MeadStark
CHARTERED ACCOUNTANTS

29 The Mall, PO Box 31, Cromwell 445 0616
38 Ardmore St, PO Box 51, Wanaka 443 8717

Setting up your business

The decision to set up a new business should never be taken lightly. With a new business there is a myriad of administrative demands that must be taken care of before or along with providing the goods or services that you were planning to provide.

Things to consider before opening for business include:

- How long is it going to take before you start making money? There are often a lot of costs to incur before the business is up and running: rental in advance, stock and supplies, professional advisor fees, sign writing, advertising, new assets etc. Where is this money going to come from? A budget of costs is very important before committing to anything. You will also have to have money to live on whilst the business gets established.
- Setting up a separate bank account, this will make administration of the business far easier
- How your customers are going to pay, do you need to get an eftpos machine or cash register, will you accept cheques, can customers pay online?
- How are you going to produce tax invoices for customers: invoice book, detailed computerised invoices or till receipts?
- How are you going to keep track of which customers have paid and which are still to pay?
- What business structure is appropriate (company, sole trader, partnership)
- Complying with your tax obligations (see below for detail)
- You will need to hold onto all your records including invoices and receipts for a period of seven years to meet you obligations under the tax rules
- Do you have someone with experience running a business who can act as a mentor to help you over the first year or so?

Tax Obligations

Understanding your tax obligations takes a considerable amount of stress out of running a business so having a discussion with an accountant before embarking on a new business is time well spent. Many businesses find complying with tax obligations burdensome.

A number of businesses get into difficulties because they fall behind with tax payments and/or fail to keep good records. Late payment of tax obligations is generally very expensive as the IRD charges interest and penalties. This information sheet offers you some ideas to help you manage your tax obligations more easily.

Understand your basic obligations

Your first task is to gain an overview of the compliance obligations every business faces. Here are two sources of help:

- **Make use of free help first**

If you are new to business, or you are having difficulty with your tax compliance, make use of the free services offered by the Inland Revenue Department (IRD).

Visit: www.ird.govt.nz

Inland Revenue
Te Tari Taake

It features free guides and how to instructions on various aspects of tax, and frequently asked questions (FAQ). You can also download a wide variety of forms, as well as complete forms online. Note: you may find some of their articles to be a little confusing (and one sided).

View our website for more helpful web based resources

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Chartered accountants provide the best advice

Few businesses achieve success without the help of good advisors. Here are some of the benefits of using a chartered accountant as your tax agent submitting tax returns on your behalf and as a tax advisor

- ✓ Chartered accountants deal with tax issues every day and keep up with the latest tax rulings and changes. It makes more sense to use a specialist than to divert your energies from your core business activities, in an attempt to keep up with changes that might affect your business.
- ✓ A chartered accountant can help you set up a good record keeping system and a calendar of tax returns to streamline your tax compliance, reducing the time you spend calculating your tax obligations and likely reducing the cost of tax compliance.
- ✓ You'll get reminders of due dates for terminal & provisional tax, helping you to avoid late payment penalties.
- ✓ Submitting your end of year tax returns is time consuming and tricky for beginners. Your chartered accountant has the experience of preparing many returns each year.
- ✓ A chartered accountant can help you claim all the expenses you're entitled to — and are likely to be aware of more than you are.
- ✓ A chartered accountant can advise you of the best structure for your business to meet your needs and protect your assets
- ✓ You also get advice on issues such as the tax advantages of leasing versus buying equipment, using a private vehicle or company car, and other tax matters.

If you consult your accountant more regularly than just for end of year accounts, you should expect to pay more for the service. Remember though, that low fees are not as important as the value the chartered accountant can add to your business. Mead Stark prides itself on offering high quality advice at a competitive price.

A tax compliance overview

The four main taxes that most new business owners will encounter: income tax, PAYE, GST and ACC levies.

Managing your income tax

Income tax is payable on the net profit or surplus of your business. That is the difference between your business income (for the goods and services you sell) and your tax deductible business expenses.

Generally, claimable business expenses are those expenses incurred in the production of goods and services for sale. Some typical business expenses you can claim include office rent, stationery and supplies, wages, electricity, business phone, etc.

The capital you introduced into business or drawings you take out are not taxable. Also, all plant and equipment you buy for the business must be depreciated over a period of time (so that you can only claim a percentage of the costs each year).

Income tax in your first year of business

Many people starting out in business are under the illusion that they don't have to pay tax in the first year. This is certainly not the case. The illusion of a 'tax holiday' comes about because the income of a new business cannot be properly assessed until the first year's accounts have been completed. Tax is then due on the net profit (if there is any).

If there is a profit, the business may be required to pay provisional tax during the course of the following year, based on the results of this first year, plus a percentage for growth in the coming year, or an estimate of likely profits in the year ahead.

Many new businesses find this 'double' tax bill in the second year (tax on the first year's trading, plus provisional tax for the second years trading) a difficult burden, as they have not made suitable provision for the tax payments.

Provisional tax is similar to PAYE for a wage or salary earner: it is a way of spreading out taxes for a business, so that instead of the business facing one large tax bill at the end of the year, the payments are evened out during the course of the year. The tax is called 'provisional' because the amounts are only an estimate, until the actual net income is determined at the end of the trading year.

The difference between the tax on actual net income and the provisional tax paid is sorted out in a terminal tax payment. This could mean an additional payment (if the business has done better than expected and not enough tax has been paid) or a refund from the IRD (if the reverse is true).

Your accountant will help you sort out the calendar of dates involving provisional and terminal tax and explain the process more fully to you. You can also download a tax calendar (covering all tax payments) from the IRD's website.

- **Dealing with the Goods and Services Tax**

You must register for GST if your business income exceeds $60,000 per year. This means that you must add GST to all your invoices, but you gain the benefit of being able to claim back the GST you pay on business expenses. You are required to pay the difference between GST gathered on income and GST spent on expenses calculated on GST returns that you submit periodically.

Smaller businesses with a turnover of below $500,000 per year have a choice between filing GST returns monthly, 2 monthly, or every 6 monthly.

At start-up you might typically get a GST refund because your expenses have been higher than your income. However, once you are up and running you should expect to be making GST payments as your income should exceed to GST expenses. If you keep getting GST refunds, your business is likely to be losing money!

GST returns are simpler to manage than the end of year accounts used to calculate income tax, and many businesses complete the GST returns themselves. The task is made easier still if you use an accounting software program that allows you generate GST returns at the click of a button. Mead Stark can help you get set up for this.

You will need some advice at the beginning from your chartered accountant on how best to make the returns, which items (such as bank charges, wages) carry no GST, and how to handle other adjustments (such as exported goods, or zero GST rated supplies).

- **Avoid the cashflow trap**

Remember that any GST you collect on invoices does not belong to you. Do not fall into the trap of using the GST you accumulate from customers to help fund your business.

- **PAYE Tax**

If you employ staff you must always deduct PAYE (pay as your earn) tax. If the PAYE for your business is less than $500,000 p.a. you must pay IRD monthly, due on the 20th of the following month. Larger businesses where their annual PAYE is more than $500,000 are required to pay twice monthly, and must file their PAYE electronically.

In addition to PAYE, employers may also need to undertake deductions for: student loan repayments, child support, KiwiSaver, ESCT or any benefits, bonuses or other allowances.

- **ACC Levies**

As an employer, or if you are self-employed, you are responsible for paying the annual ACC levy, which provides cover and compensation for work-related injuries. Your annual levy is based on the type of industry you are working in and the amount you pay in wages and/or your annual income. Be aware that if this is the first year of trading ACC levies are calculated based on the reported wages for the year which can only be calculated once the year is finished so the first ACC bill will cover 2 years, for the year passed and the year coming up.

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Your duties as an employer

If you employ staff, your responsibilities include:

- Keeping appropriate wage and salary records.
- Deducting Pay As You Earn (PAYE) tax from pay cheques (which includes employee ACC levies).
- Deducting other relevant taxes such as student loan repayments and child support payments.
- Remitting the PAYE and other taxes to the IRD by the 20th of the following month (if annual PAYE is under $500,000).
- Providing employment contracts for all employed staff.
- Developing appropriate work place policies, and implementing policies and procedures to meet all Health and Safety Standards.
- Pay employer related expenses including Holiday Pay, Sick Leave, Annual Leave, and ACC.
- Meet all employer related KiwiSaver obligations including employee deductions, employer contributions, and KiwiSaver related administration

Home businesses

If you run a business from home, you can claim a proportion of certain costs, such as telephone costs, plus a portion of the home rates rent or mortgage interest and power costs. Typically this is based on the percentage area of your home dedicated to your business. Visit the home business section of the IRD website www.ird.govt.nz for more details, and/or speak to us.

Record keeping

Keeping accurate, up-to-date records is essential. These should include:

- Banking: cheque books, deposit books, bank statements
- Your income: invoices, credit card sales, debit and credit notes
- Your expenses: invoices for purchases, credit card purchases
- Cashbook: a record of sales made paid for in cash or expenses paid out of cash
- Wagebook: a record of wages paid to employees including tax deducted (note that software is available to assist with this)

Good management includes:

- Estimating your tax liabilities at regular intervals and setting aside money to meet tax obligations. Consider opening a separate bank account for this money so that it is not confused with your other funds.
- Being aware of due dates for taxes to avoid penalties. Visit the IRD's website www.ird.govt.nz for details of late payment and late filing penalties. It is important to be on time!

If you are unable to make an IRD payment on time contact the IRD to discuss the situation, just like your business would like your customers to talk you if they are going to be a day or two late, so does the IRD. They can also consider payment arrangements

Final Comments:

- Gain a clear overview of your tax obligations, but get expert advice on details from your accountant.
- Keep good records to take the stress out of your tax work and to minimise accountancy fees.
- Eliminating tax 'shocks' is the sign of a competent business manager. Work with your accountant to prepare for your tax bills.
- Claim the expenses you're entitled to, but don't become obsessed about minimising your taxes. Focus instead on growing your business.
- Be happy about paying taxes: you only pay tax when you are making money.