Ownership Structures

Taxation Factors to Consider

A COMPANY

Advantages

- Possibly easier to transfer ownership if a partner wants to retire, although this is offset by cost of doing a share valuation.

- Limited liability.

- Possible to use imputation system to transfer profits to spouses and children at lower marginal tax rates, only if they have other income.

- Retaining profits in company can reduce ACC levies. However have to watch that saving is not more than offset by UOMI and must also ensure that you do not end up without any ACC cover in the event of an accident.

- Profits can, in some cases, be retained in company and taxed at 28%.

- Look Through Companies (LTC) may offer flexibility with regard to distributing losses.

Disadvantages

- FBT on vehicles - applies to any motor car whether owned, leased, rented etc - exception work related vehicle - some 4WD's qualify but cannot be used privately.

  Any underpayment of FBT very expensive approximately 1/8th of vehicle cost per annum.

- Higher annual accounting cost due to need to comply with Companies Act and Financial Reporting.

- Deemed Dividends Any expenditure (of a private nature) claimed by company and subsequently disallowed by the IRD is effectively taxed twice. e.g., telephone rental, overseas travel, drugs for personal pets.

- Failure to complete company accounts within a specified time can result in a fine to a maximum of $50,000 per director.

- Minority shareholders in a LTC can cancel LTC registration to detriment of majority.

- Companies which derive income from "personal" services may need to distribute up to 80% of profit to the shareholder generating the fees to avoid IRD applying "Penny & Hooper".

- Attribution rules may apply if more than 80% of income comes from the one source.

B TRUSTS

Advantages

- Limited liability, except in regard to IRD for trustees.

Disadvantages

- Complex to administer particularly if Trust operates a trading business.
- Loss of control.
- If Trust only owns plant and leases these to, say, company or partnership, it must charge a commercial lease to avoid arrangement being upset by IRD - this involves a large amount of paper work.

  No problem if Trust only owns building.

  Some taxpayers attempt to overcome problem of leasing plant by having Trust rent a fully furnished building to company/partnership.
- All Trust decisions must be properly documented.
- Increasing risk of discretionary beneficiaries suing the trustees.
- Only really suitable for close family situations.
- Distributions from the trust to minors (children under 16) taxed at 33%.
- IRD don't like trading trusts and tend to put greater audit emphasis on these.

C PARTNERSHIPS

Advantages

- None of the disadvantages of companies and trust.

- Simplicity.

Disadvantages

- Unlimited liability for:

  a) actions of partners - can be overcome to some extent by placing restrictions on a partners ability to contract on behalf of the partnership and requiring two signatures on all cheques;

  b) actions from clients - can be overcome by insurance;

  c) unpaid debts - only a problem if business not profitable.

- Can have serious adverse tax consequences on death of a partner unless great care taken with drafting Will.

- Subject to higher income tax than a company if partners share of income exceeds $48,000.

- Need to be aware of possible impact of Associated Persons rules on land sales if in partnership with persons, whose tax background you are not aware of.