NEWSLETTER

September / October 2022

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"One small positive thought in the morning can change your whole day"

DB CHARTERED ACCOUNTANTS LTD

In this newsletter we cover Income from holiday accommodation, what an FBT reimbursement is, current ratio (working capital ratio), the 2022 adjustment to the square metre rate and Banklink retiring.

INCOME FROM HOLIDAY ACCOMMODATION

Income earned from providing short-term accommodation is taxable and required to be included in your tax return. This includes income earned from letting property via Airbnb, Book a Bach or similar websites. Generally, a deduction is allowed for the costs of providing the accommodation - the calculation for deductible expenses will vary depending on the use of the property. If the property is used solely for short-term accommodation, then the costs directly related to the derivation of income will be deductible in full.

If the property is used part privately (including friends and family) and partly used to earn income, then mixed use asset rules apply.

Mixed Use Assets

The mixed-use asset rules apply to property where assets are sometimes used privately, sometimes used to earn income, and are also unused for 62 days or more during the income year.

Income received from renting out the dwelling is generally taxable. Where income is received from family members or at mates rates (less than 80% of market value), this income is treated as exempt income - and you can't deduct expenses for those days.

Expenses

Expenses relating solely to the rental activity are 100% deductible. This would include advertising costs, supplies and cleaning in relation to paying guests.

Other property expenses must be apportioned between the income-earning use of the dwelling, and the private use. This would be the case for expenses such as power, internet, interest on home loan, property insurance, rates, repairs and maintenance, depreciation on chattels.

These expenses are apportioned and deductible based on the following formula:

Income-earning nights / (Income earning nights + Counted nights)

Income – earning nights: Nights the dwelling is used to earn income, other than exempt income

Counted nights: Nights the dwelling is used, but are not "income-earning nights".

If the net rental is a loss, the loss will get carried forward to offset future mixed asset income.

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Note that the above calculations are based on the mixed use asset rules. Where the property is not unused for more than 62 days the standard tax rules apply – those rules are slightly different in that “mate’s rates” income is taxable.

To apply the tax rules correctly remember to keep good records including:
- the number of nights you rent out the dwelling at market value, and how much income you receive for this;
- the number of nights you rent out the dwelling at “mates’ rates”, and how much income you receive for this;
- the number of nights you, or people you’re associated with, used the dwelling;
- when the dwelling was available to be rented out (this will be relevant if the standard rules apply)
- any expenses you want to claim deductions for

WHAT IS A FBT REIMBURSEMENT?

Fringe Benefit Tax (FBT) is calculated when a motor vehicle is provided to an employee (including shareholder-employees) and the vehicle is “available” for private use. Exceptions to this rule include sign-written vans and utilities (but only, where the only private use is home to work travel).

The “value of the benefit” is deemed to be 20% of the vehicle cost. E.g. a vehicle costing $40,000 will have a benefit valued at $8,000 ($40,000 x 20%). FBT tax is then calculated and paid on this benefit (generally at 49.25% or 63.93%) – in this case annual FBT payable would be $6,157 (FBT plus GST on benefit)

Where an employee contributes to the vehicle running costs the “value of the benefit” is reduced.
For a number of our clients who are shareholder employees, instead of having them pay FBT we record an accounting entry to reduce the value of the benefit to nil. This then means that FBT is not required to be paid to the IRD.

An example is shown below:

Value of Benefit	$ 8,000
Less Contribution by shareholder (via accounting entry)	($ 8,000)
Net FBT benefit	Nil

The cost to the company/shareholder includes:	
Tax on the GST exclusive contribution	$1,950
GST on contribution	$1,044
Net Cost to shareholder (excluding reduction of current account)	$2,994

The Company is entitled to claim 100% of the vehicle running costs, servicing, repairs, fuel, depreciation and GST on the purchase.

Using this method there is no need to keep a log book and you can have unlimited private use of the vehicle. After three years ownership this may need to be reassessed as the depreciation benefit reduces. Other factors include the price of the vehicle and the annual running costs.

Instead of being subject to FBT, Shareholders/Employees can have the company just claim the vehicle costs based on the business usage. To do this a log book would need to be kept for a 3 month period (and see our October 2017 newsletter for more information – available on-line on our website).

JOKE

At an art gallery, a woman and her ten year old son were having a tough time choosing between one of my paintings and another artist’s work.

They finally went with mine.

“I guess you decided you prefer an autumn scene to a floral,” I said.

“No,” said the boy. “Your painting’s wider, so it will cover three holes in our wall.”

CURRENT RATIO (WORKING CAPITAL RATIO)

The Current Ratio measures the ability of Current assets (once they are converted to bank funds) to cover immediate debts (Current liabilities).

The Current Ratio calculation is: Current Assets divided by Current Liabilities

Current Assets includes:	Current Liabilities includes:
Bank Funds	Bank Overdraft
Account Receivable	Accounts payable
Other Receivables – e.g. tax refund	GST & Tax payable
Stock on Hand or Work in Progress (WIP)	Immediate loan/finance payments due

As an example, a business with:

Current Assets:
Bank funds $20,000, Receivables $80,000 and Stock $30,000 – Total $130,000

Current Liabilities:
Accounts Payable $50,000, GST Payable $15,000, PAYE Payable $10,000 – Total $75,000, would have a **Current Ratio of 1.7** ($130,000/$75,000).

Generally this would mean that as funds come in there are enough funds to pay amounts payable.

However if Accounts payable were $100,000 (total liabilities of $125,000), the **Current Ratio would reduce to 1.04**. At this level the business would have to carefully monitor cash in and cash out to ensure that it is able to pay its bills/outgoings.

Areas that can impact the current ratio include:

- Poor trading results
- New assets paid for from bank funds – this reduces working capital, whereby if financed the asset can be paid off over a longer period
- High business debt compared to trading results
- Owner drawings that are too high for the business to manage.

Another measure is the **Quick Ratio**, this excludes Stock/Inventory from the calculation as these items are slower to turn into cash.
In the above examples the Quick Ratio would be 1.30 and 0.80. At .80 the business “quick” assets are not enough to cover immediate debts/outgoings. It may need to consider a bank overdraft, ensure that stock on hand is at the right levels (and not obsolete) and ensure that WIP is invoiced on a regular basis to maintain cash flow.

Current Ratio

Current Assets / Current Liabilities

e.g 130,000 / 75,000 = 1.70

Quick Ratio

Accounts Receivable less Stock / Current Liabilities

e.g 100,000 / 75,000 = 1.33

SQUARE METRE RATE – HOME USED FOR BUSINESS

Business owners often use their private residence for both business and private purposes. This means that the business owner may be able to claim deductions for this business use. IRD provides a square metre rate calculation that can be applied. Calculating the deduction is a three step process.

One - identify the business square metres. This is the area of the private residence that is primarily used for business purposes, and can be separately identifiable as being used for business. The business square metres are then multiplied by the commissioners square metre rate (this rate is adjusted annually). For the 2022 income year this rate is $47.85 per sq.metre. This rate covers the costs of power, gas, insurance, phone and internet.

Two - divide the business square metres by the total area of the buildings on the premises. This calculates what proportion of the total premises costs is business related (expressed as a %).
Premises costs is made up of the annual mortgage interest, rates and rent that have been paid in relation to the premises for the income year. The business related percentage is then applied to the total premises costs of the buildings and their curtilage, calculating the second deduction.

Three - add the two deductions from step 1 and 2 together to get the total amount that can be deducted for the income year.
As an alternative to the above steps all property and occupancy costs can be apportioned as per the business usage percentage.
For our clients we generally calculate the annual home use claim when compiling the annual financial statements and tax returns, if we have the relevant information.

BANKLINK IS RETIRING

We have been advised that Banklink software, which we have used for many years, is to be de-commissioned. As a result we have found a new provider to provide us with bank feeds of bank transactions for our client bank accounts.
We have elected Xero as our new provider. For our GST clients and those who currently use Banklink, we will be in touch in the next 1-2 months to get the relevant forms signed in order to change to the new system. This will not result in any increase in our pricing for services.

IMPORTANT TAX DATES

20 September 2022	- PAYE Payment due - Payday returns to be filed 2 days after pay day.
20 October 2022	- PAYE Payment due - Payday returns to be filed 2 days after pay day.
28 October 2022	- 2023 (1st Instalment) Provisional Tax (6 Monthly tax-payers).
28 October 2022	- April-September 2022 (6 monthly & 2 monthly) GST Return Due.
20 November 2022	- PAYE Payment due - Payday returns to be filed 2 days after pay day.

JOKE

Teacher: "If I gave you 2 cats and another 2 cats and another 2, how many would you have?"
Johnny: "Seven."
Teacher: "No, listen carefully... If I gave you two cats, and another two cats and another two, how many would you have?"
Johnny: "Seven."
Teacher: "Let me put it to you differently. If I gave you two apples, and another two apples and another two, how many would you have?"
Johnny: "Six."
Teacher: "Good. Now if I gave you two cats, and another two cats and another two, how many would you have?"
Johnny: "Seven!"
Teacher: "Johnny, where in the heck do you get seven from?!"
Johnny: "Because I've already got a freaking cat!"

If you would like to discuss anything mentioned in our newsletter please contact us at: DB Chartered Accountants Limited.
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