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Fineprint

INSIDE:

Gift Duty Abolition

HOW WILL IT AFFECT YOU?

The proposed abolition of gift duty on 1 October 2011 will affect many New Zealanders. The implications of not having gift duty will extend not only to the thousands of people who have trusts, whether or not they have a gifting programme in place, but also others as well. This article looks at the consequences of no gift duty after 1 October.

Draft legislation has now been prepared (but not finalised when we went to print) that will abolish gift duty on 1 October 2011.

Gift duty collection

Gift duty was originally imposed in New Zealand in 1885. It was introduced to prevent the avoidance of estate duty (commonly known as 'death duty') by discouraging the gifting of assets prior to death. In 1992 however, estate duty was abolished or, more precisely, reduced to a 'nil' rate. Gift duty was retained, primarily to prevent the transfer of assets which could have an effect on government programmes such as the granting of residential care subsidies, the payment of Working for Families tax credits, student allowances and so on.

The government has acknowledged that only a minimal amount of gift duty is received; just over $1.6 million in the 2009-2010 financial year and just under $1.5 million in the 2008-2009 financial year. More than 225,000 gift statements are filed each year, of which only 0.4% result in an obligation to pay gift duty.

It must be emphasised that, at this stage, gift duty has not yet been abolished. Gift duty should still be paid for any gifts over $27,000 per 12 month period that are formalised before 1 October 2011. For the purposes of this article, however, we will presume the abolition of gift duty will occur from 1 October 2011.

Consequences for family trusts

With gift duty being abolished, family trust administration is likely to be simplified. Presuming no restrictions are given on the ability to gift assets of any value, any amounts owed by a family trust can be forgiven in one sum after 1 October 2011.

This does not mean you sign a Deed of Forgiveness of Debt only once. Many people pay regular amounts into their trust/s and, for many, it may still be

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necessary to continue to sign further Deeds of Gift or Deeds of Forgiveness of Debt and/or trustees resolutions in future years.

The abolition of gift duty will be advantageous if you have formed a family trust to divest yourself of assets as it means that your trust will own all the assets and there will be no outstanding loans owing to you.

Currently, a settlor would ordinarily form a family trust and then would transfer to that trust an asset or assets. To avoid paying gift duty the settlor lends the trust the total purchase price and then forgives the resulting debt owed by the trust at the rate of $27,000pa. The result is that the settlor no longer owns the assets but has substituted them with a loan which, in many cases, is very large. In the event that a claim was successfully brought against a settlor, then the property transferred to the trust would in most instances be safe, however the outstanding loan owing by the trust to the settlor could still be 'attacked'.

A common example of this would involve a trust being formed and property transferred to it prior to a relationship starting to avoid the 50:50 division of assets under the Property (Relationships) Act 1976 (PRA). The transferred property would not be relationship property, however a share of the outstanding loan owing to the settlor by the trust can be (and frequently is) presently claimed by the settlor's partner as relationship property.

Another example involves the settlor forming a family trust and transferring assets into it to avoid the provisions of the Family Protection Act (in which a child or grandchild who is not left what they consider to be an adequate legacy under a Will may apply to the courts for a more significant payment). Property transferred to a trust is probably safe; however currently the debt owing to the settlor by a family trust can be attacked.

In both of these instances the forgiveness of the entire loan in one lump sum (which can be done after 1 October) will leave a claimant with very little to attack.

Limitations on gifting

The abolition of gift duty on 1 October will not automatically remove all potential problems associated with the gifting of either property or outstanding loans as there is already legislation in place that can assist some claimants.

If, for example, a settlor was subsequently bankrupted after gifting all his or her assets into a trust, the Official Assignee (the court-appointed administrator of bankrupts) can annul any gifts that took place within two years of bankruptcy. For gifts made more than two years and less than five years after a bankruptcy the Official Assignee can also apply to the court to seek an annulment, if the person bankrupted cannot demonstrate that he/she was solvent when the gift was made.

Similarly, the Property Law Act 2007 allows the court to annul the transfer of assets when it is demonstrated that the person transferring assets acted recklessly and intended to avoid paying debts by transferring assets.

Other than trusts

The abolition of gift duty will not only affect family trusts; it will enable anyone to transfer assets to others without the need to pay gift duty. For example, a person could gift cash or assets of more than $27,000 pa to any other person without the need to pay gift duty.

Similarly, a house owner could transfer a one-half interest in the house to a partner without the need to either pay gift duty, or enter into a debt and gifting programme, or without the expense of signing a s21 agreement under the PRA.

What should you do?

Although it is not 100% certain that gift duty will be abolished, there is no reason to think the government will not follow through on its intentions. However, to be on the safe side, we recommend that until 1 October 2011 you should continue with your current gifting programme.

After 1 October you should decide whether you want either to continue your gifting programme or to forgive the entire debt as a lump sum.

Whatever you choose to do, we recommend you keep in contact with us and your accountant to decide whether it is necessary to gift further amounts in future years.

When gift duty is abolished and you do not have a trust, you may wish to consider forming one as the transfer of assets to it will likely be much simpler and straightforward than it has been. ■

Tax Changes Affect LAQCs

Tax changes initially proposed in the May 2010 Budget became law late last year when the Taxation (GST and Remedial Matters) Bill was passed. Property investors, in particular, have been targeted and new provisions include:

- Perceived loopholes are now closed in the tax treatment of Loss Attributing Qualifying Companies (LAQCs). From 1 April 2011 shareholders cannot deduct losses at their marginal tax rate and pay tax on profits at the lower company tax rate as the LAQC regime will have ceased on that date.
- From 1 April landlords and businesses cannot claim depreciation on buildings with an estimated useful life (for tax purposes) of 50 years or more, and
- Landlords and businesses can still claim depreciation on the fit-out of commercial and industrial buildings, as well as depreciation loading on other assets where investment decisions were made before 20 May 2010 (Budget Day) but not finalised until sometime after.

Property investors currently using a LAQC have a number of options including conversion to a Qualifying Company (QC) or to the new Look Through Company (LTC) regime, both of which are favourable in allowing capital gains to be distributed tax-free. ■

Dying Intestate

MAKE SURE YOU HAVE A WILL

For many people the thought of making a Will seems morbid and unnecessarily negative. However, every adult should have a current and valid Will; they are not just for the elderly and terminally ill. This article looks briefly at what a Will should contain, and also shows how complicated things can get for your family if you die intestate (without a Will).

Having a Will ensures that your wishes about what you would like done with your property after your death are properly carried out. A Will generally includes:

- The names of the people who you wish to deal with your estate after your death (your executors and trustees)
- Specific wishes for your funeral, burial or cremation
- Bequests (gifts of money or property) to people or charitable organisations
- Appointment of a testamentary guardian if you have children under 18 years old
- Directions about the continuance of any businesses you own
- Administration of trusts established by your Will, and
- Distribution of the balance ('residue') of your estate (everything else that you have not distributed or paid out in your Will).

Not only must your Will be drafted accurately to ensure your wishes are carried out as you want them to, but it also needs to be signed and witnessed correctly. A Will incorrectly signed can be invalid. Being left with an indication of your wishes but no legally sound basis for carrying them out could become an expensive, frustrating and emotionally draining experience for your family. Having your affairs tidy will be much appreciated by those left behind.

If you have no Will

Many people are under the impression that if you die with no Will (called intestacy), your assets automatically go to the government. This is incorrect. If you die intestate, the government has a statutory formula to distribute your assets.

- With spouse, civil union or de facto partner and no children. *All assets go to your spouse/partner*
- With spouse, civil union or de facto partner and children. *All personal chattels and up to $155,000 go to your spouse/partner. Any balance is divided between your children and your spouse – 1/3 to spouse/partner, remaining 2/3 distributed equally amongst your children*
- With spouse, civil union or de facto partner, no children but one or more parents alive. *All personal chattels and up to $155,000 go to your spouse/partner. Any balance is divided between your parent/s and spouse; 2/3 to your spouse/partner, 1/3 to your parent/s*
- With children but no spouse, civil union or de facto partner. *All of your assets are distributed equally amongst your children in equal shares*
- With one or both parents, but no spouse, civil union or de facto partner, no children. *All of your assets are distributed to your parent, or if two survive, equally between them*
- With brothers and/or sisters, no parents, spouse, civil union or de facto partner, no children. *All of the estate is held for your sibling/s. If more than one sibling, your estate is divided equally between all.*

Note, in all cases where a child receives assets, those assets are held in trust until the child is 18.

If none of the above apply, then the court will look to maternal or paternal grandparents, or aunts and uncles, and your estate is distributed like this:

- Half to the paternal grandparent/s. *If they are dead then your estate is divided equally among aunts/uncles. If none, the paternal half of the estate goes to the maternal side of the family*
- Half to the maternal grandparents/s. *If they have died, your estate is divided equally among aunts/uncles. If none, the maternal half of the estate goes to the paternal side of the family*

If none of the above situations apply, your estate will belong to the Crown. The Crown may make a payment to people who would reasonably expect you to have made provision for them under your Will, if one had been written. These people may be godchildren or those who could have looked after you in your final illness.

If you don't have a current Will, we recommend that you get one as soon as possible. It will ensure your wishes are carried out, and allow your family to grieve your loss without the uncertainty of having to deal with the government's statutory formula for dividing up the estate. ■

Protecting Your Family's Inheritance

A SIMPLE ASSET PLANNING TECHNIQUE

Every New Zealander wants to protect their well-earned assets and pass some of those on to their family. This article looks at a safe and straightforward way to help protect your family's assets and preserve an inheritance if you do not have a trust, particularly if rest home care becomes necessary.

A government subsidy is paid for people living in rest home care, however it is subject to income and asset testing. With the current asset threshold at $200,000, many people need to use a substantial proportion of their own assets and/or income to help pay for their care before they are entitled to any of the government subsidy.

A simple way to protect at least some of your assets is to change the way they are owned.

Most couples own their property, bank accounts and investments as joint tenants. When one person dies the ownership of the property automatically transfers to the survivor. However, if you change the asset ownership from 'joint tenants' to 'tenants in common', each spouse or partner will then own a distinct share (usually an equal share) of the asset. You then make these simple changes to your Will, described below.

When one spouse dies their share of the assets are held in trust for the final beneficiaries, and the surviving spouse still owns his/her own share of the property. The Will allows the survivor to use the deceased's share of the property so they have a right to remain living in the house for as long as they want, the right to buy a new house, and a right to income and capital. As the surviving spouse does not own the deceased's share of the estate (but have their rights protected under the Will) the deceased's assets are not subject to assessment for rest home subsidy purposes. This is called a life interest Will. To illustrate how this could work let us look at two examples.

Joint tenancy

Janet and John own a $500,000 house. When John dies the house transfers to Janet who now owns a $500,000 house in her name. Janet must move into a rest home and sells the house to pay the rest home fees, $300,000 of the house sale proceeds must be used to pay rest home fees before the government's subsidy comes into effect. Only $200,000 will be left for the family.

Tenants in common

Janet and John own a house worth $500,000, with their half shares being worth $250,000 each. On John's death his estate is worth $250,000 and does not transfer to Janet; it is held in trust for the beneficiaries under his Will.

Janet's assets are now $250,000. When Janet sells the house and moves into a rest home $50,000 of her own money must be used to pay rest home fees before rest home subsidy becomes available.

Changing your property ownership from joint tenancy to tenants in common is an effective estate planning tool and changes your Will. It is quick and cheaper than setting up a trust. It retains control of the assets in your own hands rather than transferring them to a trust.

We do recommend, however, that you talk with us on any estate planning matter as we will give you advice that is tailor made to your own circumstances.

Overseas Investment Office provides extra clarity

The December 2010 Ministerial directive letter to the Overseas Investment Office (OIO) took effect on 13 January 2011. The directive letter provided extra clarity and certainty for potential investors on the government's general approach to foreign investment in sensitive assets.

The letter addresses concerns around large scale (measured at x10 larger than the average farm) overseas ownership of farmland and vertically-integrated primary production companies.

The changes include two new factors the OIO must take into account under the benefit test used to assess investments in sensitive land:

1. A new 'economic interests' factor allowing ministers to consider whether New Zealand's economic interests are adequately safeguarded and promoted. This will improve ministerial flexibility to respond to both current and future economic concerns about foreign investment such as large-scale ownership of farmland.
2. A new 'mitigating' factor enabling ministers to consider whether an overseas investment provides opportunities for New Zealand oversight or involvement, for example, by appointing New Zealand directors or establishing a head office in this country.

The Minister of Finance Bill English said, "The new factors are in addition to a range of existing factors and a good character test – these are designed to ensure overseas investment results in genuine benefits to New Zealand.

"Beneficial foreign investment makes a positive contribution to New Zealand through increased jobs, capital and access to export markets.

"At the same time, the government recognises there are genuine public concerns around some overseas investment in our productive land. Taken together, the changes outlined in the letter achieve an appropriate balance."

The Timing of Your Claim

OVERHAUL OF THE LIMITATION ACT

The Limitation Act 2010 came into force on 1 January 2011 and replaced the Limitation Act 1950. It significantly alters the law on limitation defences. The new Act addresses some of the unfairness in the 1950 Act by providing greater certainty about when claims will be time-barred.

At the heart of the new legislation is the objective to achieve a balance between the rights of claimants to seek relief for justified claims, and the rights of defendants to have protection from stale claims being made against them.

The new Act provides that for most 'money claims' the limitation period is six years from the date of the act or omission on which the claim is based (the primary period). This means that a defendant may be able to raise a defence to any claim brought outside the primary period.

Late knowledge provision

Also introduced in the new Act is a late knowledge provision for the situation where the primary period has expired and the claimant belatedly gains knowledge of the facts necessary to bring a claim. In these circumstances, a claim can be brought within three years from the date the claimant acquired or ought to have acquired such knowledge.

This change addresses the unfairness that arose under the 1950 Act where the limitation period could expire before the claimant had any knowledge of the facts required to bring their claim. However, as this potentially could have allowed for indefinite liability, the new Act provides a long-stop restriction that no claim can be brought 15 years after the date on which the act or omission occurred.

It is important to note that the new Act applies to claims based on an act or omission after 31 December 2010. For claims occurring before 1 January 2011 the 1950 Act will continue to apply. Nevertheless, any claims under the 1950 Act must be brought by the later of five years ending on the close of 31 December 2015 or 15 years from the date of the act or omission. This means that the 1950 Act should be largely phased out by 1 January 2016.

There are some exceptions to the provisions. In particular the courts have retained discretion to grant relief in exceptional cases where a limitation defence would otherwise apply.

To better protect yourself and your business from potential claims, we recommend that you keep your personal and business records for at least 15 years in case a claim is made.

If you are concerned that you may fall into an exception category then we recommend that you talk your situation over with us. ■

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Post**script**

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Disaster preparedness

Since the September and February earthquakes in Christchurch, all New Zealanders are all now only too aware how important it is to be prepared for a disaster, including having an extensive survival kit. There is not enough space here to provide comprehensive information, and there is of course a plethora of advice available. We do, however, recommend that you are prepared:

- At home
- In the office
- At your holiday house, and also
- In your car.

Whilst Kiwis are probably now much better prepared and organised than we used to be, we cannot reiterate enough how important it is to have a plan, and make sure everyone in your office and your family knows what to do and how to do it.

New minimum wage rates

Minimum wage rates rose on 1 April 2011. The adult minimum wage increased from $12.75 to $13.00/hour. This equates to $104 for an eight hour day and $520 for a 40 hour week.

The trainee and new entrants' minimum wages increased from $10.20 to $10.40/hour also from 1 April 2011. That's $83.20 for an eight hour day, and $416 for a 40 hour week.

There is more about the minimum wage rates on the Department of Labour's website: www.dol.govt.nz

Overhaul of securities law coming up

The government announced in mid-March that New Zealand's securities law will undergo a comprehensive review. An exposure draft will be available for public consultation in August.

Together with the establishment of the Financial Markets Authority, the new securities law regime will largely complete the financial sector's major regulatory reform programme, said Commerce Minister Simon Power.

The review will result in a re-write of a great deal of legislation including the Securities Act, the Securities Markets Act, the Unit Trusts Act, the Superannuation Schemes Act and the non-tax parts of the KiwiSaver Act.

Officials will engage with industry during the drafting process, and the government hopes to introduce the bill to Parliament by the end of the year.

Public Holidays: Easter 2011

This year ANZAC Day (25 April) falls on Easter Monday and both days will be observed simultaneously.

This means the only public holidays in 2011 at Easter weekend will be Good Friday and Monday, 25 April, with Easter Monday and ANZAC Day being recognised as one public holiday.

Employees who normally work Mondays and Fridays will be entitled to those days off on full pay. If, however, these employees work on either of the two public holidays they are entitled to be paid at the rate of time and a half and get a day off in lieu for each public holiday worked.

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