nsaTax
Taxation and Trust Specialists

InBrief

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Practical Thoughts on the Proposed Tax Reforms

The government has indicated that a rise in the GST rate to 15% is likely to be announced in the May budget. If past reforms are anything to go by, the rate increase could be effective from as early as October 2010. While the implications of a rate increase seem simple enough, there are a number of practical issues to consider. How will the GST increase be transitioned? What rate of GST will apply to contracts that are conditional or unconditional on the date the GST rate changes? What happens if I have a fixed price contract made at the 12.5% rate but it doesn't settle until after the 15% rate applies – do I have to pay the extra tax, and if so can I recover it from the other party? These are just some of the practical questions that spring to mind.

While the details of any changes will not be finalised until after the budget announcement, it is likely that a GST cut-off date will be set (say 1 October 2010) and that the time of supply date will be the trigger point for determining whether supplies are subject to GST at 12.5% or 15%. Whether time of supply has been triggered will therefore become a crucial consideration, particularly for big ticket items or large adjustments such as a change in use adjustment or deregistration.

The time of supply is generally at the earlier of invoice or payment, however there are some exceptions to this such as supplies made between associated persons (the time of supply is when the services are provided or goods made available). In the case of a land contract where the GST portion can be significant, we recommend reviewing your client's contracts with additional care where the contract is to span the GST rate increase.

What about fixed price contracts? The GST Act has transitional provisions in section 78 to deal with a rise in the GST rate. Effectively, it allows a supplier to increase the purchase price and recover the additional GST from the purchaser where the contract has been entered into within 3 months of the rate change coming into force, but not where the contract specifically prohibits an increase or where the parties have already contemplated the rate increase in agreeing the fixed price. Case law has held that where a contract is "GST inclusive", the parties have contemplated the rate increase. We recommend that fixed rate contracts are reviewed carefully in the lead up to any change in the GST rate. Clearly whether a supplier on-charges the additional 2.5% to its customers may be a commercial decision, however for large purchases spanning the GST rate increase it may be worthwhile to consider whether specific additional clauses should be included to ensure your client does not incur an unexpected GST cost.

If any changes are announced, managing the transition to your client's best advantage will be key. This is particularly relevant for clients who have assets that are leaving the GST net (a change in use adjustment or deregistration). If a client has assets that are no longer being used

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in a taxable activity an output tax adjustment is required under section 21 of the GST Act. Similarly, where a person ceases their taxable activity, any retained assets are deemed to be supplied on deregistration. Clearly, your client will face a higher tax bill if the output adjustment is at 15% rather than 12.5%.

In the case of voluntary registrations, consideration should be given to deregistering prior to any rate change should registration no longer be required.

Another issue to consider is where a client may be considering purchasing second hand goods from a non registered vendor. A GST input tax claim is available in relation to second hand goods (subject to the usual limitations) equal to one ninth of the purchase price. This would be equal to $11,111 on a $100,000 purchase price. Delaying an intended purchase of second hand goods until after any GST rate increase would mean a GST input tax claim could be made at 15% (purchase price x 3/23). The GST portion on the same $100,000 purchase price would be $13,043.

If you would like assistance with any of the issues raised above please contact one of our Tax Consultants.

Maggie Jaques

NZ IFRS

We understand that the full application of NZ IFRS to small and medium sized business is still being considered by the Accounting Standards Review Board, and as such some practitioners have not ventured into understanding all aspects of the New Zealand equivalents to the International Financial Reporting Standards.

Do you have a client required to prepare NZ IFRS compliant financial statements due to:

- Size (classified as large under the differential reporting framework based on income, assets, number of employees)?
- Overseas ownership?
- Banking requirements?

Do you have aspects of the New Zealand equivalents to the International Financial Reporting Standards that you require assistance with?

Do you require assistance with assessing and calculating the impairment of intangible assets?

We can help should you require any assistance. Please contact either Bruce Watt (brucew@nsatax.co.nz) or Justin Gibson (justing@nsatax.co.nz).

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