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Tax Alert

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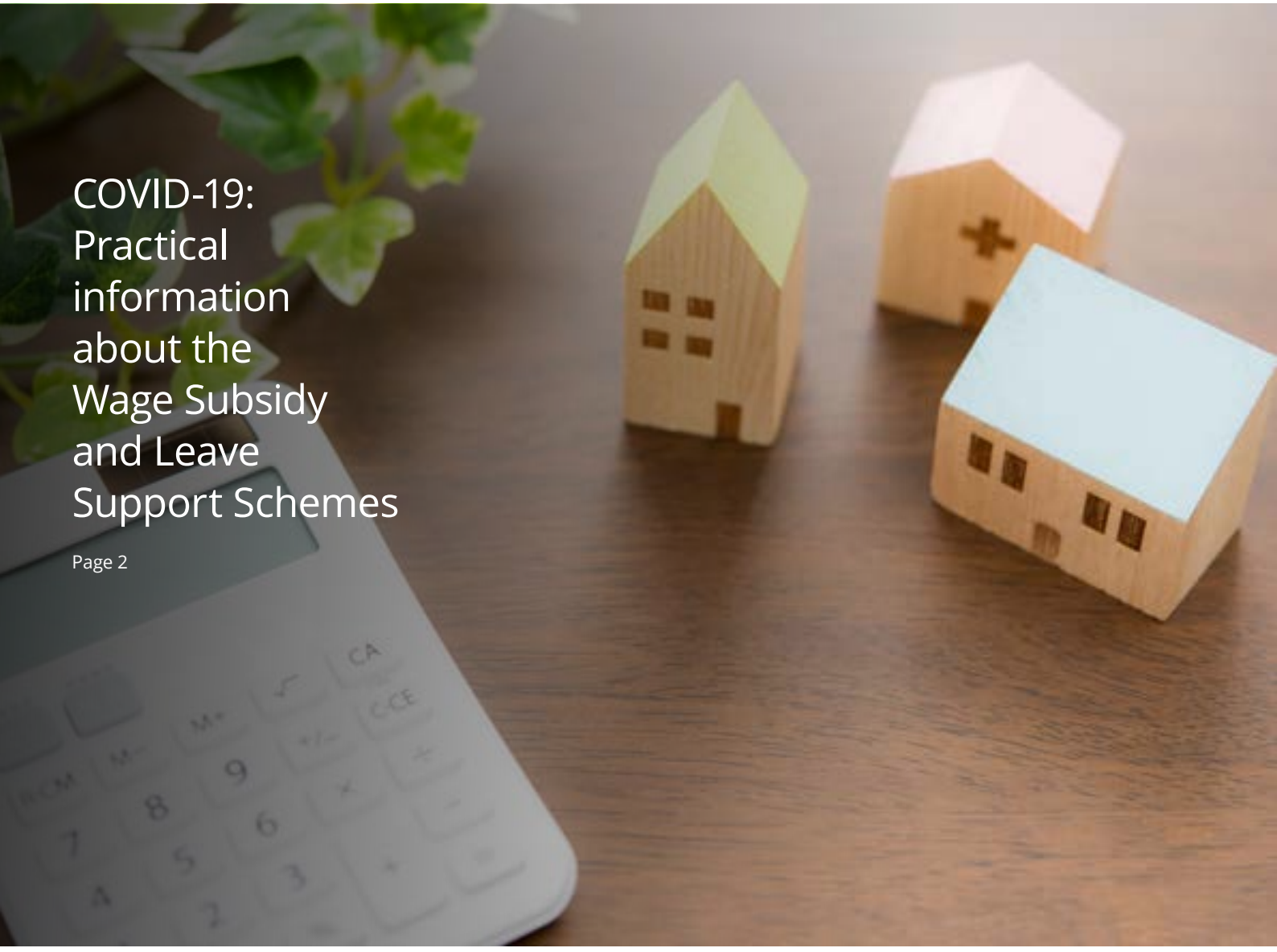

COVID-19: Practical information about the Wage Subsidy and Leave Support Schemes

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What are your entitlements under the schemes

By Robyn Walker and Blake Hawes

As the Greater Auckland region has now shifted to COVID-19 Alert Level 2 as of 11:59pm, Sunday 30 August the most recent addition to the government's wage subsidies, the Resurgence Wage Subsidy Scheme, is set to close for applications at 11:59pm on 3 September.

If your business did not make an application for the Wage Subsidy Extension it may still be eligible to apply for the Resurgence Wage Subsidy Scheme, but your application needs to be made before midnight tonight.

Summary: Resurgence Wage subsidy

- The two-week Resurgence Wage Subsidy Scheme (RWS) is available for businesses who have had, or predict they will experience, a 40% reduction in revenue in a two-week period between 12 August and 10 September, compared to a "similar period" in 2019.
- The RWS payment is $1,171.60 for a full-time employee and $700 for a part-time employee.
- The RWS applies across New Zealand and is not restricted to Auckland.
- The RWS opened for applications at 1pm on Friday 21 August. Applications will close at 11:59pm 3 September 2020. Applications are made through the Ministry of Social Development.
- The Wage Subsidy Extension Scheme (WSE) expired on 1 September 2020. If a business made an application on this date they will receive a lump sum to cover the salary and wage cost of the business for the proceeding 8 weeks.
- A business cannot be in receipt of the WSE and the RWS at the same time.

Leave Support Scheme

- The Leave Support Scheme provides the ability for employers to claim amounts to help support employees who are unable to work as a consequence of COVID-19. The Leave Support Scheme applies to four specific set of circumstances.
- The Leave Support Scheme provides a four week payment in relation to affected employees; with weekly payment rate being the same as for the wage subsidy ($585.80 for a full time worker and $350 for a part time worker).

Resurgence Wage subsidy

The RWS provides two weeks of support, being $1,171.60 per full-time worker and $700 per part-time worker.

Businesses (including the self-employed) that have been financially impacted by COVID-19 are still able to apply for the Resurgence Wage Subsidy Scheme (RWS) if they:

1. Meet the eligibility criteria; and
2. Are not currently a recipient of the Wage Subsidy Extension (WSE)

1. Eligibility Criteria

To keep matters simple, the eligibility criteria for the RWS are largely consistent with the previous schemes, with some refinements to reflect the current context we find ourselves in.

Key RWS eligibility criteria include:

- The business has had, or predicts it will have, a 40% decline in revenue over a 14-day period, and:
  - The revenue drop must be related to COVID-19;
  - The revenue drop must occur between 12 August 2020 and 10 September 2020;
  - The revenue drop must be compared to a similar period in 2019 (or to a period that gives the best estimation of the decline due to COVID-19 for high-growth businesses or businesses that have been operating for less than a year).
- The business must have taken active steps to mitigate the financial impact of COVID-19, which can include drawing on cash reserves (if appropriate), making an insurance claim, talking to the bank, and seeking advice from an accountant or other support networks, such as a chamber of commerce or industry association.
- The employees named in the application need to remain employed for the two weeks covered by the RWS. Applicants must have obtained employee approval to be included in an application.
- The employer must endeavour to pay at least 80% of each named employee's normal wages or salary for the duration of the subsidy, or pass on at least the full amount of the subsidy claimed to the employee for the two-week subsidised period (unless the employee is ordinarily paid less).

2. Not a recipient of the Wage Subsidy Extension

While the WSE is received in a lump sum payment (shortly after a successful application is made), the payment is considered an upfront payment for salary and wages for the proceeding 8-week period.

While applications for the WSE closed on 1 September 2020, businesses that made an application for the WSE within the 8 weeks before the 3 September 2020 RWS application deadline will not be eligible for the RWS.

A RWS claim also cannot be made in respect of any employees who are the subject of a Leave Support payment (see further below)..

How to measure revenue and find a comparative period

Because the RWS applies for only a 14-day period, those businesses who only prepare periodic invoices (e.g. monthly) may struggle to specifically isolate the revenue which relates to a particular 14-day period – either in 2020 or in the 2019 comparative period. There is not currently any guidance as to how businesses should measure revenue in these circumstances.

A pro-rata approach may be one solution. We recommend that anyone seeking to make use of the RWS clearly document the basis on which any application is made, as all payments made will be subject to reviews and audits by the Ministry of Social Development.

Examples

Riaan's Rugby School (RRS) is an Auckland based business owned and operated by Riaan, a rugby fanatic. RRS provides weeknight rugby training services for clubs and teams in need of specialist help. Payment is usually received in full the night a training session is held. After the initial outbreak of COVID-19 in New Zealand was bought under control many New Zealanders decided to take up sports including rugby – business was booming, and Riaan did not make an application for the WSE. During Alert Level 3 in Auckland, sports (including rugby practices) were not permitted and therefore RRS suffered a large decrease in revenue. Riaan, who was not sure when Alert Level 3 restrictions would be lifted, waited for a period of two weeks to pass in order to be comfortable that RRS's revenue had dropped by 40% when compared to a similar period in 2019, after which made an application for the RWS.

Quality Umbrella's Limited (QI) is a retail store owned by Mr Chapman that sells umbrellas in Wellington. QI has recently suffered from a bad month of business, as a result of umbrella sales falling unusually low during winter and several thefts from the store. As a result of the bad month in business Mr Chapman determines that QI's revenue has decreased by more than 40% during the 14-day period 13 August to 27 August and intends to make an application for the RWS. Unfortunately as QI's revenue decrease in not related to COVID-19 the RWS cannot be claimed.

COVID-19 Leave Support Scheme

Since early April 2020, there have been a number of variations to the Leave Support Scheme. Beginning life as the Essential Worker Leave Support Scheme (EWLS Scheme), the EWLS Scheme was designed to ensure that essential workers who were required to take leave from work to comply with Ministry of Health public health guidance continued to receive income if they could not work from home.

From 1 May, the EWLS Scheme was extended to all businesses, organisations and self-employed people experiencing hardship due to COVID-19 and was renamed the COVID-19 Leave Support Scheme (LSS). From 21 August 2020, an employer no longer needs to have been financially affected by COVID-19 in order to be eligible for the LSS. We outline below some key information about the LSS as it applies from 21 August.

Who can use the Leave Support Scheme?

Employers (including the self-employed) will be able to apply for the LSS on behalf of individual employees if those employees cannot work, and an employee has advised that they are in one of the four following affected groups:

1. They are deemed 'higher-risk' if they contract COVID-19 and Ministry of Health guidelines recommend that they remain at home for the duration of the COVID-19 public health restrictions.

2. They have household members who are deemed 'higher-risk' if they contract COVID-19 and Ministry of Health guidelines recommend the employee also remains at home to reduce the risk of transmitting the virus to other household members.

3. They have come into contact with someone who has contracted COVID-19 and are required to remain at home for 14 days (as required by Ministry of Health guidelines).

4. They have tested positive for COVID-19 and are required to remain off work until they've been cleared by a health professional to be released from self-isolation.

Employers intending to access the LSS will also have to read, understand and agree to a declaration when making an application. Importantly, employers will have to confirm that they have completed the following:

- Discussed the application with the employee(s) before making it;
- Received employee consent to the relevant points outlined in the declaration; and
- Confirmed the employee(s) meet the Ministry of Health Guidelines at the time of application (it is only necessary for the employee to confirm to the employer that they meet one of the criteria – they do not have to confirm what it is).

Employers are also expected to have a conversation about how best to support the employee. For example, they may choose to use existing sick or annual leave, with the LSS used to support paying that. If full paid leave options aren't available, the subsidy could be used to top up what is available. Employers are expected to endeavour to pay the relevant employees at least 80% of their usual wages or pay at least the LSS payment amount.

What do you get?

The LSS will provide a subsidy payment for a period of four weeks at a time for each affected employee. The weekly LSS payment amount is the same as for the Wage Subsidy, being $585.80 per week for a full-time employee, and $350 per week for a part-time employee. Therefore, four-week payments of $2,343.20 and $1,400 are received for full-time and part-time workers respectively. If an employee ordinarily earns less than these amounts, they should be paid their ordinary amount and any surplus should be used to pay other staff or returned.

Employers are able to re-apply for the same employee after each four-week period (if required) and can submit multiple applications relating to different employees.

Can a business get both a wage subsidy and the LSS subsidy?

No – employers cannot receive a wage subsidy and a Leave Support Scheme payment in respect of the same employee at the same time.

Examples

Seaside Milkshakes ('SM') is a popular café run by Hiran that has several part time employees. One of SM's part time employees, Denver, lives with her grandparents who are both in their 80s. Denver took advice from the Ministry of Health that she remain at home over the three weeks following the resurgence of COVID-19 in New Zealand as she lives with people who are at 'high risk' if they were to contract COVID-19. SM can make an application under the LSS for Denver. SM receives a payment of $1,400 which is used to pay Denver her usual pay of $300 per week for the three weeks she is advised to stay at home. SM treats these payments like a normal wage payment to Denver and withholds PAYE and other required deductions. As SM does not have any other employees using the LSS, SM returns the unused balance of $500 ($1,400 less $900) to the Ministry of Social Development.

Greg runs a successful motor dealership, V8s for Mates Limited (V84M). V84M has dealerships and garages operating across the upper North Island. Greg has a number of staff who live in South Auckland but ordinarily work at the Huntly V84M dealership; those staff are unable to get to work during the period of Alert Level 3 travel restrictions and their work cannot be done from home. While turnover is down, it is not down the required 40% in order to claim the RWS, so Greg wants to know whether the Leave Support Scheme is available to provide any assistance to the staff who are unable to work. Unfortunately the staff who cannot work because of the COVID-19 restrictions do not fall within any of the four 'affected groups' and therefore it is not possible to use the Leave Support Scheme.

Thanks to the careful planning and systems we have already implemented as a firm, we are well positioned to provide advice and support to all of our clients as the nation is affected by COVID-19. This includes aiding businesses as they access government support and entitlements.

The content of this article is accurate as at 3 September 2020, the time of publication. This article does not constitute professional advice. If you wish to understand the potential implications of current events for your business or organisation, please get in touch. Alternatively, our COVID-19 webpages provide information about our services and provide contacts for relevant experts who can help you navigate this quickly evolving situation.

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Further UOMI relief available for some provisional taxpayers for the 2021 year. Will you qualify?

By Veronica Harley

In early August, the Government introduced and enacted under urgency the COVID-19 Response (Further Management Measures) Legislation (No 2) Act 2020. The key measure from a tax point of view is a new use of money interest (UOMI) relief rule ("section 183ABAC") to supplement the earlier rule ("section 183ABAB") which has applied since 15 April 2020.

Why is the additional rule required?

The first rule, section 183ABAB of the Tax Administration Act 1994, allows the CIR to remit UOMI where the taxpayer's ability to make a payment was significantly adversely affected by COVID-19. It applies where UOMI is charged immediately for a missed payment, i.e. where the amount of actual tax owing is certain. But it has now been made clear by Officials that it doesn't cover interest charged for not getting provisional tax instalments correct.

Many taxpayers have since noted that, because of COVID-19, it is difficult to forecast their tax liability for 2021. For those affected by COVID-19, all they know now is that the standard method and the uplift options may be in excess of their actual 2021 liability. Taxpayers might look to estimate 2021 provisional tax, but the UOMI risk is too great because of uncertainty of how the year will yet play out. If a person switches to the estimation method at any point, UOMI will apply from the first instalment. If a safe harbour taxpayer short pays any instalment, they risk dropping out of safe harbour rules and incurring UOMI.

Who qualifies for the new relief rule?

First, it will only apply to those taxpayers who will be a provisional taxpayer for the 2021 income year and have residual income tax of $1 million or less. Therefore, it is targeted to small and medium enterprises. Large taxpayers are deliberately excluded from seeking this relief because they are more likely to be able to use tax pooling intermediaries to manage UOMI issues. But more on that later.

Second, the rule will apply if the ability to make a reasonably accurate forecast on one or more provisional tax instalment dates for 2021 was significantly adversely affected by COVID-19 and the taxpayer:

- Has estimated 2021 provisional tax on or before P3; or
- Used the standard uplift method, but short paid the last instalment (i.e. they paid the expected RIT); or
- Would be a safe harbour taxpayer, but for the fact they did not pay all instalments in full.

Further, any interest payable must not have arisen from a loss carry back election. The other points to note are that the 2021 return must be filed, terminal tax must be paid before relief can be applied for, and the taxpayer must apply for interest remission as soon as practicable thereafter.

Comment

This is hugely positive and will help some struggling taxpayers at the small end of town. The key to this section applying is being able to demonstrate to the Commissioner that COVID-19 has "significantly adversely" affected a taxpayer's ability to be able to forecast their

provisional tax payments accurately. For example, COVID-19 factors such as border restrictions, lock downs, the inability to trade fully or at all, problems with supply, lack of tourists etc will all be factors that give rise to uncertainty presently. For standard balance dates, there is still 7 months to go for the 2021 income year and it is difficult to predict what might happen. Will there be further lock downs, or will things improve? Who knows? The other important point to note is that those taxpayers that can pay their instalments and who are not affected by COVID-19 will not qualify for this relief. Nor will those that make no effort to try to forecast their 2021 liability. For those taxpayers where the relief provision won't apply or there is uncertainty whether it will, tax pooling will still be a valid option.

Thoughts from a tax pooling intermediary

Kathleen Payne, the Strategic Partnerships Manager at tax pooling intermediary Tax Management NZ, believes tax pooling provides certainty of the outcome for those who don't want to or can't apply for the remission. It allows the taxpayer to manage tax payments in a way that better aligns with their cash flow requirements while reducing the impact of UOMI. Unlike with Inland Revenue, acceptance is guaranteed and there is no need to provide any security either.

Payne says if taxpayers face uncertainty regarding their provisional tax position, there are several tax pooling options they could use.

She agrees that those who are ineligible to receive any relief under section 183ABAC should refrain from estimating their provisional tax and instead continue to use standard uplift. They should pay based on the lower of standard uplift or the forecast residual income tax. If it turns out they have underpaid, they can top up using the pool at low market interest rates and eliminate late payment penalties. Electing standard uplift means they enjoy the protection of UOMI being capped at the lesser of uplift or a third of the actual liability if tax for the year is underpaid.

One of the options for larger taxpayers who cannot use the concession is to make their tax payments into the pool, reviewing the position at each payment date and waiting until the end of the year to make transfers to Inland Revenue of the actual liability. This gives them the flexibility to obtain a quick refund of tax if they have overpaid, without having to file a return or estimate, or top up if underpaid. Refunds may be subject to meeting Anti-Money Laundering (AML) requirements. Corporate taxpayers need to be mindful of imputation credit account impacts when requesting a refund of tax they hold in the pool.

Where preserving cash is of primary importance, a taxpayer can use a tax pool to defer their provisional tax payments to a date in the future. For someone with a 7 April terminal tax date, they would have until mid-June 2022 to settle their provisional tax for the 2021 tax year. A taxpayer could pay a fixed interest fee upfront and then the core tax at an agreed future date. If their tax position changes before they reach the maturity date and less tax is required, they would simply pay less. Alternatively, they can choose to pay the full amount of tax plus interest at a date in the future once the amount due is known.

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Infrastructure tax: a new focus on internal employee capital costs

By Troy Andrews & Liz Nelson

What your employees are working on may become important under a new "Capex Questionnaire" that Inland Revenue has started issuing to taxpayers. The questionnaire targets taxpayers that have significant levels of capital expenditure (capex) or where employees are involved in capex delivery.

The focus of the questionnaire is on how employee expenditure associated with capital expenditure is treated for tax purposes (i.e. whether or not it is capitalised to the cost of the project or asset). This is often missed by taxpayers who mistakenly think that salary and wages are always deductible when incurred, rather than considering whether they should be capitalised for tax purposes.

The purpose of the eight page questionnaire is claimed to be to help Inland Revenue understand:

- what adjustments (if any) your business makes (for tax purposes and accounting) to capture the time and costs of employees engaged in capital expenditure projects;
- how that adjustment is reflected in the financial statements and tax calculation; and
- how the adjustment is calculated.

By definition, capital expenditure projects can be very broad in nature. In the questionnaire, Inland Revenue defines them as follows:

"Capital expenditure (Capex) projects in this context are widely defined and refers to all steps taken to bring assets owned by you into their present location and position. This for example, would include all expenditure incurred by the company from an initial feasibility / concept design stage through to completion / installation of the finished asset; whether that be a simple replacement. Typically, employees can be involved in capital works through: procurement (e.g. of material for capital projects); scoping projects and project selection; design, project management, consenting and legal, purchase negotiations, travel e.g. to site visits; to review plant, technology; licensing, installation, manufacture, software development and so on in order to bring an asset into being or into its present location and condition."

Clearly the definition is very broad and may include projects such as the purchase and installation of a new asset, implementing a new software system, or the more extreme cases of constructing a new plant or building.

Requirement to capitalise internal labour costs

The requirement to capitalise internal labour costs to the cost of a capital asset or project was confirmed in the 1993 High Court case *Christchurch Press Company Limited v Commissioner of Inland Revenue* (1993) 15 NZTC 10,206. In Christchurch Press, the taxpayer was a newspaper publisher who was purchasing a new asset to increase and enhance the printing capacity of the press. Some of the electricians and engineers employed by the taxpayer were used to install and wire up the new equipment. In addition, the taxpayer carried out a renovation that involved a replacement of the electrical wiring, using its own staff to carry out the work. In this case the taxpayer was denied deductions for wages paid to these staff while undertaking these capital projects.

The High Court found that the principal purpose of the wages paid to these employees over the period of the installation was for the installation of a capital asset. The same treatment would also apply if a third party contractor had been used to complete the installation and renovation works. Where there is room for apportioning wages between capital projects and deductible wages, this needs to be done on a reasonable basis.

What does this mean for me?

If your business does carry out capex projects (as most do, however small), we recommend you review how you identify costs that are capitalised to a particular project.

In particular, can you identify the specific employees or contractors that are involved in the capex project? This includes employees up the chain to the decision makers all the way down to those physically working on or building the capital asset.

Do you have systems in place by which you can capture the time spent on each particular project? Is this based on timesheets or an approximate percentage of each employee's time? Is it for the length of the project?

Are there other costs that should be capitalised, for example overheads? You should consider your basis for allocating other costs of the business, both directly and indirectly related to the capital project.

What about feasibility expenditure?

The questionnaire also puts a spotlight on distinguishing between feasibility expenditure and capital expenditure. The current view (as a result of the Trustpower decision) is that feasibility expenditure is only deductible where it is incurred in the ordinary course of business and one of the following situations applies:

1. The expenditure is not directed towards a specific capital project; or
2. A specific capital project has been identified, however the expenditure is so preliminary as not to be directed towards materially advancing that specific project.

The Inland Revenue questionnaire seeks a description of the approach a business takes to distinguishing between feasibility expenditure and capital expenditure. As this distinction is fact specific it is important that you can demonstrate there are clear policies and guidelines in place to help make this determination.

Can I depreciate these costs?

Once you have identified the relevant costs that should be capitalised to a particular project (including internal labour costs), the next step is to allocate them to a specific asset. If there is no specific asset, then it is likely that the costs will not be able to be depreciated. If there is a specific asset, for example a new piece of machinery, or even a building, then the costs may be depreciated in line with the relevant tax depreciation rate for that asset.

There are situations where no depreciable asset is created, in which case the costs will not be deductible. We refer to this as "black hole" expenditure, but legislative change is currently before Parliament to help address this.

The general rule is the tax treatment of the internal labour costs should follow the tax treatment of the capital project.

Concluding remarks

Up until now, we have not seen Inland Revenue explicitly focus on the distinction between feasibility expenditure and capital expenditure. However, this new questionnaire indicates that this may now be an area of focus. The Inland Revenue's Interpretation Statement on the deductibility of feasibility expenditure has been in place for some time now and Inland Revenue is expected to resurrect audit activity after a brief COVID-19 hiatus; it seems logical that the capital/revenue boundary is something that Inland Revenue may look to test.

We have not previously seen this type of specific focus on the deductibility of internal labour costs, however this questionnaire indicates that Inland Revenue will be focusing on this going forward for certain taxpayers.

If you have any questions about your capital expenditure and the treatment of internal labour costs, please contact your usual Deloitte tax advisor.

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COVID-19 represents unique opportunity for businesses to reconsider their options when it comes to motor vehicles

By Aaron Mitchell and Andrea Scatchard

It is commonplace amongst New Zealand businesses for motor vehicles to be used for both private and business travel. Businesses are often faced with the question of deciding whether they would be better off financially by buying or leasing motor vehicles through their business and making them available to employees, or to reimburse their employees for any business use of their own personal motor vehicles.

Due to the current COVID-19 environment and economic outlook, it is now more important than ever that businesses identify opportunities where they can reduce expenditure and maintain cash flow. The shift towards a work from home ("WFH") culture in many businesses raises the opportunity for them reconsider and potentially reduce their overall motor vehicle expenditure by ensuring they utilise a tax efficient option to suit their circumstances.

There is no magic formula though, it is very much a case of analysing each individual situation to determine which option may give the best outcome. We have outlined some of the key tax considerations below.

Buying a motor vehicle through the business

The approach of many businesses is to purchase or lease company motor vehicles and provide them to their employees for business use. A fringe benefit tax ("FBT") liability will arise where employers make motor vehicles owned by the employer available to employees for their own private use.

Private use

The general principle and starting point is that if a vehicle is available for private use at any point during the day, the entire day is subject to FBT and included in the FBT calculation. "Private use" of a vehicle ordinarily includes travel between home and work (unless home is a workplace) and any other travel that confers a private benefit on the employee.

Pool vehicles stored at the office are not usually subject to FBT as there is no private use (unless employees take them home).

Businesses should also be aware that employees taking vehicles home purely for security reasons will not in itself make the journey from work to the employee's home work-related, and therefore FBT is likely to still apply in such cases.

Exempt days

There are some specific motor vehicle exemptions which, if satisfied on a particular day, mean there is no fringe benefit provided on that day in relation to the vehicle. These include exemptions for work related vehicles, business travel and emergency callouts. These can result in significant FBT savings provided they are correctly applied and the appropriate supporting records are maintained.

FBT calculation

Once businesses have determined the days in the quarter which give rise to a fringe benefit, the next step is to calculate the value of the fringe benefit provided. The most common approach is to use a formula which takes 5% of the GST inclusive motor vehicle cost each quarter, adjust for any days on which the vehicle is not available.

Due to the current COVID-19 environment and economic outlook, it is now more important than ever that businesses identify opportunities where they can reduce expenditure and maintain cash flow.

The resulting amount is then adjusted for any employee contributions. FBT is payable on this amount.

The other approach is to base the quarterly calculation on 9% of the tax book value of the vehicle, calculated on a GST inclusive basis. Generally this method is only recommended if a vehicle has been held for at least 5 years.

Inherent business use portion
It has long been recognised that the FBT rules are inflexible and can result in over taxation where there is a high level of business use of a company vehicle. The quarterly FBT calculations have been designed by Inland Revenue assuming that the proportion of motor vehicle use is 25% business and 75% private, and take into account the average expenditure typically incurred in running a vehicle for 14,000km per annum.

As such, where the business use of a company car is determined to be more than 25% and full private use is allowed, it may be more tax efficient to reimburse the employee for work related use of their personal vehicle rather than providing a company car. Obviously the impact on the employee's remuneration package also needs to be factored into any decision here.

Motor vehicle expenditure deductions

Sole traders, partnerships and certain closely-held companies (where the only fringe benefits are vehicles provided to shareholder employees) are able to claim tax deductions for the business proportion of the running costs of a motor vehicle. The allowable deduction for motor vehicle expenditure is calculated using either a cost or kilometre rate method.

Cost method
The cost method is the total of expenditure incurred for use of a motor vehicle (e.g. registration, WOF, petrol, repairs, insurance etc.) plus an amount for depreciation, multiplied by the business use proportion of the motor vehicle.

Kilometre rate method
The kilometre rate method is less compliance heavy and allows taxpayers to deduct a fixed amount per kilometre based on rates published by IR. The deduction is calculated as follows:

IR kilometre rate x total number of kilometres travelled x the business proportion.

For an overview of the current kilometre rates, see our Tax Alert article here.

Business proportion
The business proportion must be calculated by either reference to actual records or by keeping a logbook for a test period to establish the proportion of business use.

The more common approach is to keep a logbook for a test period. The test period has to be at least 90 consecutive days and must represent the usual pattern of travel for the vehicle.

This calculation can then be used for a period of up to 3 years (provided business use does not change by more than 20 percentage points). Once this 3-year period has expired, another logbook will need to be completed. Many businesses find it easier to follow this approach rather than keeping actual records for every trip.

No records
If no actual records or logbook are maintained and the kilometre rate has not been used, then the business use proportion will be the lesser of the proportion of actual business use or 25% of total vehicle use.

As such, where the business use of the vehicle is greater than 25% of the total use, there is an incentive for businesses to keep a logbook in order to claim a greater deduction for motor vehicle expenditure. Inherent in applying the logbook approach is the need to take an odometer reading each 1 April to determine the total distanced travelled in a tax year.

Mileage allowances or reimbursements

A mileage allowance or reimbursement can be paid to employees to cover the cost of using their own vehicle for work-related purposes. The amount paid is often calculated by reference to the Inland Revenue kilometre rates for employee mileage reimbursements. Alternatively actual employee costs can be used to determine the amount paid to the employee as can other reputable sources such as the published AA rates.

Where the amount paid is no more than the amount allowed under Inland Revenue guidelines the payment will be tax free. However, if the amount paid to the employee exceeds the guidelines, the excess will be taxable.

In April 2018 Inland Revenue introduced a two tier rate structure for working out the allowable tax free reimbursement to employees. The per kilometre rate that can be reimbursed tax free reduces significantly after the first 3,500km per annum, or after the employee has driven a total of 14,000km for both business and private travel in a tax year (depending on what records are kept). Where employees travel greater distances, the amount that they can be reimbursed tax free, using the IR rates, has reduced compared with what could be reimbursed tax-free before 2018.

Employers with employees that do a lot of business travel have struggled to apply these rules in a cost efficient manner, and with managing employee expectations regarding the amount that can be reimbursed tax free. But despite these difficulties, where an employee undertakes more than 25% work related travel, reimbursing them for the cost should in principle be more tax efficient than providing a company car (where full FBT is paid on the company car).

Opportunities

The travel patterns and the business use proportions of a motor vehicle are important considerations businesses should take into account when determining whether to purchase a vehicle through the company or not. This however is only one of the large variety of factors businesses should look to consider.

The current COVID-19 environment and the long term impact it may have on the way business is conducted raises the opportunity for businesses to review the way they pay for work related travel. If businesses choose to shift to WFH arrangements on a more permanent basis, and to conducting more business virtually and reducing the amount of travel undertaken, this could result in a shift in the amount of work related vehicle travel in the foreseeable future. Motor vehicle ownership decisions that have been made in the past based on expected travel patterns may now need to be reviewed as they may no longer be fit for purpose. Similarly, employees that have maintained logbooks to support mileage reimbursement claims may find that new logbooks need to be kept if there has been a material change in the amount of work related travel undertaken.

With the importance of reducing excess expenditure and maintaining cash flow in the current economy, now is a good time to consider the tax implications of your current motor vehicle arrangements. Please contact your usual Deloitte adviser if you would like any assistance or guidance in this process.

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Inland Revenue provides initial guidance on COVID-19 transfer pricing issues

By Bart de Gouw & Julian Bryant

New Zealand's Inland Revenue (IR) has recently provided initial guidance on transfer pricing in the context of COVID-19. It recognises that the transfer pricing issues arising will be wide-ranging and vary between businesses and across jurisdictions.

IR states that transactions must continue to be conducted in accordance with the arm's length principle during the COVID-19 pandemic with existing guidance continuing to be relevant, including the OECD's Transfer Pricing Guidelines published in 2017. However, IR recognises that practical difficulties in applying the arm's length principle may arise during this time.

It is noted by IR that in exceptional economic circumstances, identifying reliable comparable data to support the arm's length nature of financial outcomes may be difficult, particularly in the short term. In the absence of comparable data, a "pragmatic approach" is suggested, involving reference to pre-COVID-19 expectations and analysis of variances that have arisen due to COVID-19 impacts, both positive and negative. This is likely to require detailed consideration of the financial impacts of the local entity and compilation of supporting evidence.

The importance of documenting the impacts of COVID-19 in contemporaneous transfer pricing documentation (i.e, a New Zealand transfer pricing local file) is emphasised. Taxpayers are encouraged to:

- identify and collate evidence to document the nature, duration and extent of any material COVID-19 related impacts on the group and local business;
- document relevant group and local business responses to the pandemic, including for example, any changes in business strategies, changes in the characteristics of product or service offerings and so forth;
- identify and explain any changes in group and local business functions, assets and risks during the impacted period, including how these relate to the business' exposure to, or mitigation of, COVID-19 impacts;
- identify and explain any changes in intra-group transactions and contractual terms;
- document the supporting rationale for any changes to intra-group transfer prices, including why they are considered to be arm's length in the circumstances; and
- identify the impact of COVID-19 on the overall profitability of the MNE group and the local entity.

The guidance is a timely reminder for New Zealand taxpayers which are members of a multinational group that historic transfer pricing approaches may not be appropriate for financial years impacted by the COVID-19. Greater analysis also may be required in respect of specific circumstances impacting the local New Zealand entity compared to previous years. This is especially the case given the relatively unique economic circumstances applicable to New Zealand businesses, including in the context of New Zealand's Covid-19 Alert Levels and periods of relatively unrestricted economic activity.

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Update on working from home allowance

By Andrea Scatchard and Jess Wheeler

An increasing number of people are working from home on a regular basis, regardless of any Government-mandated requirement to do so. In response, Inland Revenue have extended their guidance on the level of tax-free allowances employers can pay to cover increased expenses as a consequence of working from home. This is a short extension until 17 March 2021, by which time Inland Revenue plan to have released long-term guidance on such allowances.

In April 2020, in response to the requirement for all non-essential workers in New Zealand to work from home due to the COVID-19 pandemic, some employers paid an allowance to their employees to cover the additional costs to the employees of working from home. This would include costs such as utility bills from running heating and lighting, and tea and coffee and light snacks ordinarily provided at work. Inland Revenue released a Determination (EE002: Payments to employees for working from home costs during the COVID-19 pandemic), providing that a payment by an employer to their employee of up to $15 per week would be treated as exempt income and therefore tax-free to the employee. In addition EE002 allows for a lump sum of $400 to be paid tax free to the extent it is paid to employees to purchase furniture and equipment necessary to work from home. This Determination applies to payments made from 17 March 2020 to 17 September 2020. We summarised the Determination when it was first released.

In recognition of the fact that working from home is, for many, part of their "new normal", Inland Revenue is currently considering issuing a public statement that addresses allowances paid to employees outside of a work from home arrangement that is enforced during a COVID-19 lockdown period. This public statement will not be released before the expiry of ED002 on 17 September 2020, therefore Inland Revenue, on 14 August 2020, issued a variation and an extension to the original Determination that:

- removes the requirement that the employee's expenses arise because the employee is being required to work from home due to the COVID-19 pandemic; and
- extends the time covered by the Determination for a further six months, until 17 March 2021.

All other requirements in the original Determination still apply, and, as has always been the case, such allowances are paid at the discretion of the employer. For full details of the original determination, see our earlier article.

If you would like to discuss the tax treatment of any existing or planned allowances, contact your usual Deloitte advisor.

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Snapshot of recent developments:

Tax legislation and policy announcements

COVID-19: further management measures act enacted

The COVID-19 Response (Further Management Measures) Legislation Act (No 2) 2020 introduced on 4 August 2020 was passed under urgency and enacted on 6 August 2020. This Act aims to assist with the impact of COVID-19 and includes key tax amendments around eligible R&D expenditure, providing an in-work tax credit entitlement extension, and the Commissioner's additional power to modify time periods and remit UOMI on provisional taxpayers' terminal tax for the 2020-21 tax year. A special report on the legislation can be found here.

OECD Papers released

During August, the OECD released the following two papers:

- A working paper reassessing the regressivity of VAT by drawing on tax microsimulation models constructed for 27 OECD countries. The VAT is found to be either roughly proportional or slightly progressive in most of the countries examined. New Zealand is one of the three countries that have slightly regressive VAT, because the application of Goods and Services Tax is so broad with few exemptions available. In the broader context of COVID-19, the findings suggest there may be scope in many countries for VAT reform to increase revenue.
- A report discussing the main features of job retention schemes deployed by countries during COVID-19 lockdown (i.e. Wage Subsidy scheme in the case of New Zealand) and the ways these should be adjusted as restrictions to economic activities are gradually being withdrawn. The report includes discussion on whether firms who receive job retention support should be allowed to pay dividends and other forms of profit sharing in the same year. While bans may send a clear message that such support is for job retention only, they also have potential limitations.

Inland Revenue statements and guidance – Finalised items

Income tax – when is development or division work "minor"?

On 13 August 2020, Inland Revenue released Interpretation Statement IS 20/08 – Income tax: when is development or division work "minor"? which was previously open for public consultation. It is important to note that the Commissioner has set "safe harbour" figures for the absolute and relative costs to assist taxpayers with compliance. This statement applies from 13 August 2020.

COVID-19 variation for GST registered persons changing to making exempt supplies of accommodation

On 17 August 2020, Inland Revenue issued Determination COV 20/09 – Variation to sections 52(3) and 52(4) of the Goods and Services Act 1985.

This statement applies to GST registered persons with a taxable activity of supplying accommodation, who between 14 February 2020 and 31 October 2020, change to making exempt supplies of accommodation leaving them with no taxable activity. Under ordinary circumstances, the taxpayers are required to notify the Commissioner whether or not they intend to carry on any taxable activity within 12 months from the date they cease having taxable activity. The Commissioner will not cancel their GST registrations if she believes the customer will carry on any taxable activity within 12 months from the date their taxable activity ceased. This statement extends the 12 month period to 18 months, subject to the conditions that the taxpayers ceased their taxable activity of supplying accommodation as a consequence of COVID-19 and they notify the Commissioner of the cessation in accordance with the set requirements. The variation applies from 17 March 2020 to 31 October 2020. You can read more about GST on short-stay accommodation in our article from July 2020.

Note: The items covered here include only those items not covered in other articles in this issue of Tax Alert.

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