Newsletter

October 2016

DB CHARTERED ACCOUNTANTS LTD

Contents:

"The road to success is always under construction."

In this newsletter we cover the latest landlord's responsibilities under the Residential Tenancies Act, cashflow issues for a growing business and IRD's focus on the cash economy. Insurance, a book review, employer records and tax dates are also covered.

RESIDENTIAL PROPERTY UPDATE – LANDLORDS RESPONSIBILITIES

Changes to the Residential Tenancies Act have implemented the following:

Smoke Alarms

From 1 July 2016 all residential rental properties must meet the following requirements:

- Landlord to make sure smoke alarms are in working order at the beginning of every new tenancy
- Tenant is responsible for replacing batteries (if required)
- There must be a minimum of one working smoke alarm within three metres of each bedroom door
- In any caravan or sleep-out there must be one working smoke alarm
- Any new or replacement alarms must be photoelectric smoke alarms with long-life batteries that have a life span of at least eight years (hard wired smoke alarms are also acceptable)

Insulation

All residential rental homes in New Zealand will be required to have insulation to keep a home warm in winter and cool in summer. Social housing must be insulated by 1 July 2016 and all other rental homes by 1 July 2019. This will include ceiling insulation and timber flooring insulation. (There are exceptions where the subfloor has less than 350 mm of clearance or a flat roofed property.)

The cost of smoke alarms will be a tax deductible cost, however, insulation costs would generally be a capital improvement and so not tax deductible.

The Act also introduced updated rules to speed up the process for landlords regaining possession of abandoned properties.

BUSINESS GROWTH AND CASHFLOW

Growth in a business can be a great thing. Increased sales, increased customers and all being well, an increase in profitability. However, a growing business can mean cashflow pain and cashflow can often be an issue. Why?

Increase in Stock on Hand – If sales are increasing bigger stock levels may be needed to meet demand. If paying for stock today, this may not be sold until next month and then funds not received until the following month. This can mean a 40-70 day lag before receiving a pay back from the increased stock.

Increase in Purchases – Even if goods are not received into stock, there could be an overall increase in required monthly purchases, with a significant time lag between payment and receipt from customers.

Increase in Accounts Receivable – If you sell goods or services on credit, any delays in receiving payment will impact on the cashflow. If clients are extending terms out past 30 days, this can significantly reduce available cash and bank funds.

Wages – If new staff have been taken on to meet customer demand and service requirements they may get paid weekly or fortnightly. However, the work they are completing may be invoiced monthly (and then payment received 30 days after that). The cost of wages will need to be covered until customers pay their accounts.

Increase in GST Payments – While you may budget for $X per month for GST, increased sales will mean an increase in the regular GST payments.

Tax – Just when you think you are on top of things, the IRD will want their share of increased profitability. If no allowance is made for this, the terminal tax payable will be significantly higher than the provisional tax paid.

Profit Margins Not Being Maintained – The increase in sales (and purchases) may be great for the ego, however, if the gross profit or overall profitability has reduced the final net profit could be lower than anticipated.

In summary, if in growth mode take the time to assess the impact on cashflow and set expectations around expected profitability so actual results can be monitored against forecast. It is always easier to ask for a loan or extension on an overdraft well before you need it.

Social Media

I've given up social media for the New Year and am trying to make friends outside Facebook while applying the same principles. Every day, I walk down the street and tell passersby what I've eaten, how I feel, what I did the night before, and what I will do tomorrow. Then I give them pictures of my family, my dog, and me gardening. I also listen to their conversations and tell them I love them. And it works. I already have three people following me - two police officers and a psychiatrist.

THE CASH ECONOMY – STILL AN IRD FOCUS

As we have mentioned before, the Cash Economy is an area that IRD are putting more focus and resources into. While it is not illegal to pay a tradesman in cash for a job well done, it is illegal for the tradesman to not declare this income in a GST or income tax return. Once found out, the IRD will impose shortfall penalties, late payment penalties, interest and of course, require payment of the tax itself.

The IRD has a number of tools at its disposal to find the likelihood of cash not being returned as income, including:

- Comparing gross profit, gross margin, net profit ($ and %) against similar businesses and industries.
- While for some businesses a large number of transactions are processed through EFTPOS, the IRD has a rough estimate (based on averages) how much, as a percentage of turnover, cash sales would be. (In fact, IRD can contact Paymark and credit card companies directly for a particular business to compare EFTPOS sales information against GST returns filed.)
- PAYE unpaid – with the huge number of tax returns filed each year the IRD has a good database of average costs for a particular industry. If wages costs are well below average, the IRD could investigate if wages are being paid "under the table" with no PAYE being deducted.
- A taxpayer being dobbed in directly to the IRD.

While cafes, restaurants and liquor stores have previously been in IRD sights, the focus is now moving to the construction industry, including sub-trades, to reduce tax leakage. For every $1 spent on audit the IRD will generally achieve a $6 return, so for them it is money well spent.

PERSONAL INSURANCES – What can be claimed for tax purposes?

Loss of Earnings/Profits Insurance – When the benefits are calculated with reference to income lost by the insured, IRD's view is that any benefit from this type of policy is assessable income. Any personal premiums paid can, therefore, be included as a tax deductible expense in a personal tax return.

Sickness and Accident Insurance – These policies will generally provide for a specified lump sum payable to the insured as a result of accident or sickness. Generally, any payout will be exempt income and not taxable, provided the payment is not calculated according to a loss of earnings. In this case, premiums are not tax deductible.

Life Policies (as security for a loan) – While costs to arrange business finance are generally tax deductible, the IRD has stipulated that premiums paid for a life insurance policy as a requirement of obtaining a loan are not tax deductible.

BOOK REVIEW

"The Real Life MBA" – Jack and Suzy Welch (2015)

The General Electric ex-CEO tries to simplify business as he sees it including confirming a business is committed to its core purpose (or redefining it) so that the organisation can make sure it has the right people (in the right positions) on board. Crisis management is covered (Welcome to the Coliseum – "Almost every day the Internet demands a head on a platter"). Perhaps the main advice here is that "This too shall pass" – even though it doesn't feel like it when you are in the thick of it. Lessons on marketing, finance and leadership are covered. If a set back occurs, own it and fix it. Retirement gets a mention as well, mainly as a chance to reinvent yourself and direct your energies into different areas. While a career/business/job ends, life does not.

PROPERTY – New lending restrictions – What's changed?

New loan LVR (loan to value ratio) restrictions are being introduced by the Reserve Bank from 1 October 2016, however, most banks have already started to implement the new rules.

Generally the new rules require (for all of New Zealand):
For an owner-occupier property the LVR to be set at 80% - this means a 20% deposit will be required.

For residential property investors the LVR to be set at 60% - meaning a 40% deposit will be required (and is generally the same for commercial property).

In some cases there may be exemptions for new builds and first home buyers.

Existing lending will generally be okay but if looking to top up a loan the new LVR rules are likely to apply.

EMPLOYERS – RECORD KEEPING

MBIE is penalising employers who do not keep adequate records for the staff they employ.

The requirements include:

Full employee details, a written signed employment agreement, details of hours worked each day (including start time, finish time, non-paid breaks, days of employment in each pay period), wages paid each pay day and method of calculation.

For those in the farming or other seasonal sector the minimum pay rate ($15.25 per hour worked) needs to be met.

If you would like to discuss anything mentioned in our newsletter please contact us at:
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IMPORTANT TAX DATES

30 September	Student loan repayments due for overseas-based borrowers
28 October	2 & 6 monthly GST Returns due. 1st 2017 Provisional tax payments due (May balance date).
28 November	2 monthly GST Returns due
15 January	2 monthly GST Returns due (October/November period). 2017 Provisional Tax instalments, student loan interim payments.