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Business or Hobby?

From a tax perspective, it is very important to distinguish a business from a hobby. Any income made by a business will be taxable but income from a hobby is not taxed. In the same way, expenses relating to the activity can be claimed by a business but can not be claimed if the undertaking is classified as a hobby.

While this seems like a simple matter, deciding whether an activity is a business or a hobby can actually prove quite complex.

The courts have ruled that if an activity is conducted in an organised manner with a motive to make a profit, this is a good indication that the activity is a business. A hobby, on the other hand, is an activity that is undertaken for the primary purpose of recreation or enjoyment - any income generated by the hobby is incidental.

Although the ultimate test of a business is the intention to make a profit, the IRD and the courts have looked at the following features to help differentiate a business from a hobby:

- The scale of operations (large or small)



- The volume of transactions (high or low)
- The investment of time, money and effort (major or minor commitment)
- The period of time over which the taxpayer engaged in the activity (long or short)
- The pattern of activity (regular or intermittent)
- Whether the activity is carried out in a similar way to other profitable operations in the industry (yes or no)
- The financial outcome (high

or low dollar values / profits or losses - although this is often not a reliable indicator on its own)

While this gives an indication of the factors considered to make the distinction between a business and a hobby, each case must be decided on its facts. If you are unsure whether your activity should be classified as a business or a hobby, please contact your accountant for advice.

Tax Returns and Forms (e.g. Income Tax, GST, FBT etc).

Please ensure that all IRD forms and returns are completed and filed by their due dates regardless of whether or not you are able to pay. The penalties are as harsh for nonfiling as they are for nonpayment. If you are unable to pay IRD debt by the due date please contact us or the IRD well in advance as there are other options available.

Charitable Donations from a Company

For a company to claim charitable donations as a deduction for tax purposes, there has to be sufficient taxable profit in that year to cover the donations. Any excess would create a tax loss, which would not be tax deductible.

*"What lies behind us
and what lies before us
are tiny matters
compared to what lies
within us."*

Ralph Waldo Emerson



What Do Leaders of Successful Businesses Do?

For a business to be successful, it must have a strong leader. Leadership can make or break a company. This is why public companies pay several million dollars for a new chief executive officer. Below are nine characteristics of successful business leaders. It is therefore important to ensure you are equipped to manage the situation in the best way possible.

Guy Kawasaki has given his opinions on how to handle this difficult process in his recently released book; "Reality Check". We have summarised a few of his key tips below:

Overseas Travel

Expenses relating to overseas travel are deductible to the extent that they are incurred in the course of carrying on the business but there is no deduction for any private or holiday component of the trip. There is also no deduction available for employees for expenses incurred while travelling overseas in the course of their employment.

The IRD accepts that overseas travel may incorporate both business and holiday elements. However, it is important from a tax perspective to be able to separate out the private content of the travel costs.

In regard to airfares, the primary purpose of the trip will determine the deductibility:

- Main purpose is business-related and holiday element is incidental - 100% deduction
- Main purpose is private (e.g. holiday) and business element is incidental - No Deduction
- Two distinct purposes (business and private) - Apportionment required

Other overseas travel expenditure, such as the cost of accommodation and meals, will only be deductible to the extent that they relate to the business aspect of the trip. For example, if you were to spend seven days overseas and spend three of these on business, then only the cost of accommodation and meals on these three "business days" will be deductible. In this example, presuming the trip was intended to be part-business / part-pleasure, a deduction of 3/7th of the airfare cost would probably be considered a reasonable apportionment.

The IRD may request certain information to support a claim for overseas travel expenses, such as: the itinerary, a list of business contacts visited, details of business conducted, diversions from the business itinerary for private purposes, items of expenditure and the total cost of the trip.

Generally there will be no deduction for costs relating to the taxpayer's spouse or other family members accompanying them on an overseas trip. However, there are exceptions to the rule, and claims may be possible in certain circumstances, such as if the spouse or family member is employed full-time in the business and is actively involved with business activities while on the trip. Deductions may also be allowed where an associated overseas organisation expects the taxpayer to bring their spouse or if the taxpayer must be accompanied due to ill-health.

If you are unsure what to claim in relation to your overseas travel costs, please contact your accountant.

Source : RSM Prince

1. Have a positive attitude. Believe that your business is the best business in the world. Self-confidence leads to decisiveness and in particular, the ability to back your own judgment and to take risks. Be determined. Be persistent. Be resilient. Overcome setbacks. Do not dwell on past mistakes and learn from your errors.
2. Love what you do. Enjoy your work and the challenge it provides. Work should be fun, not merely something to be tolerated. Enthusiasm generates a hard work ethic and a passion which becomes part of the culture of your business.
3. Seek wealth creation. Aim to maximise your sales by increasing your prices, selling more to your existing customers or obtaining more customers either in your local area, in another state or in another country. Control your costs. Eliminate waste. Sell unproductive assets and discontinue unprofitable products. Know your business. Measure your marketing. Strategic partnerships with suppliers and customers can give your business greater flexibility and enable you to better manage your costs and maintain or increase your margins. Maintain your competitive advantage. Study your competitors' assets, capabilities, marketing, costs and culture.
4. Delegate. It is impossible to do everything yourself. It is also unwise as it is more productive to get those with the appropriate skills to do appropriate tasks. The ability to get people with different skills to work as a team is a starting point for all successful businesses. Recruit high quality staff with complimentary skills and organise these people in the most efficient way. Motivate your staff and encourage them to think independently. Non-performing staff which don't fit the culture of your business need to be replaced quickly because they can affect relationships with your customers and other staff members and ultimately the profitability of your business.
5. Seek financial, marketing and legal advice. Have a vision and clear goals. These goals should include future income and the achievement of various tasks. A strategy to grow the business and a detailed business plan consisting of marketing and financial plans are important. Manage your growth at a rate that enables your cashflow to remain positive.
6. Concentrate on doing what you do best. Specialise. Focus on single industries rather than diversifying. Maintain your core business. Outsource non-core activities and functions. Dominate a niche market rather than attempt to serve a large number of markets.
7. Have systems in place. You need the business to run efficiently even if you are away from the office for 12 months. The best example of a company with efficient systems is McDonalds. Teenagers can run their outlets profitably and efficiently because appropriate systems are in place.
8. Worksmart. Success does not mean working 100 hours a week. Today, it is more likely to mean working 35 hours a week and spending time with our family and pursuing your leisure interests. Working smart is much more important than working hard. Spend time working 'on' your business and not 'in' your business. Seek continual improvement. This may mean more efficient procedures, better systems, better marketing or better cashflow.
9. Have a good support base. Hire staff you can rely on for advice. However, use discretion when listening to advice from others. Encourage training. Foster an attitude of continuous learning both for yourself and your staff. Have a mentor. Be a mentor to your senior staff. Read and attend seminars. Notice what others are doing.

Source : Australian Credit Stationers

Gift Duty

Gift duty is a charge on any gifts that one person makes to another. It is only charged when gifts with a combined value of more than \$27,000 are given in any 12-month period.

For gift duty purposes, a gift is something given when:

- Nothing is received in return; or
- Something is received in return, but its value is less than the value of the property given.

If something of lesser value is received in return for a gift, the value of the gift, for the purpose of charging gift duty, is the difference between the two values.

Some examples of gifts include:

- Transfers of any property (for

- example, company shares or land)
- Any form of payment
- Creation of a trust
- Forgiveness or reduction of debt
- Allowing a debt to remain outstanding so that it cannot be collected by normal legal action

If any person makes gifts with a combined total value greater than \$12,000 in any 12-month period, they must complete a Gift Statement (IR 196) and submit this to the Inland Revenue Department. However, they will not be liable for gift duty unless they exceed the \$27,000 gifting threshold.

The rates of gift duty are outlined below:

Value of Gifts	Duty Payable
0 to \$27,000	NIL
\$27,001 to \$36,000	5% of value over \$27,000
\$36,001 to \$54,000	\$450 plus 10% of value over \$36,000
\$54,001 to \$72,000	\$2,250 plus 20% of value over \$54,000
Over \$72,000	\$5,850 plus 25% of value over \$72,000

The person who made the gift is primarily liable for any gift duty payable. If the giver does not pay the gift duty, the recipient of the gift will be liable for it, but they have the right to recover the amount paid from the giver.

An exemption from gift duty is given for gifts made to create or aid a charitable trust or any society or institution established exclusively

for charitable purposes. From 1 July 2008, that charitable trust, society, or institution will need to be registered by the Charities Commission for the gift to be deemed exempt.

For more information on Gift Duty, please refer to the IRD Gift Duty Guide (IR 194) or contact your accountant for advice.

Source; RSM Prince

IRD Refund Cheques

Before banking a tax refund cheque from the IRD, take the time to ensure that it is correct. The IRD will charge use of money interest if you accept a refund cheque that you're not entitled to and you could be prosecuted if you should have known the refund was not rightfully yours.

You should also ensure that by banking the cheque, it will not result in a shortfall elsewhere. For example, a situation could arise where the IRD refunds overpaid tax that you had intended to transfer to another period or tax type. If this cheque is sent back to the IRD, the refund can be reversed and the funds can be transferred to the other tax account at the date of the original payment. However, if the cheque is banked, you will have to pay again - along with

interest and penalties if the payment is then overdue!

This is why some taxpayers consider it safer to have the IRD send refunds by cheque rather than transferring the money directly into their bank account. If you still prefer the convenience of receiving refunds by direct credit, be sure to check any refunds received. If you are not entitled to the refund, it should be returned to the IRD as soon as possible after the error is discovered.

Of course, there is also a chance that your refund has been underpaid for some reason - this is another good reason to check that all refunds received from the IRD are in line with what is expected.

Source; RSM Prince



Change to mileage rates

IRD mileage rates were last revised in 1996.

Self employed

- Maximum still 5000 km
- Engine size does not matter
- Diesel or petrol does not matter
- First applies in the 2009 year
- Does not apply to motor cycles
- Rate is 70 cents per km

Employees

Employers may make a reasonable estimate of expenditure likely to be incurred by employees and use the 70 cents rate to reimburse them. Employers may also choose to use the AA rates if they wish, which are generally higher than 70 cents or a rate that is lower than 70 cents. The IRD announcement on the 70c rate is specific to self employed persons claiming a deduction against income.

Double Tax Agreement

On 27 June the Australian and New Zealand Governments signed a new Double Tax Agreement (DTA) between the two countries. The Australian DTA is one of our most important tax treaties given the level of commercial and human ties between the two countries. Once in force, the new DTA will replace the existing 1995 DTA. The new DTA reduces withholding rates on dividends, interest and royalties - this is consistent with the reduction in rates under the recently signed Protocol to the DTA with the United States.

There are also a number of other changes:

- Pensions that are tax-free in one country are also exempt in the other when the recipients move across the Tasman.
- The inclusion of an exemption for short-term secondments (90 days or less in any 12 months) in the Income form Employment Article.
- 7 year time bar on re-assessing past tax returns for enterprises (other than in cases of fraud, gross negligence or where a tax audit has commenced).

The new DTA will come into force once the Governments of New Zealand and Australia ratify it. The lower withholding rate will apply from the second month following the month the new DTA comes into force. In respect to other taxes, the new DTA will apply to the income tax years beginning on or after 1 April following the date when the DTA comes into force. For most of New Zealand companies it is expected to be 1 April 2010.

Source; RSM Prince

Surplus Cash – Loan repayment generally wise

Clients often wonder if they should use surplus cash to repay a bank loan. The alternative is often to invest the money back with the bank.

A client recently sold one of his rental properties and had \$100,000 left over. The bank was paying him 4%. He had two other properties with mortgages on them. He was paying 8.5% interest on these.

Generally you are better off to use the savings to reduce your mortgage. The interest income is taxable and the interest expense is tax deductible, so, from a tax point of view, you have a neutral situation.

It is true the rental property may well make a profit as a result of repaying the debt. However, if you do the arithmetic you will find you are better off repaying a debt, even though your taxable income rises.

There is one time when you should always repay a mortgage. Unless it is just a security for a business loan, it is the one you have over your own home. This is not tax neutral. You pay tax on the interest you earn, but you do not get a claim for tax on the interest you pay.

It can pay to hang onto the cash, if you are going to want the money for another project. If the project

is personal, such as buying a boat or a holiday home, use your own money rather than borrow, because the interest you will pay is not a tax-deductible cost.

You might also want to conserve your cash if you think you will have difficulty persuading the bank to lend to you and you have plans to borrow more. However, beware of getting over-extended with your borrowing. The bank's lending criteria can change without warning. You could be in trouble when it comes to the time for refinancing.



Shopping Mall Refund Stalls Cause Headaches for Tax Agents

Tax Agents (accountants) across the country are finding clients being deleted from their agency lists as these clients visit tax refund stalls set up in shopping malls. What people do not realise is that in order to access personal income details the clients are linked to the agency list of the 'Tax Refund' Company, automatically delinking them from their current tax agent. Once the refund is processed the client is

then delinked. This leaves the client with no tax agent and therefore no extension of time.

Individuals with tax agents are urged not to visit these stalls but to explore these alternatives:

- 1) Go to the IRD website at www.ird.govt.nz where you can find out yourself if you are due a refund.
- 2) Contact your accountant as they would be able to notify you of any refunds due. The cost of this would often be less than the commission taken at the malls.

Source : RSM Prince

Candy Gillespie

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	- Auckland	(09) 262-3634
RSM Prince	- Auckland	(09) 379 5324
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Sudburys Limited	- Whangarei	(09) 438 1113
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	- Kerikeri	(09) 407 7117
	- Mangonui	(09) 406-2173

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* Physical address * E-mail address * Phone and/or fax numbers *
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