

Business Advice



Business Matters

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Why the GST Ratio could change the way you pay Provisional Tax

If you are GST registered and a provisional taxpayer the following article is a must read as it will effect what and when you pay your provisional tax. It could either save you time and money or it could cost you time and money. The result will depend on your circumstances and your decisions, so please read and consider the following.

So what are the changes?

First is the introduction of a new GST ratio option to calculate provisional tax, and.

Second is the change in provisional tax payment dates.

We will now look at each change in more detail, as like all tax changes these days the devil is in the detail

GST Ratio option

What is it?

This is a new option for you to calculate your provisional tax payments and it allows you to pay your provisional tax at the same time as your GST, using the same form as for your GST.

What are the benefits for me using the GST ratio method?



The benefits are as follows:

1. Use Of Money Interest (UOMI) will not apply to underpaid provisional tax until your terminal tax date. The down side is that UOMI will not be paid on any overpaid tax. This means that you may be able to reduce or eliminate any Use Of Money Interest (UOMI) altogether.
2. If you expect your current years profit to be lower than last years you will not have to base your current years provisional tax payments on your previous year's residual income tax (RIT) to avoid interest and penalties.
3. You should have less IRD payment dates to remember as you will be able to pay your GST and provisional tax at the same time – ie all in the same payment.
4. You may be able to slightly reduce your accounting costs as if you select this method we will not have to monitor and calculate your provisional tax payments – however this can also have it's downside as well – see below.



5. In theory while your provisional tax payments maybe higher than under other methods, your higher sales levels should mean there is increased cash flow to cover these increased tax payments.

What are the downsides of using this method?

The main ones are

1. You need to be more careful with your budgeting as each payment will be much larger than they were in the past.
2. You will need to ensure the method is actually beneficial as it is calculated on your income rather than your tax figure.
3. You could become liable to UOMI and penalties. The two main ways this would happen are
 - a. If you find out after the due date of your first provisional tax payment (usually the 28th August) that you know longer qualify to use this method.
 - b. If you opt out after the due date of your first provisional tax payment .
4. You will make 6 provisional tax payments rather than 2 or 4 payments under the other methods.
5. If you use this method and elect not to have us monitor your provisional tax payments then we will not be able to give you the reminder tax letters and phone calls that we usually do. Also we will be unable to give you the tax summary outlining when and how much your tax payments will be for the upcoming year. This could mean that any issues are not detected until your books are done at the end of the year and the result could be more expensive than the savings in our costs.



The benefits and downsides of this method will vary for each person and therefore the only way to determine whether you should, or should not, use this method is to look at your situation individually.

So can I use this new method ?

To be eligible to use the GST ratio method you need to be:

1. In business and GST registered. This will eliminate many people as the individual partners in a partnership and shareholders are not usually registered for GST and in most cases these are the people liable for provisional tax – not the actual GST registered entity.
2. Registered for GST for the whole of the previous year, which cannot be your first year in business.

3. Filing either monthly or two-monthly GST returns; and
4. Your RIT for the preceding year must be between \$2,500 and \$150,000; and
5. Your GST ratio percentage must be between 0% – 100%. If you choose the ratio method the IRD will calculate your ratio and let you know, but make sure you check the calculation to ensure it is correct.

If you meet the above criteria , and few people will, then you can choose to use the GST ratio method provided you elect before the start of a current income year **ie for this year the 1st of April 2008.**

If your RIT information is not available for the immediately preceding year (i.e. year ended 31 March 2008 in this case), the information from the previous year is used and the GST ratio is corrected later.

What if I find I no longer qualify to use this method

If, for whatever reason, you no longer meet the above qualifying criteria, the ratio option ceases to be available to you.

If the availability of this option ceases prior to the first provisional tax due date (remember this will now be the 28th August, not the 7th July), you can choose to use either the current standard or estimation method to calculate your provisional tax (i.e. the so-called “normal rules”). However, if your ability to use the ratio option ceases after the first provisional tax due date, you will have to use the estimation method (which could create UOMI and penalties).

How do I calculate my provisional tax under this method?

The IRD will calculate the ratio to use and inform you directly - it will also be printed on your GST form.

However, for those of you who want to know how the ratio is calculated so you can work out if this method is beneficial then the amount of your provisional tax payment due, per GSTpayment, is calculated as follows:

1. First divide your RIT for the preceding year by the total GST taxable supplies for the same preceding year. Note this is your income not your profit. This is the ratio





2. Then multiply the above result by the taxable supplies for the current GST period.
3. This will be the amount of provisional tax that you will pay with your GST payment.

Change in provisional tax payment dates

What has changed?

You would have noticed that the Inland Revenue Department (IRD) has aligned your GST periods to your balance date. This was done to prepare the way for the introduction of the new provisional tax rules coming into force for the 2008-2009 income year. For those of us with a standard balance date (ie 31st March) these changes will apply from 1 April 2008. However, the new rules already apply to taxpayers with early balance dates that is those whose financial year starts from 1st October 2007.

This will mean that provisional tax payments will be payable on the 28th of the month rather than the current 7th. The exception is for payments due on the 28th of December and April, these will be payable on the 15th of January and 7th of May respectively.

Technical Stuff – the devil is in the detail

To keep the technical matters to a minimum we will assume you have a 31st March balance date for the purposes of this article – if you don't then contact us for your applicable dates.

Depending on the frequency that you file GST returns, the new provisional tax payment dates will also differ.

- If you are **not registered for GST**, the provisional tax payments will be due on the 28th August, 15th January and the 7th May after the 31st of March, instead of the 7th of July, November and March.
- If you file **monthly or two monthly GST** returns and do not chose the GST Ratio method; the provisional tax payment dates are the same as for a non-registered person (see above).
- If you file **six-monthly GST** returns, the provisional tax payments will be due only twice a year – on the 28th of the two GST payment dates.
- If you chose the **GST ratio method**, your provisional taxes will be due six times a year on your usual GST payment dates ie 28th of June, August, October, 15th January, 28th of February and April.

Remember that under the GST ratio method you pay tax six times a year rather than the current three times, but each payment should be smaller.

Other Frequently Asked Questions

Will my ratio change during the year

The ratio can (and most likely will) change during the year. The most likely reasons for this will be:

1. If a new income tax assessment is issued - e.g. once your 31st March 2008 tax return is filed,
2. If there is a reassessment of your GST and/or income tax figures for the previous year – eg as a result of an audit.

If my ratio increase will I have to make a top up payment?

We are still awaiting confirmation from the IRD on this point, and we will let you know once we hear. For businesses that have a large increase in profits this top up payment could have cash flow implications.

What if I sell an asset?

In order to prevent an overpayment of provisional tax when an asset is sold, the amount of taxable supplies in any period is reduced if the sale price exceeds the greater of \$1,000 or 5% of the taxable supplies.

What if I deregister for GST

Then you will lose the ability to use the ratio method.

Will I be required to make a top up payment if my ratio increases?

We are still awaiting confirmation from the IRD on this matter and we will let you know once we hear.

What if I am late filing a GST return

If your GST return is more than 60 days overdue then you lose the ability to use the ratio method. Also even in the situation of a nil or refund return, the IRD will be charging a late filing fee of \$250 from the 1st April 2008.

Can I change my mind?

You are free to stop using the ratio method at any time. But (there is always one in tax) **if you do so after the 28th August you will have to use the estimation method for the entire year, which could expose you to penalties and interest if you underpay your provisional tax.**





So what should I do?

The new method, even with its benefits, will not suit all businesses, and you need to consider how this change will effect or benefit your business and what method best suits you. **But remember if you want to use the new method for the 2008/09 year you must elect before the 1st April 2008.**



While applications can be either by writing or done over the phone we recommend that you always do so in writing.

Most people we have talked have advised that the take up rate for the GST Ratio method has been very low with most people waiting to see what teething problems occur and they will review this option again prior to the 31st March 2009.

Actions to take

1. Make a decision whether the GST ratio suits your situation and if so make an election to the IRD before the 31st March 2008.
2. If you elect to use the GST ratio method please inform us so we can update our records
3. Enter the new provisional tax payment dates that are applicable to you in your diary

Who should I contact if I need more information or assistance

Us of course - If you require any assistance in making this decision, have any queries, or require more information please contact us – that is what we are here for.

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