,000.

How the ratio method works: IRD calculates a ratio based on your tax for last year divided by your GST taxable supplies last year. Your GST taxable supplies will usually be your turnover for the year including GST.

An example follows. Your residual income tax for the year ended 31 March 2007 was $50,000 and this was before taking into account any provisional tax payments made. You also had taxable supplies for GST purposes of $600,000 and this was before taking off the GST on any inputs.

This gives: $\frac{50,000}{620,000}$ or 8%.

This ratio will then apply for the 2008 provisional tax payments and IRD will advise you of your ratio. So when you complete your next GST return you will multiply the ratio by the taxable supplies to give you the amount of provisional tax to pay at that instalment. So if you had taxable supplies (generally sales) for April and May of $130,000 then you would pay 8% or $10,400 as provisional tax.

For two monthly GST return filers it will mean making 6 provisional tax payments during the year, with every GST payment. If you file GST returns monthly you will also make six provisional tax payments, one with every second GST return.

The ratio method would suit those with lumpy income or those who would prefer more regular cashflow but you can still use the estimation or standard options.

Budget Update – R&D expenditure

The rules around the deductibility of expenditure on research and development have changed in the last budget (07) with the aim of encouraging more investment in R&D.

While it sounds exciting the devil as they say is in the detail!

From 1 April 2008 tax credits of 15 cents will be available for every $1 spent on eligible R&D expenditure. A tax credit reduces the actual tax you pay.

Eligible R&D Expenditure includes "core" and "supporting" R&D. Core activities are defined as systematic, investigative and experimental activities that seek to resolve scientific or technological uncertainty or involve an appreciable amount of novelty. They result in new knowledge or improved material, products, devices, processes or services.

Supporting activities are tied in with the activity and may include essential and associated administrative support for the core activity.

It appears that the R&D process must be planned with a hypothesis formulated and the experiment monitored against the hypothesis.

Activities specifically excluded are: resource exploration, research in social sciences, the arts and the humanities, market research, patenting and feasibility studies. However some of these activities could be considered supporting activities.

The actual costs may be claimed including salaries, depreciation, training and overheads but other costs such as professional fees, interest and financing costs and the development of in-house software for internal use (which exceeds $2m) may not be claimed.

If you think you may be eligible it may be worth providing your project plan and hypothesis to IRD before you start to ensure any planned expenditure will be eligible for the tax credit. A detailed R&D tax credit claim will need to be filed with your tax return to claim the credit and the detail around this new legislation will be finalised over the next few months.

Overseas Investments

If you own investments costing more than $50,000 in your own name outside NZ then you will have to pay tax based on the lower of the actual income received or a fair dividend rate. The fair dividend rate (or FDR) is currently 5% and is calculated on the market value of the investment at 1 April 2007.

It is therefore very important that you obtain the market value at 1 April 2007 of any shares you hold in any country other than NZ.

This should be done promptly as trying to find this information to complete your tax return in the middle of next year may be very difficult and costly.

We will cover this in more detail, including the treatment of Australian shares, in the next newsletter.

Accounting Systems

We are often asked to recommend appropriate accounting software but there is no "one size fits all" answer as each business has different needs.

However if you are operating a simple system with only a small number of transactions each month, 1-2 bank accounts and no staff eg a consulting company with one or two shareholder employees then using an Excel spreadsheet may be sufficient. You can go one step further and save yourself a lot of data entry by downloading your bank statements directly into an Excel spreadsheet. This also means your spreadsheet cashbook will tie in with your bank statements, making your accountant's job easier. Typically Excel has no additional cost and is generally well understood by users. The biggest problem is ensuring that the details tie in with the bank statements.

If your business is more complex, for example you have a larger number of transactions and more staff you may prefer to use a specialised accounting package. These range from Quick books to MYOB which are database systems that require manual input of all transactions. These packages provide a range of reports including GST return information. You can buy a package such as MYOB for around $300 as a one-off cost.

Other products such as BankLink download bank statement information into the accounting system. You can then code any unexplained items to the appropriate expenditure or revenue category and the system will provide you with report information when required. This uses less manual input than the database packages and provides instant bank reconciliation as the information has come from the bank statements. However it will only provide you with information that has been processed by the bank – unpresented cheques will not be included until presented so that may distort your cashflow. It costs around $60 per month and you need to go through an accountant to use it. Go to www.banklink.co.nz for further information.

The newest product, Xero, also feeds bank statement detail to an accounting system but allows you to access all your information online and make any adjustments online. It has been designed to be easy to use for clients. Your accountant can also log on and tidy up any errors, year end adjustments etc. It has been designed to intelligently recognise transactions so that client input is minimised but again it does rely on bank information so if significant cheques have not been presented they will not be included. Given the move to more electronic banking this has become less of an issue. It costs $50 per month including support and would suit those who like to use the internet for their accounting.

We are now a Xero partner as it fits with our own internet based business. As we have undertaken training on Xero we would be happy to talk to you about it. Go to www.xero.com for more information or call us.

Contact details:

Please remember that the information in this newsletter is of a general nature only. For advice relevant to your situation please contact us.

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