Tax Tonic Sept 2020

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Employee Share Schemes

Q: What is the journal entry where employee shares are transferred from current shareholders? Dr P&L share scheme $100k Cr Old shareholder current account $100k?

A: As a general rule we would recommend that transferring shares from existing shareholders (rather than issuing new shares) should be carefully planned and advice sought.
The intent of the new rules is that the company has an increase is ASC (paid up capital) equal to the taxable/deductible ESS benefit (section CD 43(6E)). Therefore the ASC should be credited with the $100k rather than the current account

Q: Could you set up a trust to let employees participate in benefits especially dividends?

A: Yes you could, but it would careful planning and a clear idea of what the company was wanting to achieve. There would still be a taxable ESS benefit for the employees as they are getting the benefits of share ownership (together with the right to dividends and future growth).

Land and Tainting

Q: Land tainting: if not "IN BUSINESS", does it mean it's out of the GST net and to be tainted, needs to be "IN Business"?

A: Income tax and GST are not always in sync when you are looking at land transactions. Sometimes you have GST and no income tax and sometimes you have income tax and no GST. In terms of someone having a land "business" that would undoubtedly be a taxable activity for GST purposes, however if it is a residential rental that is tainted then it won't be subject to GST even if it is in the same entity that is carrying on the business.

Q: Is there any exemption under these rules if the property is used as a genuine residence for the associated party?

A: Yes definitely

Q: Why does the slide say "2 year period for bright line", is it less than the 5 years? (on slide 42 and 44)

A: Good spotting! That is incorrect now – it should be 5 years. (It was 2 years when IRD released the statement)

Q: In the Royal Flush and Ex Prince example where the rental house is tainted by adding on the room, what/when is the cost price calculated ? Is it the cost price or the value at time of improvements?

A: Good question. Unfortunately it is the original cost of the land. Interestingly if the property had been transferred to another associated entity for some commercial reason before the work was done the cost base would be the new cost base. I actually had a question on this last week!'

Fonterra deferred payments

Q: Re Fonterra deferred payments. If I am preparing financials under IFRS and estimate the income based on full estimated payout (eg $7.10), can I then file tax on a different cash basis? Or am I under IFRS accrual rules?

A: The tax rules around derivation take precedence as far as calculating the profit for tax goes (and this is not a Financial Arrangement so these spreading rules don't arise), therefore you could do a tax adjustment to back out the deferred payments until they are actually quantified and paid.

Quick Fire

Q: Quick Fire: if a person has 2020 RIT of $3500, hence not required to pay 2021 prov tax. But when that person files actual 2021 income tax, and 2021 RIT turns out to be $5,500, they become provisional taxpayer for the 2021 tax year. Will there be penalty & UOMI for the no payment of 2021, P1, P2, P3?

A: No provided assuming the 2020 return was filed before P1, P2 and P3. If 2020 wasn't filed at P1 no prov would be payable provided 2019 was below $5,000 RIT was between RIT

Leaky apartment R&M audits

Q: The biggest issue we have with the larger leaky home issues with Body Corps is trying to understand what levies are actually tax deductible. Body Corps are not clear, particularly the larger ones. Most of the time we are left with making a judgement call and at most, taking a conservative approach, anything done for a property shut down sometime for years would have to be seen as structural in its entirety

A: Just because the leaky remediation project takes a few years does not mean it is capital expenditure, ie. it doesn't suddenly mean the work amounts to a "renewing, replacing or reconstructing substantially the whole of an asset" based on the relevant case law, merely due to time taken. A 'conservative' approach may not be helping the client here.
We accept it can be difficult to get sufficient information from Body Corps, and ideally we need a detailed breakdown of the work completed, the builders quotes etc. As a very general guide my approach would be to start with 75-80% as acceptable R&M based on many apartment complexes I've seen.

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