

# Accountable News

## Quote

“A diplomat is a man who always remembers a woman's birthday but never remembers her age.”

**Robert Frost**

## Are Mortgage Break Fees Deductible?

This has been a hot topic over the last year as a lot of people were willing to pay a lump sum now in order to lock in a much lower interest rate for a few years to come.

The biggest disappointment once again is how few people actually consulted with their accountant before taking the plunge – something we have been trying to encourage our clients to do for years now. You may be surprised how much less it costs to get advice first rather than paying for the extra time involved trying to find an exemption later if the issues are complicated.

For mortgage break fees to be deductible we must consider whether:

- it is incurred by a cash basis person (only individuals can fall into this category and must meet other criteria too)
- the mortgage is being terminated whereby the Base Price Adjustment will crystallise the break fees
- the mortgage is being varied rather than replaced

Non-Cash Basis Persons will be required to spread the break fee over the remaining loan term if the interest rate reduction is merely a variation of their existing loan.

By contrast, non-Cash Basis Persons who replace their loan with a new financial arrangement will get a current-year deduction for the break fee under the BPA.

Cash Basis Persons who do not break the preset threshold will get a current-year deduction for the break fee, regardless of whether the loan is terminated or refinanced, on the basis that the amount is “interest” and the general permission is satisfied.

Cash Basis Persons who exceed the threshold due to the size of the break fee are disqualified from the Cash Basis Persons definition and will need to apply the same rules as for non-Cash Basis Persons.

Persons who terminate their existing loans, rather than refinancing them, and incur a break fee in doing so will get a current-year deduction under the Base Price Adjustment regardless of whether they are Cash Basis Persons or non-Cash Basis Persons.

In summary, tax relief by way of an immediate deduction will be available for many persons who incur break fees in relation to their business-related loans. For others, the break fee might have to be spread over the remaining term of the loan. By putting suitable arrangements in place with their banks, persons can ensure that they do more than just vary an existing loan, by terminating the old loan and commencing a new one, and in doing so will ensure that immediate deductibility of the break fee is available in the current year.



## Business

### Tip

#### Create a brand.

Spend a little money to create a professional logo, business card and stationery.

Present a professional image.



### **Reminder:**

If you have not collected your records from the previous financial year could you please do so next time you are in our area.

We do have limited space and with the new work coming in that space is getting smaller.

If you live out of the area at your request we can arrange for them to be couriered to you.

Please contact Kate Mitchell with any issues regarding this matter.

## Business Builder Success Story

Dodd & Associates takes pride in the various accounting processes that we offer and one such process "Business Builder" has proven to be very successful for one client. This client is in an industry which gained unexpected large contracts in the later part of the year which resulted in a large lift in profit. If Companies (and sometimes individuals) have an unexpected lift in profit for the year Inland Revenue charge Use Of Money

Interest (UOMI) which we believe is unbelievably harsh. Business Builder was designed to beat the UOMI charge from IRD. Our client could have been facing significant UOMI had they not signed onto Business Builder. Not only did they receive monthly financial statements which allowed them to manage and respond to changes in their business but they more importantly negated the UOMI charge. This client was able to save

well in excess of \$6,400. This is money that stayed in their bank account rather than being paid to IRD. The saving on UOMI was also more than the fee we charged for the year. Their comment to us was that Business Builder has paid for itself and been a life saver. We recommend those facing uncertainty in their business should sign onto Business Builder. If interested contact Kate Mitchell for a quote.

## Managing Your Tax Account

Because of the incidence of errors in the accounts Inland Revenue maintain for you with the details of the tax you owe them we find it necessary to monitor and track (as best we can given the infrequency of the data available) the correctness of what Inland Revenue believe you owe them. The cost of us doing this is significant and you will recall that we charge an annual fee for that

in February or March of each year. We have for the last two years been trialing a system where we have charged the actual costs incurred for each individual client. Unfortunately, the work required to charge on this basis is disproportionate to the amount of cost recovery we achieve. We are therefore going back to the original system we used of charging a standard fee for

each taxpayer client. For the current financial year we are setting this fee at a nominal \$19.00+GST per taxpayer client. This will again be charged in February or March of next year. We will then assess the overall economics of others to decide whether \$19.00+GST is sufficient for the year ended 31 March 2011.

## IRD Tax Debt Increasing

Parliament has this week reported that the Inland Revenue Department has been ineffective in managing tax debt owing. Between 2004 and 2008 total tax debt grew by 91% to \$1.92 billion. This could balloon to \$8 billion if IRD do not take action.

For a country of 4 million people this is horrendous. Given the Government's forecasted budget deficits it is likely that IRD will take action on this. This action could include court action, personal visit/call from IRD or a letter requesting payment. If you owe the Inland

Revenue Department tax debt you need to be talking to us. We can negotiate with IRD on your behalf. IRD can be understanding when it comes to tax debt. Call your accountant today if you are concerned!

## New GST Policy

As part of the end of year financial statements we attempt to reconcile your GST returns against those we calculate as part of your financial statements. If there is a difference we attempt to identify and note them on our reconciliation form. This is known as a GST reconciliation and is a requirement of the New Zealand Institute of Chartered Accountants. As we are noticing an increasing trend of differences (particularly during a recession) between us and you the client we have developed the following policy which is effective for the 2008/09 year onwards:

1. For the year just ended any differences will be advised to you when we send your financial statements. We will also advise how to make the necessary adjustments and correct them with Inland Revenue. It is your decision as to whether you make the adjustments and you take ultimate responsibility for those adjustments.
2. If we cannot fully resolve the differences and it is very small we will write that difference off. If the difference is large we will report this to you for your consideration and action.
3. A new section will be added to our annual checklist asking whether you made the adjustments and if so when those adjustments were made.

Some clients are carrying differences from earlier financial years and which have never been adjusted despite them being advised with the financial statements. For those clients we will write to you separately and recommend the following course of action:

1. We meet to review the differences we are carrying in the financial statements and to discuss the consequences of not adjusting these.
2. Develop a course of action which will address these differences. The course of action will be very dependent upon each client and there are several options available.

The aim of this policy is to ensure that any differences we report back are addressed in the appropriate manner and in a timely manner. By addressing the differences you are minimising any exposure to Inland Revenue that you may have. We note that those clients who are TriTec or DIY-Easy GST are normally perfect with their GST for the year. Plus they are spending very little time preparing their GST returns. If you want to know more about TriTec or DIY-Easy GST please contact Kate Mitchell for a quote.

## Deductibility of Personal Expenses

We have been fielding a lot of queries lately on what types of expenditure are deductible. In these tough times people are looking for ways of claiming extra expenses in order to reduce their tax bills. Unfortunately, if you are using an experienced Chartered Accountant, you are probably already claiming everything you are entitled to. And if claims are made that Inland Revenue do not condone you may face difficulties when they catch up with you.

Broadly speaking for expenditure to be deductible it must be necessarily incurred in the operations of the business or have sufficient nexus with the income earning capacity of the taxpayer.

One particular issue that has been before the courts is expenditure on clothing. People in certain occupations believe they need to spend more on clothes in order to "look the part", however Inland Revenue do not accept this. Broadly, the authorities say that expenditure on clothing and its maintenance is generally of a private nature and non-deductible.

Another example is glasses or contact lenses. In Case E47 (1982) 5 NZTC 59,281 it was held that bifocals produced only efficiency and not income. The taxpayer was a public servant employed as a design engineer and he claimed a deduction of \$104 for the purchase of a specially prescribed pair of bifocals. Held, there was not a sufficient relationship between the expenditure and what it provided or sought to provide on the one hand and the income earning process on the other for the expenditure to come within the words of s 104: acquisition of the bifocals simply made an efficient person more efficient so that taxpayer gained efficiency and convenience through the purchase but he did not gain income.

We suggest you think very carefully before trying to claim anything personal such as clothing, eyewear, cosmetics, hairdressing, medical insurance etc. Probably the best self-test is to ask yourself - Would I spend money on these things if I wasn't self employed? If the answer is yes then the expense is probably personal rather than business related.

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