



Budget - May 2010

There were a couple of surprise changes in the *Budget* announced on Thursday, even though a number of changes had been widely tipped prior to the announcement.

The two biggest surprises were tax relief for *middle income earners* and the lowering of the *Company tax rate* from 30 cents to 28 cents, these were widely kept secrets. On the other hand *property investors* took a bit of a hammering, but at this stage not as bad as had been widely predicted.

So what does all mean for us?

Income Tax Changes for Individuals

As expected, the Budget cut the top and bottom income tax rates for individuals, but delivered larger than expected benefits for middle income earners. Previously, personal tax rates were hinted at falling from 38cents, 33 cents, 21cents and 12.5cents to 33 cents, 19cents and 10 cents. In reality they fell as follows:

	Pre Budget	<i>1 October 2010</i>
Income above \$70,000	38 cents	<i>33 cents</i>
Income from \$48,001 to \$70,000	33 cents	<i>30 cents</i>
Income from \$14,001 to \$48,000	21 cents	<i>17.5 cents</i>
Income from \$0 to \$14,000	12.5 cents	<i>10.5 cents</i>

GST to Increase

Tempering the tax reductions above, will be the fact that *GST increases from 12.5% to 15.00%*. This increase will take *effect also on the 1 October 2010*. So with the GST increase and the tax deductions, what does that mean for us, the following table gives a brief overview.

Annual Pay	Tax Reduction	GST increase	Total Change
40,000	22.28	12.94	+9.94
46,000	26.92	14.68	+12.24
50,000	29.42	15.71	+13.71
54,000	31.73	16.75	+14.98
58,000	34.04	17.80	+16.24
62,000	36.35	18.84	+17.51
66,000	38.65	19.88	+18.78
70,000	40.96	20.92	+20.04

Company Tax Rate Change

From the 1 April 2011, the Company tax rate will reduce from 30 cents down to **28 cents**. For once, this puts us ahead of Australia, who plan to reduce their Company tax rate to 28 cents but phased in over 3 years commencing from 2012 / 2013.

So what does this do for us? A lower company tax rate will encourage productive investment in NZ, thereby increasing productivity, raising wages and creating jobs (that political speak, as it comes from Treasury).

Depreciation - on Buildings goes / New Plant & Equipment reduced

Depreciation deductions will no longer be allowed for buildings with an estimated useful life of over 50 years or more. This applies directly to rental houses and the commercial sector. From a conceptual view, this is one scenario that is hard to agree with, as we all know that properties that are tenanted do depreciate, while the land they sit on appreciates.

What we may see coming out of this, is commercial property managers fronting up to the IRD and **attempting** to prove that their buildings have depreciated in terms of having a short life option of less than 50 years. For example cool store operators and meat operating plants.

However, on the positive side landlords will not face the feared ringfencing option, which would have meant they could not use losses on their rental to reduce their overall tax bill.

One item that has crept into the equation but has not been given too much media comment is the effect on QCs / LAQCs (residential property investors are still the greatest users of these sorts of entities) on the actual taxation of these companies. We will discuss those next.

One other item of concern is the commercial building fit out policy. At this stage it still exists but MAY yet be tightened as the Government has hinted that it intends to review the deductions if it deems fit.

With respect to residential properties, any rethink is likely to be a continuation from previous years, where the focus goes on what constitutes part of a building and what does not.

Businesses will also not be allowed to claim the 20% accelerated depreciation on new plant and equipment. This change is effective immediately. So assets purchased up to and including the 19 May will still get the deduction while assets purchased from the 20 May will not.

We consider this a bit harsh as the justification for the reduction is that some businesses may buy a car or a computer and get the 20% loading but not invest in a second hand piece of machinery, because they cannot load the depreciation claim.

Loss Attributing Qualifying Companies (LAQCs)

The comment made in the budget was *"Many investors hold property through LAQCs. After a short period of consultation, legislation will be proposed so that from 1 April 2011 all LAQCs will be taxed as limited partnerships"*

Prior to the Budget there was some speculation, that LAQCs would be dropped and that property losses would be ring - fenced in the vehicle making the investment.

Although the proposed loss ring fencing rules are not comprehensive, the new rules do limit the amount of losses that can be passed from and LAQC to the shareholder.

These losses will be limited to the amount the shareholder has invested in the LAQC – very similar **to Ltd Partnerships**.

The new rules mean that where investors want to be able to access the losses at their own personal tax rates by passing through the losses, they must also **pay tax on the income in the good years at their personal rates**.

Investors in properties, may need to look at whether an LAQC is the best investment for the future.

Working for Families Adjustment

From the 1 April 2011, the value of assets held in Trusts will be countered as part of the household's income when calculating the Working for Families. Investment losses and PIE income may also be included. In terms of what the Working for Families is about, this adjustment is fair as it places a more accurate entitlement to the assistance.