



# The Tax Lady

Accounting Services for Small Business

[www.thetaxlady.co.nz](http://www.thetaxlady.co.nz)

## Client Newsletter [February & March 2018]

### Income and IRD Audits

Increasingly, accountants, tax consultants and tax advisers see clients who face severe penalties and audits where they did not declare income and failed to meet their tax obligations.

Sometimes this can arise where taxpayers think the Inland Revenue Department (IRD) can be outsmarted, that it is possible bluff through when an IRD investigator turns up, that the occasional off-the-books transaction will be fine, or where the taxpayer inadvertently overlooked an income source. The taxpayer may find that they then become subject to a full tax audit.

### What triggers an IRD audit?

The purpose of the audit is to ensure that the correct amount of tax has been paid and that the taxpayer's obligations under the various Inland Revenue Acts have been complied with. An audit might simply be a check of a GST registration, or it could be a full investigation of business records.

The IRD can start investigations for all sorts of reasons. Some of these triggers are:

- Information anonymously received from other taxpayers: ie a tip-off. There is a form, IR873, where individuals can report suspected tax evasion or fraud.
- Computer analysis of the taxpayer's business accounts or personal tax returns. IRD has data that, once analysed, highlights potential discrepancies.
- Deviations from industry averages and cash economy. IRD has ramped up its systems of mining data to see if the income of a business stacks up against the industry levels. Tradespeople or those who operate in cash-based industries, in particular, may not always keep complete records or may overlook some takings. This can result in a nasty shock as IRD inspectors can check whether the business fits within the industry averages. If it does not, they will conduct an audit.
- Checking of third party records (such as employer or bank records) and matching to the taxpayer's records. IRD can access bank accounts and credit card data held by Kiwis in 51 different countries. They can also identify New Zealand bank accounts that have been credited with foreign income or are paying off overseas balances.
- Holding an overseas credit card or bank account. Often such accounts are used to bring overseas income into the country. A recent example is when the IRD gave a deadline to declare the transfer of pensions, as they attract tax, but some taxpayers did not declare them. The IRD had already obtained details of up to 30,000 clients from the pension firms. They waited until the deadline had passed before issuing audit letters to those who did not make the declaration.
- Random selection. Sometimes it is just that "your number is up" and it is your turn.
- Taxpayer's compliance record. Whether the taxpayer has complied with the tax laws in the past.
- Taxpayer's payment record. Whether the taxpayer has paid taxes on time in the past.
- Examination of a particular issue or problem. This might affect a particular group of taxpayers.
- Information received while conducting another taxpayer audit. This may suggest that the taxpayer's records should be checked.

Inland Revenue will not tell taxpayers which specific factor or factors led to their selection for an audit.

An audit is a costly exercise for the taxpayer regardless of its outcome. A simple investigation can cost a taxpayer thousands in professional adviser's or accountancy fees. Even where there is none or a small amount of undeclared income, the process is not only costly but also stressful.

Where penalties and interest are imposed, these may be more than the core outstanding tax. However, penalties can be significantly reduced if the taxpayer discloses any undeclared income before the commencement of an audit whether it was omitted accidentally or by design.

Recent IRD investigations saw \$146 million recovered in "hidden economy" discrepancies in the hospitality industry while given recent property activity, a 52-member IRD property compliance team now focuses on identifying landlords and speculators who may have avoided or evaded tax. It is believed that for every \$1 spent by the IRD on investigations, approximately about \$5 is recovered.

If you have any concerns regarding any undeclared income, please get in touch so we can discuss your particular circumstances.

## **Leaky building remediation costs**

The Inland Revenue Department has updated the Residential Property "Leaky buildings" webpage.

Inland Revenue have highlighted the steps to work out the type of repair and maintenance costs of the leaky building (as a rental property) and whether you can claim them as a deduction for tax purposes.

Generally, where a buyer purchases a property that is leaky, none of the remediation work is deductible because it is usually reflected in the purchase price of the property.

The deductibility of remediation expenses is based on the IRD's Interpretation Statement IS 12/03 Income Tax – deductibility of repairs and maintenance expenditure – general principles . This provides detailed analysis on the matter.

To find out more go to [www.ird.govt.nz](http://www.ird.govt.nz) (Search keywords: leaky buildings).

## **Promoting Your Business**

There is nothing like the start of a new year to promote your business "special-ness" or unique "core" differentiator.

If your current marketing material does not actively promote what is different about your business, you are missing a huge opportunity to grow and increase sales. The common marketing mistake that business owners make is to promote the features and price of their products and services rather than the benefit clients would receive without offering any other point of differentiation. Marketing this way fails to educate your potential customers and clients about the real differences that your business offers – the differences that make yours the better business to deal with.

Your unique core differentiators must permeate your entire business:

- The way your team members present themselves
- The way you deal with your customers or clients
- The way your business presents itself.

Virtually every area of your business must fulfil that differentiation. Because of that, unique core differentiators are powerful in 2 ways:

1. They articulate exactly what the customer wants, and
2. They give a laser-like focus to everyone on your team.

This means that when you identify your unique core differentiators, you will have a much better chance of building a better business - one that stands out from the rest of your industry. A business that potential customers will want to deal with because they know you will serve them better.

Important: This is not advice. Clients should not act solely on the basis of the material contained in the Client Newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We therefore recommend that our formal advice be sought before acting in any of the areas. The Client Newsletter is issued as a helpful guide to clients and for their private information. Therefore, it should be regarded as confidential and should not be made available to any person without our prior approval. 01/2018.