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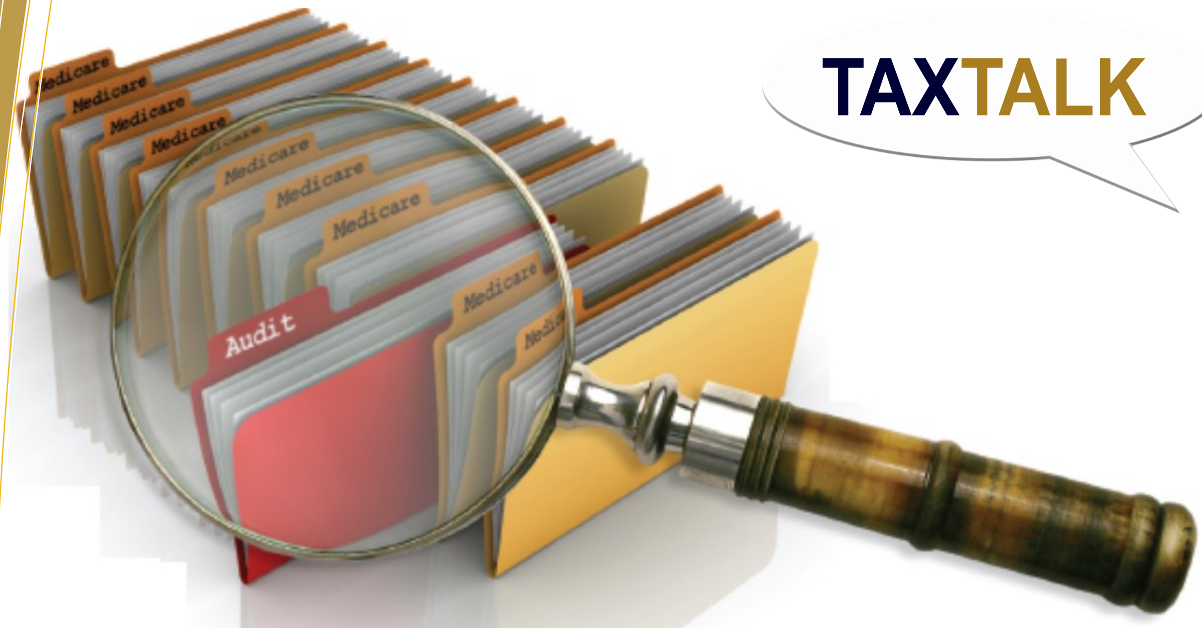
TAX AND BUSINESS ACCOUNTANTS

TAXTALK



Audits: What to do when IRD calls

What's an audit?

An Inland Revenue audit looks at your financial affairs to make sure you've paid the right amount of tax and complied with tax laws. It could be a simple check of your GST registration or a full examination of all your business and personal records.

Who gets audited?

Inland Revenue can audit any business. It uses a range of methods to select who to audit, but won't disclose the reason you have been chosen.

How it works

Inland Revenue may sample your records to see if an audit is needed. If everything is okay, the inquiry ends there and Inland Revenue will confirm you won't be audited.

If an audit is necessary, you'll get a letter telling you what records Inland Revenue needs to see, with an information sheet on how the process works. Usually, Inland Revenue will follow up with a face-to-face interview to learn more about your business and answer your questions.

Some audits focus on a small part of a business. In these instances, Inland Revenue may not need to meet you and may instead choose to conduct the audit by email or through your tax agent.

An audit will look at your:

- ledgers
- journals
- invoices
- payroll records
- bank statements.

How long do audits take?

Audits, like the businesses they look at, are all different. At the start of the process, Inland Revenue will give you an estimate of how long it thinks the audit will take.

Results

Near the end of the audit, Inland Revenue will meet you again to discuss its findings. It should be clear at this point if you'll get a refund or need to pay more tax.

The auditor will also tell you where you've gone wrong and how to put things right.

You can download a Audits Guide from the Inland Revenue website.

in this issue >>>

Consumer Law: footing the bill for faulty products or services

Who is responsible for fixing a product if it breaks after the manufacturer's warranty or an extended warranty has expired? If you answered "the customer", you should read on — the good reputation of your business may depend on it.

If your business sells, hires or leases products — or supplies services for household or personal use — here's what the Consumer Guarantees Act says you must do if something goes wrong.

Faulty products

Products your business sells must meet certain quality guarantees under the Consumer Guarantees Act (CGA).

If any of these guarantees are not met, a customer can come back to you and ask for a solution. If the problem is minor and can be easily fixed, it's your choice whether to offer repairs, a replacement or a refund.

If you fail to do so within a reasonable time, or refuse, then the customer can either:

- get someone else to fix it and claim reasonable costs from you or
- return the item and ask for a refund.

If the problem is serious or can't be easily fixed, then it's the customer's choice to either:

- return the product and get a refund or replacement
- keep the product and claim compensation for the drop in value.

The customer can also claim compensation for any loss or damage as a result of the faulty product that your business could have anticipated.

CASE STUDY:

Christine buys a new & expensive oven from H Berry Appliances, perfect for baking the sweet treats that her family loves. After three years of occasional use, the oven stops working and an appliance repairer quotes more than $1,000 to fix it. Christine contacts Harry Berry, who sold her the oven, who tells her it was only guaranteed for two years and therefore "not my problem."

Christine is not impressed. After getting advice, she sends Harry a letter asking for free repairs under the Consumer Guarantees Act (CGA).

Since the oven must be fit for purpose under the guarantee of acceptable quality, it should be able to heat and cook food easily. In this case, as it's a lightly used oven that cost a lot but doesn't do what an oven should, it's reasonable for the retailer to fix the problem. Harry agrees to repair Christine's oven under the CGA. Although Christine can once again bake her sweet treats, she is left with a sour taste in her mouth over Harry's initial refusal to comply with the law. She tells her friends about it, damaging H Berry Appliances' reputation. If Harry had just offered to fix the problem straight away, he might have turned this bad news story into a good customer experience.

Faulty services

Your business must meet certain quality guarantees under the Consumer Guarantees Act (CGA).

If the problem with a service is minor, the customer must give you a chance to fix the problem free of charge within a reasonable time.

If you refuse, or fail to do so within a reasonable time, the customer can either:

- get someone else to fix it and claim reasonable costs from you
- cancel the contract and refuse to pay for work done.

If the problem is serious or can't be fixed easily, a customer can either:

cancel the contract and ask for all or some of their money back
claim compensation for any drop in value of the service.

The customer can also claim compensation for any damage your business could have anticipated

Guarantees won't apply when you sell to another business — also known as contracting out of the Consumer Guarantees Act.

Contracting out of the Act

This applies if you sell goods or services to another business, and you have both agreed to contract out of the CGA in writing. It must also be fair and reasonable for both you and the other business to do so.

Aside from contracting out you can't tell customers that the guarantees under the CGA won't apply. To do so can breach the Fair Trading Act.

Beware Terms and conditions

Many large suppliers seem to be using their terms and conditions in ingenious ways to take advantage of their customers.

It's been reported that TrustPower advertised unlimited broadband for $49 a month. However, customers needed to sign up for a minimum of two years and in the small print it stated that the second 12 months was to be charged at $79 a month. The commerce Commission has filed charges under the Fair Trading Act.

Magazine publishers sometimes include a clause in their terms and conditions which says if you don't say you do not wish to renew your subscription, the company automatically renews it for a further year.

Be selective in choosing who you are going to allow to direct debit your bank account. If there is a dispute, you might find it hard to get your money back. Unfortunately, none of us has enough time to read all the terms and conditions. About the best we can do is be aware they can be badly skewed against the customer.

question time >>

Q: Is Children's Income exempt from Income Tax?

A: *Read below to find out*

A husband and wife partnership operates a takeaway outlet.

The partnership employs the partners' two children, both under 14 years of age, in the takeaway business. Each child earns less than $2,340 per annum.

In this situation, is the children's income exempt from tax?

A limited-income exemption for children was introduced in the 2013 tax year as part of the 2012 Budget, replacing the former child tax credit. The limited-income exemption exempts a school child from tax on up to $2,340 of income if that income is not subject to tax at source.

The exemption does not apply when:
* the income is subject to withholding tax such as salary or wages, or interest, or
* the child earns more than $2,340 of income that is not taxed at source.

Because the payments to the children would constitute a payment of salary or wages, the children's income will be subject to withholding tax (in this case PAYE) and the exemption would not apply.

Therefore, the payments by the partnership to the partners' children will not be exempt income of the children and the partnership will need to account for PAYE on these payments.

REFERENCE:

Income Tax Act 2007, ss CW 55BB, RD 2-RD 8.

Source: CCH/TEO Question & Answer Service

TAX SOLUTIONS

Some contractors don't have to have withholding tax deducted from their income. As a consequence, they have substantial provisional tax liabilities. Some people prefer to have some tax deducted as they go. It's proposed that from 1 April 2017 they will be entitled to require the payer to deduct withholding tax at a rate they choose, so long as it's at least 10%.

WEB SOLUTIONS

A COUPLE of months ago some horrendous stories were published in the daily papers about businesses unable to function because they could not get their internet connection repaired.

One firm in Auckland was without the internet for five weeks. One supplier said: "The average time to fix the fault has increased to more than 60 hours, with some customers waiting considerably longer."

Before selecting your internet service provider, check the firm out as best you can. The internet is a great resource for this purpose as are your friends, particularly on Facebook. If the service provider has a bad reputation, avoid it, even if the price is a bit lower.

If you've got a couple of minutes, try checking out your existing internet service provider. It could be time for a change.

Recently, Ken was approached by a power company with an offer for cheaper power and a free ultrafast broadband connection. He found communicating with the company was very difficult and it was almost impossible to talk to the supplier of the ultrafast broadband connection.

For this reason, he cancelled his arrangement. It later transpired that the broadband supplier was none other than the one who failed the Auckland business described above.

How to reduce bad debts

PREVENTION is better than cure when reducing the number of bad debts.

- Avoid giving credit to a stranger, without undertaking a credit check.
- If you have to give credit without doing a proper check, be sparing.
- Giving credit can help you gain customer loyalty, but be careful.
- There is no obligation to give credit to anyone. Try to make it a habit, if your type of business will permit, to assume you will be paid on the spot.

If it can't prevent bad debts then:

- Jump on new customers who start to abuse your credit arrangement.
- Make notes of every conversation you have with a debtor.
- If you have to make follow up calls, quote back to the customer what he/she undertook to do.
- Immediately after you have made a call, make a note in your diary of the day on which you will next call if the money has not been received and keep a record of what was said.
- Discontinue giving credit to the chronically bad payers. The time you put into them will destroy your profitability. You could be doing better things with the same time.

What about the big customer who will not pay on time?

Small businesses often find their biggest customer is their worst payer. You feel you can't afford to be too demanding, in spite of the fact you're entitled to your money. What should you do?

The answer is not to have one major customer that dominates your business. You will **always** be vulnerable while you let this continue.

Set a maximum percentage of total sales from any customer and do your utmost to see this is not exceeded. If your big customer goes broke it could take your business with it.

Quick Quote

Whether we want them or not, the New Year will bring new challenges; whether we seize them or not, the New Year will bring new opportunities. ~Michael Josephson

Don't grab all the money

IF you sell your business, which you run through a company, the money does not belong to you. It belongs to the company.

You can only take it out if you are entitled to do so. If there is money owing to you, according to the balance sheet of the company, then that money can be paid out. However, any more than this becomes a loan to you or may even be an illegal distribution.

A problem often arises when a business is sold. The seller gets paid for "goodwill". This is the value of the customers who have been built up over the years. It is a payment for the potential to get a higher income.

The sale of goodwill in excess of what was paid for it (if anything) is usually a capital gain. This capital belongs to the company.

You can get it out if your company happens to be a Look-through company or one of those old qualifying companies. Otherwise, it must stay there until the company is wound up. If you take the cash out prematurely it has to be treated as a loan from the company to you. There are tax consequences as a result. If you want the capital gain paid out to you, without tax consequences, you must first have a signed special resolution of shareholders resolving to wind up the company. A Liquidator can do this for you.

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