Telephone: (03) 365 0881
Facsimile: (03) 377 2991
Email: admin@brownglass.co.nz
Website: www.brownglass.co.nz

BROWN GLASSFORD AND CO LTD

Beyond the Farm Gate

Farming Newsletter

November 2012

THIS EDITION

- **Spring Arrivals**
- **Spring Departures**
- **Fringe Benefits & the Company Car**
- **Repairs and Maintenance / Development**
- **Livestock Scheme Changes**
- **Interest Rates**
- **2013 Provisional Tax Payments**
- **New Premises**

Spring Arrivals

We are very pleased to announce that three baby boys have arrived since the last newsletter:

- Rachel gave birth to Benjamin Paul McVie on 23 September 2012 weighing 7lbs 7oz.
- Christie gave birth to Mason Paora O'Donnell on 4 October 2012 weighing 7lbs 10oz.
- Jing Yi gave birth to Jay Yue Tan on 5 October 2012 weighing 8lbs 5oz.

- Elaine Adams -

We are also very pleased to welcome Elaine Adams to the BG Team, having recently moved to Christchurch from Northland where she worked for other accounting firms for some 20 years. Elaine was brought up on a dairy farm and more recently lived on a small beef unit.

We have been fortunate to acquire the short term services of Rachel Fickling who recently moved to Christchurch from Blenheim, and also Chris Hussey, a past employee, who has returned to Christchurch for a short time.

Spring Departures

We recently said farewell to Linda Hook who had been with the firm for ten years. Linda is looking forward to spending more time with her family and we wish Linda all the best.

We also say farewell to Louise Wohlers who leaves us in mid December and we wish her well for her future endeavours. For those of you who deal with Louise, please contact Peter or Graham if you have any queries.

Fringe Benefits & the "Company Car"

We sometimes get questions from our clients as to how they should be treating the expenditure related to vehicles that are used for both business and private purposes.
Generally speaking, those operating under a sole trader or partnership structure need to make an adjustment for private use for the running costs and the GST on these running costs by way of a % allocation, typically by keeping a logbook or using the IRD "default" business use allocation of 25% where a logbook is not kept. This is relatively easy to administer.

For those operating under a company structure, there are generally two scenarios as outlined below. Note that a company is caught with Fringe Benefit Tax (FBT) obligations on the basis of availability for private use ie: you pay FBT whether the vehicle is used or not.

1. Vehicles Available For Non-Shareholder Employee Use

Any vehicle owned by a company and made available to non-shareholder employees for private use will be subject to FBT. There are some limited exemptions for work related vehicles, however, any private use that is more than incidental means that these exemptions do not apply.

Essentially it becomes a bit of a balancing exercise. If FBT is paid, all costs including depreciation and the FBT paid will be deductible to the company for income tax purposes, so there is a 28% tax benefit to the company. However, FBT must be returned on a quarterly basis at 49% on 20% of the value of the vehicle (incl all on road costs & GST) eg: a $50,000 Prado (inc GST) would attract FBT of $4,925 ($50,000 x 20% = $10,000 x 49.25%) on annual basis. On these numbers, average annual running costs including depreciation would need to be $12,664 ($4,925 / 28% = $17,589 less $4,925 FBT deductible = $12,664) for it to be "tax neutral".

In addition, there is quarterly filing of FBT returns to be completed, and annoying penalties for late filing which can occur at busy times on the farm.

2. Vehicles Available For Shareholder - Employee Use

Where a company vehicle is made available for use to a shareholder-employee, there is a legitimate option available to both recognise and adjust for the private use of the vehicle and remove the compliance cost, hassle, and angst that seems to be a feature of FBT.

This method involves calculating the value of the fringe benefit, then charging that to the shareholder. This reduces the fringe benefit to nil. The amount charged is treated as company income and will be offset by the deductible running costs associated with the vehicle.

Using the example above, the $50,000 Prado that is available for private use 100% of the time would result in a fringe benefit value of $10,000 split $1,304 as GST payable and $8,696 as taxable income for the company, $2,435 of income tax, and therefore a total cash cost of $3,739 (ie: the income tax + the GST).

If we did not do this calculation, the company would be required to pay FBT of $4,925, plus GST of $1,304, less an income tax deduction of $1,744, therefore a total cash cost of $4,485. The net cash cost under the "contribution" option is less and the compliance has been removed.

Repairs and Maintenance / Development Expenditure

With stronger commodity prices over the past few seasons (and hopefully to come) we have seen a general increase in the amount of repairs and maintenance and development expenditure on farms.

Generally, expenditure incurred on the repairs and maintenance of assets is an allowable deduction. However, this deductibility may be limited or disallowed if it significantly alters or affects that asset. We will normally consider the following in determining how to treat the expenditure:

- The nature and value of the expenditure relative to the value of that asset.
- The effect of the work carried out on the operation and character of that asset.
- Whether or not the work has gone beyond remedying fair wear and tear on the asset.

The IRD also has some particular rules around the deductibility of development expenditure on farms. In many cases, this type of expenditure can be significant and will result in long term improvements to farm assets and could therefore be clearly seen as capital in nature. However, many of these development projects (eg: fencing, tree and stump removal, pasture renewal if not part of a larger capital project) are fully tax deductible in the year it is incurred.

If you are doing this kind of work then we would recommend you keep detailed records of the work and discuss it with us so that we can ensure the approriate treatment for income tax purposes.

Livestock Valuation Rules

As noted in our April 2012 newsletter, the IRD has changed the rules so that those who elect to use the 'herd scheme' cannot change to the alternative 'national standard cost scheme', except in narrow circumstances. These changes apply from the 2012/13 income year, unless those elections were made prior to 18 August 2011.

The IRD have introduced further proposed changes through a September 2012 Tax Bill as follows;

- Allowing an exemption to the Herd Scheme election being irrevocable cases of inter-generational transfer of livestock.
- Allowing an exemption to the Herd Scheme election being irrevocable where there has been a change in the farming regime eg: change from beef breeding to beef fattening.
- Forcing the purchaser of livestock to adopt the vendor's Herd Scheme election and base numbers where those parties are associated.
- Combining the Friesian and Jersey dairy cattle classes into one class, and doing the same with Red Deer and Wapiti.

We would recommend that you contact us if you are considering any change in business structure, or transfer of livestock assets to an associated party, to ensure that the impact of the above proposed changes is considered accordingly.

Succession Planning

There is no doubt that this topic has been gaining more prominence in recent times, with almost all rural publications devoting plenty of newsprint space to it. We don't plan to repeat all that here, but in our experience the key messages are:

- It is never too early or too late to start considering your succession plan.
- There needs to be a sustainable business to be succeeded.
- All parties need to be involved in the plan, but typically the party passing the business on needs to be ready to start the process (and may need some positive encouragement to do so).
- The hard conversations around each party's expectations need to be had, and the assistance of an independent third party to chair these is often worthwhile.

We are regularly involved in succession planning activities with our clients. If you wish to discuss how it could be beneficial to your family and business, then please contact us.

Interest Rates

Our view hasn't changed regarding what is currently happening with interest rates. Most commentators see short term rates staying low for some time yet.

Given continued volatility in overseas capital markets in particular, we continue to recommend that you obtain regular (say two weekly) information from your bank as to the movement in interest rates (e.g.floating through to 5 years fixed). It will help you get a feel for the general direction of interest rates.

This is certainly useful if you have fixed interest rates expiring, or if you are contemplating fixing interest rates on debt that you currently have on a floating rate.

2013 Provisional Tax Payments

By now most of you will have paid your first instalment of 2013 Provisional Tax (those with June balance dates will pay this on 28 November 2012).

In general, the commodity price outlook over the coming 2013 year is lower compared to 2012. For those of you using the "uplift" basis (ie: 2012 Residual Tax + 5%) to determine 2013 Provisional Tax payable, there may be a case for using the "estimate basis" to lower the 2013 Provisional Tax payable if you think your Taxable Income will be significantly reduced. We will cover this with you in the course of completing your 2012 Annual Report & Income Tax Returns.

We are happy to discuss it with you prior to then if you wish, or to discuss again if you think your 2013 Taxable Income will be further significantly reduced from the level we discussed when completing your 2012 Income Tax Returns.

Brown Glassford – Premises Update

We are now very happily settled into our new premises on Level 2, 504 Wairakei Road.

We have client carparking available under the building and we look forward to seeing you in our new office.

***PLEASE NOTE*: We have a new postal address which is: P O Box 39195, Harewood, Christchurch 8545**

Christmas Hours

We will be closing for Christmas at midday on Friday, 21 December 2012 and reopening at 8.30am on Monday, 14 January 2013.