

# TaxTeamTalk

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## Budget 2011

Last week, the Finance Minister delivered a 2011 Budget with very few tax changes but with a significant focus on funding matters. The principal changes relate to the Working for Families, KiwiSaver, and student loan schemes.

This newsletter focuses on important Budget initiatives that are relevant to the public sector. We also outline recent tax developments of which you should be aware.



## Further belt-tightening in the public sector

The Budget announced that public sector employers will be required to meet the costs of funding retirement savings schemes from their own budgets.

This change affects KiwiSaver, the State Sector Retirement Savings Scheme and the Teachers' Retirement Savings Scheme, and is to occur from 1 July 2012, which at least gives organisations some time to prepare.

As a priority, you will need to:

- Assess the extent of the additional costs to your organisation, and how those costs will be funded;
- Identify any additional compliance obligations following these changes, if any; and
- Be prepared to respond to likely employee queries.

The Minister of Finance has stated that one reason for this initiative was to ensure that the public sector faces the same pressures as the private sector to improve efficiency and productivity. However, unlike the private sector, most public sector entities cannot pass on additional costs in the price of their products.

Given ongoing 'belt-tightening', it is now more important than ever for thorough budgeting to differentiate 'must-haves' from 'nice-to-haves'. Unfortunately, tax is a 'must-have', with significant fiscal and political costs of non-compliance.

Identifying these costs is the best way to ensure that budgeting is effective and there are no surprises.

There may also be a risk that the so-called Zero Budget will de-motivate staff, who will interpret this as meaning a freeze on salaries. One challenge for the sector is thinking of creative, cost-effective tools to keep valuable staff engaged.

Within the tax laws, there are incentives for employers to provide tax-efficient benefits to staff. These include, for example, an exclusion from fringe benefit tax for benefits provided on the premises.

**If you would like to discuss the implications of the retirement savings scheme amendments, implementing a tax compliance programme for your organisation, or tax-efficient methods to provide benefits to your employees, please contact your TaxTeam advisor.**

# KiwiSaver

In an attempt to shift the fiscal cost of KiwiSaver away from public funding and towards private savings, the Budget introduced a number of changes to KiwiSaver.

## The key changes

- **Member tax credits** (“MTCs”) will be halved from the current maximum of \$1,042 to \$521 a year. This will effectively apply from 1 July 2011, and will be reflected in payments to KiwiSaver accounts in the second half of 2012.
- **Employer Superannuation Contribution Tax** (“ESCT”):
  - From 1 April 2012, the ESCT exemption that applied to employer contributions to KiwiSaver and other complying superannuation funds will be removed.
  - From 1 April 2012, the current default ESCT rate of 33% will be removed, which means that you will have to calculate and pay ESCT to the IRD at the employee’s marginal tax rate.
- From 1 April 2013, the minimum **employee contribution rate** will increase from 2% to 3%.
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## What the changes mean to you

### Contributions holidays

As a result of these announcements, you may receive requests from employees wishing to take a contributions holiday from KiwiSaver. When processing such requests it is important to note that:

- Contributions holidays can only be taken by employees who have been in KiwiSaver for one year or more; and
- You must continue accounting for both employer and employee contributions until you receive a letter from the IRD approving the employee’s contributions holiday.

### Calculation and payment of ESCT

As the default ESCT rate of 33% will be removed from 1 April 2012, all employer contributions will be subject to ESCT calculated at the employee’s marginal tax rate.

Given the specific ESCT exemption that has historically applied to KiwiSaver, you should not have previously paid ESCT on KiwiSaver contributions up to 2%. With the ESCT exemption removed, *all* employer contributions will be subject to ESCT. You will need to check that your payroll systems can perform these calculations correctly.

### Employment contracts

Depending on how an employment contract has been drafted, the employee may end up bearing the costs of these KiwiSaver changes.

If employment contracts are drafted on a ‘total remuneration’ basis, the employer KiwiSaver contributions may be deducted from the employee’s gross salary. In these cases, increases in

employer KiwiSaver contributions impose no additional cost on employers, since the costs of KiwiSaver are typically passed on to the employee by way of salary sacrifice.

However, for employment contracts drafted on a ‘base salary plus other benefits’ basis, the employer incurs the employer KiwiSaver contributions in addition to the base salary, meaning that the employer KiwiSaver contribution is an actual cost to employers.

**As such, employers should review all existing employment contracts to evaluate the impact of these upcoming changes, and also review templates to ensure that the costs of KiwiSaver are managed appropriately for future employees.**



## Tax compliance audits

The Minister of Revenue announced that, for the first nine months of the 2010/2011 financial year, every dollar that the IRD invested in tax compliance recovered **six** dollars of tax.

This success justifies the IRD’s approach to ensuring that organisations are “getting it right at source”, as outlined in its Tax Compliance Focus Report for the 2010/11 financial year.

Although Budget 2011 provided no *extra* funding for the IRD, extra funding of \$120 million was announced last year specifically for the IRD to bolster its tax compliance audits over a four-year period.

**We have seen a significant increase in IRD audit activity in the public sector over the last two years—the greatest impact on organisations being the time-cost associated with the audit.**

## Public-private partnerships

A cornerstone of the Budget was growth underpinned by infrastructure projects developed in conjunction with the private sector.

There are significant opportunities involved in public-private partnerships (“PPPs”), particularly through tax-efficient planning to optimise the tax concessions. Undoubtedly, the private sector will be well aware of possible opportunities to maximise their return, of which tax will be one component. To position yourself effectively, it is critical to be fully informed of all possible costs and benefits before and during negotiations on PPPs.

It is also worth bearing in mind that the *true financial cost* of a project to Government will be net of tax recovered from the private partner.

**If you would like to know more about PPP structures, contact your TaxTeam advisor.**



## Canterbury Earthquake Relief payments

The Taxation (*Canterbury Earthquake Measures*) Bill was recently passed by Parliament.

The Bill provides that \$3,200-worth of cash and other benefits given to an employee within eight weeks of either earthquake can be provided as exempt income (i.e. not subject to PAYE). One of the conditions is that cash payments must not replace ordinary income of the employee. Non-cash benefits provided during the same period can be excluded from FBT (up to the \$3,200 per-employee threshold for total benefits).

**If you have previously accounted for tax on the above benefits, you may be entitled to a refund from the IRD.**

## Mileage reimbursements

The IRD has increased the approved mileage rate that may be used to reimburse employees tax-free for private use of their vehicles, from 70 cents to **74 cents** per kilometre (“IRD rate”). This amendment is effective from 27 April 2011.

The IRD rate is intended to reflect a reasonable estimate of the costs involved in vehicle-use, and is based on surveying the running costs of both petrol and diesel vehicles across a range of engine sizes, over 14,000 kilometres of travel a year. These running costs do not focus solely on the cost of petrol/diesel, but include all costs relating to vehicle ownership, such as insurance, maintenance, etc.

An increase in the mileage rate may result in increased costs to the organisation, so this should be closely considered before implementing a change. Importantly, if your employment agreements refer to the approved IRD rate, your systems will need to change to reflect the increase.

You are not *required* to use the IRD rate—you can use any method that provides a reasonable estimate of the likely costs. Any such reimbursement calculated in this way can be paid tax-free. Other approved methods include the AA's published mileage rates.

**Before reimbursing mileage for elected appointed officials at the new IRD rate, you may need to consider guidance from the Remuneration Authority or other regulatory body.**



# Tax rates

Although the Budget did not signal a change in tax rates, we outline below the applicable rates for the 2011/12 year.

## Income tax rates

INCOME THRESHOLD	INCOME TAX RATE
\$0 - \$14,000	10.50%
\$14,001 - \$48,000	17.50%
\$48,001 - \$70,000	30.00%
Over \$70,000	33.00%

## FBT rates

QUARTER	FLAT-RATE	ALTERNATE-RATE
1 (April – June)	49.25%	42.86%
2 (July – September)	49.25%	42.86%
3 (October – December)	49.25%	42.86%
4 (January – March)	49.25% or Attributed rates	Attributed rates

## Other rates

COMPANY TAX RATE	
Company Tax Rate	28%

GOODS AND SERVICES TAX RATE	
Goods and Services Tax Rate	15%

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