IS YOUR BUSINESS READY FOR A GST INCREASE?

The Government is considering increasing the GST rate to 15%. A rate increase could apply as early as October this year. Businesses must plan now to ensure they are well prepared.

A rate change will have wide implications. It is not simply a case of changing the rate in the accounting system. A rate change will affect consumer behaviour and put pressure on business margins. Systems and pricing issues may arise. There will be opportunities for some and industry specific challenges for others, incurring costs and unnecessary risks.

As a minimum, all businesses should be considering the following matters to ensure they are ready for a possible GST rate increase:

- What changes do we need to make to our accounting system?
- Can our accounting system issue credit and debit notes at the 'old' GST rate after we have altered the default rate to the new rate?
- Can we increase the price payable for supplies?
- Can we cope with higher consumer interest in the lead up to a higher rate?
- Do we have to make a payment basis GST adjustment?
- Do we have to file two GST returns if the rate changes?

Unless specific rule changes are introduced by the Government, the GST 'time of supply' rules– generally the earlier of an invoice being issued or any payment being received – will determine whether GST should be charged at the old or at the new rate. Practically, this means that, if a contract is entered into prior to the GST rate increasing, but no invoice is issued or payments made until after the rate increases, the sale will be subject to GST at the new rate.

Credit and debit notes for supplies that took place before the rate increase would need to be issued at the old rate. Billing systems will, therefore, need to be able to able to cope with two rates of GST for a transitional period.

Attention to pricing expressions in the contract will be vital:

a. If the pricing is expressed as 'plus GST" or similar, the supplier has the right to increase the amount of GST charged to reflect a new rate. For this reason, it is recommended using 'plus GST' in all contractual pricing expressions.
b. If the pricing is stated as 'inclusive of GST', there is a risk that the total price is capped and cannot be increased to cover an increased rate of GST.
c. If the contract is silent on the question of whether the increase can be passed on, the GST Act gives a limited right to gross up the price where there is a rate increase provided that certain conditions are satisfied. This right does NOT apply if the parties have specifically agreed the price cannot be grossed up for a GST rate increase, or where the relevant agreement was entered into more than three months after the introduction of a new GST rate.

Whether businesses will wish to pass an increased GST cost on to customers is a commercial question. It should not be assumed a GST rate increase will automatically result in higher prices.

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GST INCREASE - COMMERCIAL ISSUES

Experience from the last increase in 1989 suggests consumer spending will rise immediately prior to a GST rate increase.

Consumers will be focused on achieving savings on the rate increase so there is likely to be an increase in purchases of consumer goods (e.g. furniture, home appliances and electronics). Goods purchased on lay-by could be paid off earlier, hire purchase arrangements that 'lock in' the lower rate will be popular and there may be a push to go unconditional on house purchases earlier. Consumers may seek to prepay any recurring costs (e.g. rates, insurance premiums, gym membership subscriptions) where they perceive a price advantage in doing so.

In 1989, there was a dip in retail consumption immediately after the rate increase. It is therefore prudent for businesses to be ready for potentially increased demand in the months leading up to the rate change and also plan for possible decreased sales immediately after.

GST cannot be recovered where the tax invoice shows the incorrect rate (or amount) of GST. Businesses in this case should request a corrected tax invoice. There should not be any issues taking a deduction where the tax invoices shows the total price paid and a statement that is GST is included.

However, if the tax invoice shows an incorrect rate and amount of GST, there is a risk it is not a true 'tax invoice' for GST purposes. Businesses which hold perpetual or scheduler tax invoices, such as for ongoing leases payments, may need to request updated tax invoices.

There may be commercial (and relationship) issues where an 'invalid' tax invoice is provided. Purchasers may refuse to pay unless a corrected tax invoice is issued. Suppliers will need to ensure their system and any pre-printed tax invoices showing applicable GST rate are updated on time.

GST INCREASE - PRACTICAL BUSINESS CONSIDERATIONS

Product pricing, deposit amounts and similar may need to be updated. Some businesses will bear a greater GST cost or have greater GST timing disadvantages. A shift in rate to 15% would represent a 20% increase over the current rate.

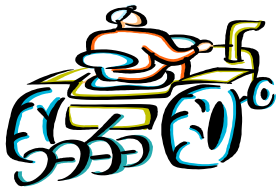
Businesses must fund the timing cost of GST (i.e. pay GST on costs upfront and then recover this outlay via a deduction in GST returns). This funding cost may be offset by the GST collected on sales. Where a business is always in a GST refundable situation or does not charge and collect GST (e.g. exporters, banks), there may be an increase in the funding required to carry the GST on costs.

An increase in the GST rates raises the stakes for GST compliance issues. More than ever businesses will need to be comfortable that their GST processes and controls are robust and can withstand Inland Revenue scrutiny.

When a rate change occurs partway through a taxpayer's return period, two GST returns are required to be filed. This will be relevant for taxpayers filing two or six-monthly GST returns.

Customers who decide to pay early will need to be catered for – especially when supply contracts are with end consumers and span the rate change date.

The new 'tax fraction' for a 15% rate can be calculated by either multiplying the GST inclusive amount by the fraction 3/23 (e.g. $100 x 3/23 = $13.04) or dividing by 7.6 recurring.



INTERNATIONAL RECESSION BITES FARM INCOMES

While the international recession has impacted on growth of agricultural wages and salaries, the 2010 Rabobank/Federated Farmers Farm Employee Remuneration Report shows farm workers are still considerably better off than their urban counterparts.

This year's Report was produced from a comprehensive survey of members of Federated Farmers, conducted between August and October 2009. It shows that it has been a very tough year so far for farm employers as they have faced a very high dollar with increasing pressure on interest rates to rise sometime over 2010.

The Survey reports that average wages and salaries increased highest in the arable sector (up 8.1 per cent), followed by sheep and beef, up 4.4 per cent, and dairy, which arguably suffered the wildest income fluctuations over the past year up 2.1 per cent.

Farm workers earned an average salary of $43,294 (up 3.3 per cent in the year to October 2009). However, the total package value for farm workers (with salary and benefits) was $48,388 (up 4.4 percent in the year to October 2009). This is $5,227 more than the average personal (mean) annual wage and salary income, $43,161, as recorded by the Statistics NZ Household Economic Survey.

The total package value for the most senior managerial positions averaged $80,265 (dairy), $72,099 (arable) and $63,613 (sheep/beef).

There has been a fall in level of remuneration being paid to casual farm workers. Unskilled farm labourers saw their hourly rates fall by almost a dollar and, while they had a much smaller decline, even skilled casual workers saw a fall in hourly rates. Casual skilled staff earned on average $19.80 per hour - casual rates remain highest in the North Island. Unskilled casual labourers earned $16.99 per hour. This arguably reflects a sharp pruning of farm operating costs with employers moving resources to retain skilled permanent staff at the expense of casual staff.

LEGAL EXPENDITURE CAPITAL VERSUS REVENUE

There is no specific provision which governs the deductibility of legal fees. Broadly, the deductibility provisions require an expense to be incurred in running a business or deriving gross income and not be capital in nature. A general rule of thumb that is often followed is to determine the purpose for which legal fees were incurred and follow the treatment of that underlying purpose.

For example, if a person acquires a rental property and that rental property represents a capital asset, the legal fees incurred to acquire the property will be capital in nature and non-deductible (although a portion may be depreciable).

Recognising that the deductibility of legal fees can be a complex issue, legislation has recently been enacted, providing that where a taxpayer incurs legal fees of less than $10,000, the legal fees will be deductible irrespective of whether they are capital in nature.

OFF THE PLAN!

Have you sold property purchased 'off the plan'? The Inland Revenue is targeting profits made on the sale of properties resold before the contract to purchase becomes unconditional.

In a recent publication, the Inland Revenue outlines its view on the tax treatment of such transactions. According to the Inland Revenue, if you sell a property while the contract is still unconditional, any gains made will be taxable no matter what your intention was when you acquired the property.

The Inland Revenue's reason is that, if the contract is still unconditional, you can choose to cancel it rather than sell the property. This position is contentious.

TRUSTS AND PRESCRIBED INVESTOR RATES

Personal income tax thresholds and rates changed as from 1 April 2010 and as a result consequential adjustments have been made to investors' rates of resident withholding tax ("RWT") and their portfolio investor rates ("PIRs").

All investors with a PIR of 19.5% at 31 March 2010 will automatically move to a new rate of 21% for 2010-2011. An Amendment Act passed in December 2009 also allows trustees to elect a PIR of 21% (in addition to the 0% and 30% options) effective from 1 April 2010. This may assist if the income being distributed to beneficiaries on this lower tax rate as they receive the net income with the benefit of an appropriate tax credit.

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FISHING…….NZ STYLE

On a tour of New Zealand, the Pope took a couple of days off to visit the ocean for some sightseeing. He was cruising along the beach at Wanganui in his car when there was a frantic commotion just off shore.

A helpless man wearing a green and gold Aussie rugby jersey was struggling frantically to free himself from the jaws of a five metre shark.

As the Pope watched helpless and horrified, a boat cruised up alongside with two men wearing All Black jerseys. Rangi quickly threw a harpoon into the shark's side. Hohepa reached out and pulled the mauled, bleeding and semiconscious Aussie from the water. Then, using long clubs, Rangi and Hohepa killed the shark and hauled it into the boat.

The Pope was waiting for the heroes as they pulled their boat ashore. "I give you my blessing for your brave actions" he told them. "I have heard there was some bitter rivalry between New Zealand and Australia, but I have seen with my own eyes that this is not true".

As the Pope drove off, Rangi asked Hohepa "Who the hell was that, bro?" "That was the Pope, cuz", Hohepa replied. "He's in direct contact with God, bro' and has access to all God's wisdom"

Well, Rangi said, "He may have access to God's wisdom, but he knows bugger all about shark fishing. Is the bait holding up okay or do we need more Aussie burley?"