GIFTING AND RENTAL PROPERTY INVESTMENTS

Two relatively significant changes to our tax structure are to occur in 2011.

Gift duty

The government intends to abolish gift duty. Currently, anybody who gifts more than $27,000 worth of their assets in a 12-month period is liable to pay tax on the amount over that amount. This is to ensure people do not divest themselves of assets in a way that is both detrimental to the tax base of the country and would defeat any creditors of the person making the gift.

People with family trusts will be aware of the gifting regime.

Inland Revenue has confirmed that only approximately $1,000,000 of gift tax is collected annually. That contrasts with the many more millions that are spent policing the system.

So, on 1 October 2011 the government has indicated this tax will be abolished. This will mean that a couple with a house valued at $540,000 can immediately transfer that house into a trust and have the whole value of that asset owned by the trust, instead of having a debt back to the original owners forgiven at the rate of $54,000 every year ($27,000 per owner).

But any creditors of the owners will still be able to attack the transfer, if it is done to defeat their claim.

What also seems likely to remain is the ability of government departments to “claw back” transfers in situations where owners take advantage of social assistance programmes such as aged residential care subsidies.

Presently, if an elderly person is asset rich but cash poor, the government will pay their aged care costs (approximately $35,000 per year) but then place a charge over the home of the elderly person to recover the bulk of those costs when the house is sold.

One way around that is to transfer the house out of the name of the elderly person.

The government treats any such transfers within 5-10 years of the elderly person going into a rest home as done to avoid the repayment of the subsidy. The government can reverse that transfer and treat it as if it never happened - a claw back.

RENTAL PROPERTY INVESTMENTS

The other interesting tax change focuses on investment properties.

Loss Attributing Qualifying Companies (LAQCs) were originally set up to help small business owners, and were not primarily designed for investment property ownership purposes.

In terms of tax advantages, they offered no more advantage (in terms of claiming losses against income) than owning the property in your own name. Their advantage lay in the flexibility around the transfer of shares.

LAQCs were abolished from 1 April.

Prior to 1 April, it was possible to apply to become a Qualifying Company (QC) which is a normal limited liability company, where losses are able to be carried forward to be used against profits, and where shareholders are liable for all company related taxes. An advantage of the QC is that capital gains can be distributed without having to liquidate the company.

Under a new entity that is created, the Look Through Company (LTC), losses and profits will be able to flow through to the shareholders' personal tax returns, and dividends from capital gains are tax free to shareholders.

However, the offsetting of losses is subject to a limitation which takes into account shareholder loans, including shareholder guarantees and shareholder current accounts.

Because LTCs are transparent, shareholders will be regarded as holding the assets directly and therefore a sale of shares in a LTC will be treated as a sale of the underlying asset therefore possibly triggering depreciation recovery.

Of course, one of the main reasons for putting all of these changes in place is to make the tax system more efficient and less costly.

It seems the more often governments change the rules to make things simpler, the more work it creates for lawyers and accountants!