



Taxation Advisory Services

Tax developments for property investors WHK and Duke & Cooke Limited

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better advice for a better life

- Tonight's session: Recap last 18 months or so...

- Associated persons changes October 2009
- Budget 2010
 - Changes in tax rates
 - Immediate reduction of depreciation re new assets
 - Depreciation re buildings targetted
 - LAQC reform signalled
- IRD review of what constitutes a “building”
- Actual LAQC reforms put in place



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Associated persons changes

- So-called “tainting”: “Associated person” concept important where you have interests in development-type activities, and long term property investment
- If you get it wrong: Potential for capital gains to be taxed
- Previous “associated person” definition was relatively easy to get around
- From 6 October 2009 much harder to escape “tainting”

Two main situations:

- ‘Taxable land activities’ carried on at time investment land is acquired, or at time improvement to land started
 - Number of potential exclusions, but they do not always apply in a ‘logical’ or ‘fair’ way
- Sale or transfer of land from taxable entity to ‘investment’ entity
 - Eg. Development entity sells land (taxable) to related ‘investment’ entity (which intends to hold for long term purposes)
 - Often overlooked

Tainting: How to manage

- Appropriate advice before transactions occur
- Appropriate structures for joint land ownership arrangements: for example partnerships are dangerous structures as all partners taint all other partners, and an associate of one partner can taint the partnership (all partners)
- Take the time to get this right, as mistakes can be very expensive

Budget 2010 – income tax rate changes

- Personal tax cuts:
 - *\$0 to \$14,000: 12.5% reduced to 10.5%*
 - *\$14,001 to \$48,000: 21% reduced to 17.5%*
 - *\$48,001 to \$70,000: 33% reduced to 30%*
 - *Over \$70,000: 38% reduced to 33%*
- Changes occurred from 1 October 2010
- Company tax cut – 28% from the start of the 2011/12 tax year

Budget 2010: Depreciation changes

Depreciation

- Immediate change: Depreciation loading removed on assets purchased on or after 21 May 2010
- From 2011/12 income year no depreciation allowed on buildings with an estimated useful life of 50 years or more
 - Residential rental and commercial properties
 - Significant impact on a number of property investors and businesses
 - Provisional tax and cash flow considerations

Building Fitout

- Generally speaking an asset can still be depreciated separately when it is not a permanent fixture of the building
 - Residential investment rentals
 - IRD guidelines released May 2010 stating “building” includes most fitout items
 - Represents a double whammy on residential property investors
 - Commercial investment properties
 - IRD statement effectively means no change from previous practice of allowing fitout to be depreciated separately

May 2010 IRD Statement re residential property fitout

- Relatively short list of residential property chattels/fitout items that can be separately depreciated
- Issued as an Interpretation Statement rather than as new legislation
- IRD audit approach

IRD Statement re residential property fitout

- Not separate assets:
 - Plumbing and piping
 - Electrical wiring
 - Internal walls
 - Doors
 - Fitted furniture
 - Kitchen cupboards
 - Bathroom furniture and fittings
 - Lino and tiles (wall and floor)

IRD Statement re residential property fitout

- Separate assets (can be depreciated as separate assets rather than as “building”):
 - Wardrobes and cupboards not built into the wall
 - Carpets
 - Curtains
 - Blinds
 - Water heaters
 - Hot water cylinders

QC/LAQC changes

- Proposals for change released shortly after budget
- Legislation passed 10 December 2010, took different approach from that initially signalled
- Significant change for many clients from 1 April 2011

QC/LAQC changes: Options

- Do nothing – if you have an LAQC it loses its “LA” status
- ‘Re-badge’ as LTC (elect in to LTC rules)
- Move to non-corporate structure (sole trade, partnership, LP) on a tax concessional basis if done within two years
- Elect out of QC regime entirely (and be treated as an ‘ordinary’ company)

LTCs: Limitation on losses

- Government's concern is that losses available > amount 'at risk'
- Limitation rule tries to limit loss availability to 'equity' of shareholder
- Important: 'Owner's basis' needs to be calculated upon entry into new regime, and each year losses are made
- Owner's basis = investments – distributions
+ income – deductions – disallowed amount

Loss limitation rules

- Important to recognise that shareholder advances and security offered by associates can be taken into account
- A lot of companies/shareholders will not be adversely affected
- Will add to annual compliance requirements as each year a loss is made this needs to be recalculated for each shareholder

LAQC changes: Key points

- Good opportunity – not often opportunities to move to new structures or restructure on tax concessional basis, but need to get it right first time!
- LTCs offer some potentially very good outcomes if used appropriately
- Some ‘fishhooks’ in the LTC rules, for example tax on exit, and the fact only one shareholder needs to revoke status for all shareholders to be impacted – make sure these are considered before you jump in

Companies incorporated from 1 April 2011

- Will be able to elect to be LTCs (similar to electing to be QC/LAQC currently)
- Will be company for all purposes other than income tax purposes – effectively a sole trader or partnership for income tax purposes
- Will be very useful (similar to LPs) where there are multiple investors with different tax profiles (onshore vs offshore, taxable vs exempt, with profits vs with losses etc)
- Provide valuable opportunities in some situations

GST on land transactions

- Sales between registered persons to be zero-rated from 1 April 2011
 - Will remove some of the issues around when land is a going concern
 - Exempt portions remain treated as currently eg curtilage
- Issues include what is “land” for these purposes?
More work for the lawyers....
 - Marine farming licenses, forestry rights, exclusive vs non-exclusive rights to use etc
 - Most commercial leases not “land” therefore not zero-rated under this rule

GST on land transactions

- Changes to the way land used for dual purposes is treated for GST purposes
 - Eg. Residential property developed for sale but tenanted for time being pending sale
 - New calculations from 1 April 2011 re what GST is and is not charged on

IRD Audit Activity

- IRD getting \$119.3m additional funding over 4 years (starting 2010/11) to increase audit activity
- \$26m is targeted at property-based audits
- We are seeing more audits and more aggressive approaches from IRD
- investigators appear to have upskilled, doing more preparatory work -> audits are more challenging, more issues being identified, and more technical issues being identified

IRD current focus (our experience)

- GST – claims for assets purchased followed by little or no outputs
- Land – sales post re-zoning

- Questions ?

WHK Tax Consulting Team

WHK in Nelson is fortunate to have a team of four full-time specialist tax consultants. Because we do not prepare annual accounts, GST returns and such like, we are able to spend all our working hours looking for and delivering the most robust and most valuable tax solutions we can.

Whether you are a WHK client or not we welcome the chance to work with you. We are perfectly happy to work along side your existing advisers to help make sure your needs are met, in fact we have had some fantastic successes doing precisely this.

If you think we may be able to help you with the peace of mind you need around your tax affairs call us and lets chat about how we can help you.



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