NEWSLETTER

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Forestry in the Emissions Trading Scheme (ETS) – Pre 1990 Forest Land

Landowners of pre 1990 forest land are currently "in jail" but have the opportunity still to obtain a "get out of jail free card". If you own any forestry block make sure you understand the ETS implications so that you can make the right decisions urgently.

Landowners who deforest more than two hectares of pre 1990 forest land in any five year period will be mandatory participants in the Emissions Trading Scheme (ETS) and incur liabilities for carbon emissions from those forests, subject to the exemption noted below.

In this respect, two important deadlines are looming for owners of pre 1990 forest land – being land covered by forest species, native or exotic, on 31 December 1989 that remained forested, and was mainly exotic on 31 December 2007.

Exemptions – landowners with less than 50 hectares of pre 1990 forest land can apply for an exemption from the ETS that allows them to deforest this land without incurring deforestation liabilities. **The deadline for applying for this one-off opportunity closes on 30 September 2011.**

As a general rule we would not recommend applying for the exemption unless the relevant forest land was suitable for a change in land use eg conversion to dairy etc.,but instead apply for NZU's as discussed below.

Applying for an Allocation of New Zealand Units (NZU's)
NZU's are the unit of trade in the ETS representing one tonne of carbon dioxide equivalent of emissions or removals. NZU's were recently worth about $25 with their dollar value changeable based on supply and demand.

There is a one-off allocation from the Government to partially compensate land owners for the potential loss in value of their forest land which is compulsorily dragged into the ETS. Landowners can choose whether to hold the NZU's to offset future deforestation liabilities or sell the units. This allocation of NZU's is GST exempt and income tax free and at recent NZU prices is worth up to about $1,500 per hectare.

The deadline for applying for an allocation of NZU's is 30 November 2011.

We urge any forest landowner with pre 1990 forest land who could see a situation where their forest will be harvested in the future and not replanted to act now re one or other of the two options outlined above.

This summary is of necessity just that, and we emphasise the devil is in the detail. Further information can be obtained from us, Ministry of Agricultutre and Forestry (www.maf.govt.nz) or via a forestry consultant.

Source : Farm Accounting Busing Russell Volume 78

Working for Families – Changes to Family Scheme Income Definition

The Working for Families (WFF) Tax Credits Scheme is provided by the Government for families with children aged 18 or younger, to help with day-to-day living costs. To more accurately reflect the amount of income available to meet these costs, the definition of "family scheme income", which is used to determine family assistance entitlements, was amended from 1 April 2011.

While the previous definition incorporated similar adjustments for calculating the correct level of WFF income, the latest round of changes is designed to go a step further. These changes seek to eliminate perceived loopholes that exist, such as the sheltering of income through the use of family trusts.

The following amounts will now need to be included when calculating a person's income for family assistance purposes:

- The income of a trust of which the person is a settlor (certain trusts are excluded, but income of a generic family trust will be caught), and income of a company of which that trust (and an associated person) holds 50% or more of the shares. In this situation the attributed income of the company is calculated based on the trust's proportionate shareholding in the company. The amounts attributed are reduced if the trust or company has either distributed its income or paid a dividend, respectively. If there is more than one company, the net income of each company is calculated and attributed separately and if one company has incurred a loss, the loss cannot be offset against the profits of other companies,
- The taxable value of fringe benefits attributable to a person who (including associated persons) holds 50% or more of the shares in a company,
- Total passive income over $500 derived by dependent children such as interest, dividends, royalties and rent,
- Portfolio Investment Entity (PIE) income where the income is not locked in until retirement,
- 50% of certain pensions and annuities that are treated as exempt income,
- Foreign sourced income of a person's non-resident spouse,
- Tax exempt salary and wages such as those from specific international agreements e.g. salaries received from employees of the United Nations,
- Deposits paid to the main 'Income Equalisation Scheme' (for income from farming, fishing or forestry). Deposits captured include those made by the person and companies and trusts that meet the above requirements for family scheme income. Conversely refunds from the scheme are excluded,
- A further catch-all provision has been introduced to capture additional payments received by a person that are used to replace lost or diminished income or meet the living expenses of the person's family if the total of the amounts received exceed $5,000. For example, if a person's parents pay his/her family's utilities bills each month and the amounts total more than $5,000 per year, then that total amount is included as income.

It is important that families who are currently receiving WFF payments review all sources of their income and contact Inland Revenue to ensure they are receiving the correct level of benefit.

PAYE vs FBT

PAYE generally applies to cash paid by an employer to an employee, while FBT applies to non-cash benefits provided by the employer to the employee. However, it is not always clear whether PAYE, FBT or neither applies.

The basis upon which an employee receives a benefit will determine how it should be treated. For example, to reward an employee for their efforts an employer pays for an employee to attend an educational course of their choice, and the employee chooses to attend a cooking course for their own personal interest. In doing so, any one of the following scenarios could apply:

1. The employee organises to attend the course, receives the invoice and pays the cost, but is reimbursed by the employer.
2. The employee organises to attend the course and receives the invoice, but the employer pays the invoice on the employee's behalf.
3. The employer organises the course, receives the invoice and pays for the cost of the course.

The reimbursement payment under the first scenario will be subject to PAYE as it is akin to an additional salary/wages payment. In the second scenario, as the expense has been incurred by the employee (i.e. the invoice is in the employee's name), upon payment by the employer it is specifically captured as "expenditure on account of an employee" and also subject to PAYE. The third scenario is distinguished from the first two scenarios, on the basis that the employer contracts to procure the right for the employee to attend the course directly and provides that right to the employee, i.e. a non-cash benefit, and is therefore subject to FBT.

However, if instead of a cooking course the employer required the employee to attend a leadership development course, under each scenario above, no FBT or PAYE would be payable.

In the first scenario, a reimbursement payment is not subject to PAYE if the reimbursement qualifies as a non-taxable reimbursement. To qualify as a non-taxable reimbursement, the course would have to be deemed to have developed the employee's capacity to perform their job. On this basis, the payment would qualify as a tax-free reimbursement not subject to PAYE.

In the second scenario, the payment for the course is not captured as expenditure on account of an employee as it is for the benefit of the employer's business and therefore is not subject to PAYE. In the third scenario, because the benefit removes the need for the employer to pay a non-taxable reimbursement, FBT does not apply.

It is important to consider all the facts when determining if PAYE or FBT apply. It must be established whether the employer or the employee is incurring the underlying expense, and whether the employer benefits from the expense or if it is of personal benefit to the employee.

Making the Most of the 90-Day Trial Period

The new Employment Relations Amendment Act 2010, which came into effect on 1 April 2011, extended the 90-day trial period to all employers; prior to the amendment only those with fewer than 20 staff qualified.

The Employment Relations Act legislation requires that in order for a trial period provision in an employment agreement to be valid, the agreement must be in writing and state:

- that it is for a specific period not exceeding 90 days starting at the beginning of the employment, and
- that during the period the employer may dismiss the employee, and
- if the employee is dismissed they are not entitled to bring a personal grievance or other legal proceedings in respect of the dismissal.

If any of these elements are missing the trial period is not valid. In addition, the trial period provision provides that the employee has not previously been employed by the employer.

Since the enactment of the trial period provision, there have been several cases heard through the employment courts that give some clarity of interpretation of this legislation.

In *Parkes v Squires Manufacturing Ltd,* a recent personal grievance case, the employee received her employment agreement before starting work and signed it at lunchtime on her first day of work. The employer signed it a week later. The Employment Authority found that, as the employee had already started before signing the agreement, the trial period clause was not valid.

In *Smith v Stokes Valley Pharmacy (2009) Limited*, the Employment Court tested the 90-day trial period and applied a very rigid interpretation, which now provides the ground rules for employers. The court concluded that the employment agreement must include the trial period provisions (as stated above) and must be signed by both parties before the commencement of the employment.

It was also concluded in the *Smith v Stokes Valley Pharmacy case* that although the employee cannot claim wrongful dismissal, they are still entitled to the protection of the good faith provisions of the Employment Relations Act. These require the employer and employee to be communicative and responsive in their relationship. The employer is not required to give reasons for the dismissal in writing but they are required to give the employee feedback so that they can learn from the unsuccessful trial and hopefully have greater success with their next role.

The Judge also looked at the issue of notice with respect to the trial period and concluded that notice can be given during the 90-day period for the employment to terminate after the 90 days. However, in the event of an unsuccessful trial there is no provision for 'payment in lieu of notice' or 'termination without notice'. Thus the notice period must be worked out, unless the parties agree to it being paid in lieu at the time that the employee is given notice.

In essence, the trial period provides a level of protection if you have sincerely endeavoured to meet the standards expected of a "fair and reasonable" employer.

Snippets

Earthquake Relief – Donation of Trading Stock

Currently, if a business makes a donation of trading stock, it is deemed to be sold for market value and tax is payable accordingly. To support businesses who have or wish to make donations in support of the victims of the Christchurch earthquakes, the Government has introduced draft legislation exempting donations of trading stock from this market value rule.

The draft legislation provides disposals of trading stock will be exempt if it has been disposed of:

- to an unassociated person,
- for the purpose of relief from the adverse effects of a Canterbury earthquake, and
- the donation is made between 4 September 2010 and 31 March 2012.

A similar exclusion from gift duty has also been included in the draft legislation.

Update: Penny & Hooper v CIR

Penny & Hooper is a landmark case involving two orthopaedic surgeons operating through companies and not receiving "commercially realistic salaries".

The case was originally found in favour of the IRD by the Taxation Review Authority and later overturned by the High Court. In June 2010 the Court of Appeal swung in favour of the IRD. The taxpayers appealed to the Supreme Court.

The hearing by the Supreme Court of the appeal by Penny & Hooper has been delayed until 28 & 29 June 2011. The case was due to be heard by the Supreme Court in early March 2011, but this has been rescheduled due to the Christchurch earthquake.

New Team Member

We would like to welcome Nicole Sue to our team at Fluker Denton Limited. Nicole started with us on a full time basis at the beginning of the year. She is a local person and she was educated at Fairfield School and Horowhenua College. She has recently graduated from Victoria University with a degree in Accountancy and is now working to obtain her qualification as a Chartered Accountant with the Institute of Chartered Accountants of New Zealand.

If you have any questions about the newsletter items, please contact us, we are here to help