

PROPOSED GST INCREASE

AT A GLANCE

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INTRODUCTION

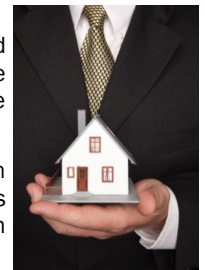
Recent media reports surrounding the release of the Tax Working Group's report in January 2010 suggest that the Government is considering increasing the rate of GST to 15%.

It is important to remember that there has been no confirmation that such a proposal will be adopted, nor any potential effective date. However, this newsletter raises matters that local authorities need to consider prior to any GST increase.

INCREASED COST TO RATEPAYERS

The cost to householders will increase, which is likely to draw close scrutiny from media and ratepayers alike. Whilst the GST increase may appear only small at 2.5% of the value of the supply (assuming an increase to 15%), this will be cumulative with any general rates increase as a result of inflationary pressures or otherwise.

For example, where an intended 4% rates increase is planned, together with an increase in the rate of GST, the taxpayer will suffer a 6.3% bottom-line increase to their rates bill! This may be seen as contentious, at best, and, at worst, in direct opposition to promises from Councillors and Mayors that rates will not increase significantly.



GST TIME OF SUPPLY

Perhaps the most perplexing issue that is likely to arise will be the GST time of supply, and the effect on the rate at which GST should be charged. To complicate the matter, the effect will be different for those councils who return GST based on a "payments basis", compared to those who operate on an "invoice basis".

Unless specific rules are introduced, the time-of-supply rules will operate as normal. For rates purposes, the time of supply is, generally, the earlier of an instalment notice being issued to the ratepayer requiring payment, the date on which payment is required by an instalment notice, or any payment being received.

However, forewarned is forearmed. Should a GST rate-increase occur during the income year (for example, as at 1 October or 1 April), Council will need to consider these time-of-supply rules; particularly where rates are paid in advance of an instalment notice being issued by Council, and that notice is issued after the date that the rate of GST change is effected. Typically, this is where a direct debit mandate is in place. This may have further implications where instalment notices issued later in the year charge more than the earlier rates assessment.

However, if a GST rate-increase occurs as at 1 July, the effect will be reduced, as the majority of Council's rates revenue will have been collected for the previous year, and only a relatively small portion would be paid in advance for the current year.

GST RETURNS

To allow the IRD to track each taxpayer's income and expenditure at the old and new rates, special rules require a two-part GST return to be filed; part one at the old rate of GST, and part two for the new rate of GST. However, only where a GST return period straddles the date of change are these special, two-part GST returns required.

This will have a significant effect on smaller local authorities with a two-month filing period. The majority of local authorities return GST on a monthly basis, however, so this will have little or no effect on those entities.

FACILITATION

GST has increased before—in July 1989. Thanks to this previous change, specific provisions already exist within the GST legislation that prescribe special returns, calculations and allowances in the event of a GST increase.



This means that finance staff are able to determine the ramifications to Council now. It is likely that the conclusions reached will be that special rules are required for the time of supply!

For rates, two broad options appear to exist, being:

- A predetermined, composite rate of GST; or
- A special 'time of performance' rule.

We discuss these briefly overleaf. As with any matters involving legislation, there is no certainty that any such proposal to the Government would be accepted in time, or at all.

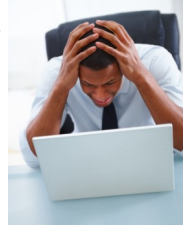
FACILITATION, CONTINUED...

COMPOSITE RATE

Rates are struck on a GST-inclusive basis (so ratepayers are advised of their total liability for the year). This GST-inclusive amount is undermined if there is a subsequent change in the GST rate. We understand that this process may have been alleviated last time by using a composite GST rate.

A composite rate was provided for rates charged in the 1989/90 income year that permitted a special GST rate of 11.25%. Whilst a composite rate is a potential solution to alleviate the financial strain imposed on ratepayers, this may introduce further compliance concerns for Council, including:

- The possibility of having three rates of GST in use—12.5%, 13.75% (a potential composite rate), and the proposed 15%;
- Computer systems' ability to handle these rates, and the additional review procedure required to ensure that the correct rate is used at the correct time; and
- The flow-on effect on other charges, such as rates remissions, postponements and penalties (the latter carry no GST themselves, but are based on the GST-inclusive rates charged).



TIME OF PERFORMANCE

International precedent exists for a 'time of performance' rule to apply when a GST rate changes. So it could be 'deemed' that the time of performance occurs at the date rates are struck.

This has the advantage of a single rate applying and certainty existing at the date of the rates strike. However, care would be needed to ensure that councils do not become liable to pay the entire year's GST output tax at this time!

SYSTEMS

To facilitate any change to an increased rate of GST, Council will need to ensure that it has adequate system capabilities, to change not only the rate at which GST is charged and claimed, but also the time. Given the potential for invoices or even credit notes to be required, at different rates, these systems will need to be more flexible than previously.

As with any changes to systems, robust review processes will need to be carried out to ensure that any changes are implemented correctly.

NOT JUST RATES

Much of the focus and debate has been centred on the impact of a GST increase on rates. However, many other matters still need to be considered, including the impact on fees and charges imposed by local authorities. These may include financial and development contributions, parking charges, dog-licensing and penalties, water charges (where these are charged separately from general or targeted rates), and liquor-licensing fees.

These simple examples demonstrate the complications that can easily arise:



Example 1

Parking fees are currently set at \$2.00 per hour (GST-inclusive), so the options for Council may include receiving \$0.03 less per hour in gross revenue, or increasing parking fees to \$2.05 per hour.

Given that New Zealand no longer has 5c coins, the actual cost of parking may need to be revised, and meters may need to be reprogrammed, replaced, or relabeled.

Example 2

Council issues dog registration notices in July 2010 to those dog owners with known dogs. The notice includes the relevant charges, inclusive of GST at 12.5%, and states that "this invoice becomes a tax invoice when paid". The GST time of supply will arise upon payment being received by Council.

The rate of GST increases to 15%, effective 1 October 2010. A dog owner pays the amount, as invoiced, after 1 October 2010. Council is required to return GST on that payment at 15%. This poses several problems:

- A shortfall arises to Council, as a greater amount must be returned as GST. Council is entitled to recover this from the ratepayer, although this will incur administrative costs;
- The tax invoice provided to the dog owner now incorrectly states GST at the lower rate. Technically, Council should issue a debit note in respect of the additional GST charged on the supply.

CONCLUSION

Local authorities need to take urgent action if the impact of GST changes are to be managed. Ratepayers are likely to experience increased costs. Your Council will also incur significant costs if proactive steps are not taken.

Assessing your Council's income streams, determining system changes and influencing changes to current GST rules will aid both ratepayers and Council.

To discuss these matters further, please contact Richard Toovey on (04) 494 2394, or your regular TEAM contact.

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