



February & March 2011

Client Newsletter

Travel Expenditure

Travel expense, like any other expense, is deductible for tax purposes provided it is incurred in the course of business. Travel including accommodation and meal expenses must be connected to the income-earning process of the taxpayer for it to be deductible.

Holiday or Business?

The most common form of travel expenditure is overseas travel. Often taxpayers tag a holiday to an overseas business trip. If the principal purpose of the trip is business, then airfares and all business-related expenses are fully deductible. Expenditure relating to the holiday component of the trip is not deductible. A mere allocation on a percentage basis is not normal – records of the trip must be kept, such as the itinerary, places of business visited, actual business conducted, items of expenditure etc. Any element of private expenditure must be treated as drawings when analysing the expenses for accounting at year end.

If business is merely incidental to a holiday trip then airfares may not be deductible. There has to be a nexus between the trip and the production of income for business portion to be deductible. Where overseas travel to conferences, trade fairs etc relate to the business operations, then such travel is deductible. Often the taxpayer is accompanied by their spouse on such trips. If the spouse is assisting the taxpayer in presenting a paper or expected to attend the function, then usually the spouse's travel expenses may also be deductible.

Purpose of the business trip?

If the business trip is in relation to purchasing a capital asset e.g. a farmer may make a trip to buy a tractor, the travel cost must be capitalised to the fixed asset cost which is then subject to depreciation. Where such travel costs result in the failure to purchase a fixed asset, it is likely not to meet the nexus test for the income-earning process in which case it becomes black hole expenditure. However, if the travel is to gain knowledge of the market or to investigate expanding operations, then the travel cost may be deductible.

As is the case with the deductibility of most expenditure items bordering on grey areas, the above serves as a guideline only and you should seek advice from your advisor.

Depreciation on Buildings

From 1 April 2011 depreciation on most buildings will be eliminated as per the legislation enacted following the budget announcement in May 2010. A new Schedule 39 is in the Income Tax Act which lists the types of buildings on which depreciation may continue to be claimed as they are deemed to have a useful life of less than 50 years.

Some of the items in Schedule 39 are:

- Carports (hired out to householders);
- Portable Huts;
- Cool-stores and freezing chambers;
- Slaughterhouses on farms;
- Plastic hothouse and PVC tunnel houses;
- Glasshouses;
- Buildings affected by acid;
- Milking sheds;
- Wintering barns and simple loafing barns;
- Temporary buildings

Some of the assets in Schedule 39 do not exactly agree with the IRD Depreciation Table. For example, the IRD table deems all “barns” to have a useful life of less than 50 years, and are therefore depreciable, but Schedule 39 deems only “wintering and simple loafing barns” as depreciable. There is no comment on where the “drying barns” or “hay barns” stand. Similarly the IRD Table allows depreciation on “dairy sheds and yards” whereas Schedule 39 allows only on “milking sheds”.

The IRD is aware of these discrepancies and attributed it to the lack of time in the Budget legislation. Amendments are expected shortly, so watch this space.

IETC (independent earner tax credit)

The IETC is a tax credit for individuals whose annual net income is between \$24,000 and \$48,000. Taxpayers are entitled to an IETC for any of the months during the period 1 April 2009 to 31 March 2010 if they:

- are a New Zealand tax resident;
- are not entitled to Working for Families Tax Credits (or received an overseas equivalent) – this includes their partner;
- didn’t receive an income-tested benefit;
- didn’t receive NZ Super or a veteran’s pension or a foreign pension or benefit, or an overseas equivalent of any of the above benefit.

If the taxpayer doesn’t meet the above criteria for even one day of any month they won’t be entitled to IETC at all for that month.

Formal Written Agreements for Family Arrangements

A recent High Court decision highlights the importance of having carefully worded signed agreements for family arrangements to avoid misunderstandings. In this case, a son allowed his mother to occupy a property of his. She occupied the property for 7.5 years. No rent or outgoings were paid for by the mother but she did purchase chattels and maintained the gardens. The son and mother fell out and the son served a Notice to Quit the property.

The mother sued the son. Since she had only been given an “indication” from her son that she could live at the property for the rest of her life and did not have a legally binding agreement, the court found it to be “an unenforceable promise”. If the mother had had a formal written agreement setting out the basis on which she could occupy the property, no court case would have been required.

An agreement of this nature should include the basis of the right to occupy ie permanent or temporary, whether there is a requirement to contribute to the maintenance and the outgoings of the property and what alterations are allowed to be made to the property. A formal written agreement would protect everyone involved in such a family arrangement.

Redundancy tax credit extended

Although the May 2010 Budget repealed this tax credit from 1 October 2010, the Government has now extended to 31 March 2011. The intention to extend the credit is in response to the Christchurch earthquake where without the tax credit, in some situations, people could be taxed too highly if they had worked part of the year.

The redundancy tax credit was originally introduced to provide some tax relief to those who received a redundancy payment. In these situations, the payment often moved the person into a higher tax bracket. This was perceived to be an unfair outcome and the tax credit rectified that situation. The extension will apply to all redundancies received before 1 April 2011. A Redundancy tax credit (IR524) form is required to be lodged with the IRD to claim for redundancy payments received on or after 1 October 2010. It will be paid at the rate of 6 cents in the dollar to a maximum of \$3,600 for each redundancy payment.

Important: This is not advice. Clients should not act solely on the basis of the material contained in the *Client Newsletter*. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. The *Client Newsletter* is issued as a helpful guide to clients and for their private information. Therefore it should be regarded as confidential and should not be made available to any person without our prior approval. 188/2011.