

Greater Wellington Regional Council High-level tax compliance review

*Strictly private
and confidential
September 2016*



This document is a tax advice document and should be kept confidential. It is not required to be disclosed to Inland Revenue. Inland Revenue can request disclosure of "tax contextual information".

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		PAYE	Pay-As-You-Earn Tax
		PwC	PricewaterhouseCoopers
		SOLGM	New Zealand Society of Local Government Managers
		TA	Territorial authority
		WHT	Withholding Tax

1. Executive summary

This report summarises the core findings of the areas covered by this tax compliance review where we consider there to be scope for further improvement and/or where further investigation would potentially be warranted. For completeness, it also briefly summarises the numerous aspects of Council business where the correct tax treatment is being applied, and also comments on matters identified in Council's previous tax compliance report. Overall, Council maintains a high-level of tax compliance, and of the matters identified herein, most represent tax opportunities for Council to consider investigating, as opposed to areas of tax risk.

The findings contained within the report were discussed with the Team Leader Accounting and Strategic Finance Manager at our exit meeting on 10 June 2016. In summary, the principal risk areas are:

- **Insurance proceeds and premiums** – We note Council has been returning GST on all insurance proceeds received. Our review entailed consideration of Aon insurance premium invoices, and we noted that a portion of the premiums are charged by Aon in the United Kingdom do not have a New Zealand GST component. Ordinarily, Council is not required to return GST on insurance proceeds received where GST is not charged on the corresponding insurance premium. In this regard, Council has likely over-returned GST on certain insurance proceeds received.

We recommend that Council undertake a review of all insurance proceeds received over the last four years and quantify the GST output tax over-returned on the receipt of insurance proceeds where no New Zealand GST was charged on the corresponding insurance premium, and consider submitting a voluntary disclosure to Inland Revenue to correct prior GST periods.

- **Overnight allowance paid to Biosecurity staff** – Where Biosecurity staff are required to stay away from home, Council appears to pay a tax-free 'overnight allowance' to compensate the individual for the discomfort and inconvenience suffered by staying in accommodation provided by Council. We understand that these amounts are based on historically negotiated amounts in the collective employment agreements and have incrementally increased over time. It is unclear whether Council has sufficient evidence to support the value of this allowance being a reasonable estimate of actual business expenditure incurred.

We recommend that Council undertakes a valuation-type exercise to consider whether the value of this allowance does represent an estimate of actual business expenditure incurred, and if so, maintain that documentation to support the tax-free payment of this allowance. Alternately, we recommend that Council begin accounting for PAYE on the payment of the overnight allowance, prospectively. Further, Council should quantify the PAYE shortfall over the last four years and consider submitting a voluntary disclosure to Inland Revenue, if appropriate.

- **FBT on trauma insurance and income protection insurance** – Council incorrectly classified trauma insurance as an unclassified fringe benefit for FBT purposes, rather than a ‘classified’ fringe benefit in the FBT return for the quarter ended 31 December 2014; this has likely lead to Council over-returning FBT on unclassified benefits for the quarters ended 31 December 2014 to 30 September 2015. Further, Council is currently returning FBT on the provision of income protection insurance to employees. As this type of insurance is excluded from being a fringe benefit¹, Council has over-returned FBT on the provision of this ‘benefit’ to its employees.

We recommend that Council undertake a quantification exercise to determine the extent to which FBT has been over-returned on unclassified benefits provided to employees in the FBT returns for the quarters ended 31 December 2014 to 30 September 2015, and consider submitting a voluntary disclosure to Inland Revenue to correct prior FBT periods, if appropriate. We also recommend that Council cease returning FBT on its contribution towards the provision of income protection insurance to employees. Further, Council should quantify the FBT over-returned on this ‘benefit’ to date, and consider submitting a voluntary disclosure to Inland Revenue to correct prior FBT period, if appropriate.

The above points are discussed in detail within the ‘Significant matters’ sections below.

Action plan

We include, as **Appendix One**, an action plan for Council to implement/record its decisions on all of the various matters raised in this report. Please note that certain more minor matters identified during the review can also be found in that appendix.

While this four day review cannot be expected to replicate an Inland Revenue investigation exactly, Council should reflect positively on having taken the proactive step of instigating this review and obtaining a clear, independent view of those areas that it should address to facilitate tax compliance.

¹ Provided the receipt of the insurance proceeds is considered taxable income of the employee.

2. *Scope of review*

The scope of our high-level tax compliance review was set out in our proposal dated 2 May 2016. Briefly, the aim of the review was to provide the GM Corporate Services/CFO with a high-level assessment of Council's tax compliance in respect of GST, PAYE, WHT and FBT, and involved:

- Identifying any material instances of non-compliance, drawing on our experience in undertaking compliance reviews across the local government sector;
- Ensuring that Council's current policies and procedures facilitate tax compliance; and
- Enabling Council to demonstrate to Inland Revenue that it has taken reasonable care in managing its taxation affairs.

The initial on-site review was undertaken from 8 June 2016 to 13 June 2016. The approach taken for the review was to interview key staff (as outlined in **Appendix Two**) and examine certain key documentation, together with the tax treatment applied to a variety of transactions undertaken by Council. The documents selected and employees interviewed were based on our knowledge of the current areas of tax on which the Inland Revenue is focusing, and our experience gained from our close involvement with the local government sector, of the problematic issues that can arise.

As agreed, the culmination of the review is the following report, providing an overview of Council compliance with existing tax legislation, our recommendations for policy and process improvements, where appropriate, and our comments on tax opportunities/risks identified.

We would like to convey our appreciation of the assistance and open co-operation provided by Council personnel throughout the course of the review.

3. Significant matters

3.1. Insurance proceeds and premiums

During the 2015 and 2016 financial year Council lodged insurance claims and received the insurance proceeds thereto. We understand that Council returned GST output tax on all insurance proceeds received.

Under the GST legislation:

- GST is required to be returned on the receipt of insurance proceeds where GST has been charged on the insurance premium relating to those insurance proceeds;
- GST is not required to be returned on the receipt of insurance proceeds where GST was not charged on the insurance premium relating to those insurance proceeds; or
- GST is not required to be returned where the insurance proceeds relate to an exempt supply made by Council (eg the insurance proceeds relate to Council's residential rental properties).

Our sample review of the Aon insurance premium invoices indicated that, in many instances, the insurance premium invoices included a portion of the insurance premiums that have been charged by Aon in New Zealand and Aon in the United Kingdom respectively. Council has correctly not claimed GST input tax on the portion of the premium that is charged by Aon in the United Kingdom, as the insurance provider is outside of New Zealand and no GST has been charged.

Our review of the insurance proceeds indicate that, Council has over-returned GST on the insurance proceeds received from Aon. That is, as Council is not required to pay GST output tax on the portion of insurance proceeds that was paid to Council by Aon United Kingdom. Council has a tax opportunity in this regard, as it is likely to be entitled to a refund of GST output tax over-returned on overseas insurance proceeds received.

Recommendation

We recommend that Council undertake a review of all insurance proceeds received over the last four years and quantify the GST over-returned on foreign insurance proceeds that relates to the premiums paid by Council where no GST was charged² and consider submitting a voluntary disclosure to Inland Revenue to correct prior GST periods.

² Eg. to Aon in the United Kingdom, other foreign insurers etc.

3.2. ‘Overnight allowance’ paid to Biosecurity staff

Council has a collective employment agreement with the ‘Central Amalgamated Workers Union and the Public Services Association’. Under this collective employment agreement, Biosecurity staff are entitled to an ‘overnight allowance’ when they are required by Council to stay away from their usual place of residence for work purposes. Further, this allowance is paid by Council in addition to the provision of accommodation and meal allowances/reimbursements, and appears to ‘compensate’ Biosecurity staff for any inconvenience, discomfort and/or additional expenses incurred. There are three categories of allowance that can be paid, each recognising the differing standard of accommodation that may be provided; these being:

- High standard of accommodation - \$32.45 per night.
- Below standard of accommodation - \$36.34 per night.
- Accommodation without basic facilities (i.e. DOC huts) - \$49.33 per night.

Council currently treats this allowance as non-taxable.

Ordinarily, for an allowance to be paid on a tax-free basis, Inland Revenue generally requires there to be a business need and the value thereto should be based on a reasonable estimate of actual business expenditure to be incurred. Importantly, Council *must* hold documentation to support that value as being a reasonable estimate of actual business expenditure incurred.

In this instance, we note that the allowance values are based on amounts historically negotiated in collective employment agreements and have incrementally increased over time. While the original amount *may* have been based on a reasonable estimate of actual expenditure incurred³, it is unclear whether the current value does - this is something that should be re-evaluated on a regular basis. There is a risk that Inland Revenue could consider the allowance currently being paid to the Biosecurity staff is to compensate them for the *level discomfort and inconvenience suffered* as a result of the quality of the accommodation provided by Council⁴.

As such, we consider that, in lieu of supporting documentation, this ‘overnight allowance’ is taxable as there does not appear to be a readily apparent basis to provide the payment on a tax-free basis. If this is the case, then Council will have a PAYE shortfall in relation to the ‘overnight allowances’ paid tax-free over the last four years.

³ Whilst on-site, we were not able to confirm what the original values of the overnight allowance were.

⁴ Which may indeed be the intention of this allowance.

Recommendation

In this first instance, we recommend that Council undertakes a valuation-type exercise to consider whether the value of this allowance does represent an estimate of actual business expenditure incurred, and if so, maintain that documentation to support the tax-free payment of this allowance.

Alternately, we recommend that Council begin accounting for PAYE on the payment of the overnight allowance prospectively. Practically, this may require Council to set up a new taxable allowance code. Further, Council will also need to consider whether to 'gross-up' future payments for PAYE, to ensure the employees receive the same 'after-tax' amount as stated in the collective employment agreement.

We also recommend that Council quantify the value of the PAYE shortfall on the payment of overnight allowance over the last four years, and consider submitting a voluntary disclosure to correct prior PAYE periods, if appropriate.

3.3. FBT on trauma insurance and income protection insurance

Council uses the 'FBT partner' software for the preparation of its FBT returns. 'FBT partner' includes the functionality to determine motor vehicle fringe benefits, and fringe benefits pertaining to the provision of insurances, gifts, etc. to employees; it also tracks the value of unclassified benefits provided against the *de minimis*⁵ threshold. Currently, Council has been returning FBT on all unclassified benefits provided each quarter.

Our review of sample FBT returns indicated that Council has incorrectly categorised trauma insurance as an unclassified fringe benefit for the FBT return for the quarter ended 31 December 2014. Whilst trauma insurance is ordinarily a 'classified' fringe benefit and FBT should be returned accordingly, the incorrect classification of this fringe benefit has potentially lead to Council over-returning FBT on all unclassified benefits provided during the quarters ended 31 December 2014 to 30 September 2015.

Further, we note that Council is also currently returning FBT on the provision of income protection insurance to employees. The ITA specifically outlines that an employer's contribution towards an employee's income protection insurance premium is 'excluded' from being a fringe benefit *provided it is taxable in the hand of the employee*. Returning FBT on the provision of this 'benefit' to employees would currently represent an unnecessary FBT cost to Council. In this regard, Council has over-returned FBT on the provision of income protection insurance to employees.

Recommendation

We recommend that Council ensure that trauma insurance is consistently excluded from being treated as an unclassified fringe benefit, and is treated as a 'classified' fringe benefit. Council should then undertake a quantification exercise to determine the extent to which FBT has been over-returned on unclassified benefits provided to employees in the FBT returns for the quarters ended 31 December 2014 to 30 September 2015, and consider submitting a voluntary disclosure to Inland Revenue to correct prior FBT periods, if appropriate.

We also recommend that Council cease returning FBT on its contribution towards the provision of income protection insurance to employees. Further, Council should quantify the FBT over-returned on this 'benefit' to date, and consider submitting a voluntary disclosure to Inland Revenue to correct prior FBT period, if appropriate.

⁵ Being \$300 per employee per quarter, or \$22,500 for all employees for the current and previous three quarters.

Appendix One - Summary of findings

Area of focus	Our observation	Our recommendation	Action taken by Council
GST			
Insurance proceeds	<p>Council has over-returned GST on certain insurance proceeds received as a portion of the proceeds relate to an insurance premium where no GST was charged.</p> <p>Please refer to 'Section 3.1' for further comments.</p>	<p>Please refer to 'Section 3.1' for further comment.</p>	
Procedural documentation	<p>Council does not have a formalised procedural document for the preparation of Council's GST return.</p> <p>This potentially exposes Council to a key person risk, should the GST return preparer be absent for an extended period of time, or leave the organisation, as there is no covering personnel or documentation to ensure GST returns continue to be filed accurately and on time.</p> <p>This highlights the importance of having a procedural document to enable the continuity of Council's GST compliance. We note this matter was also identified in our previous tax compliance report.</p>	<p>We recommend that Council expedite the development of a formal procedural document. Importantly, it should be detailed enough to enable another member of the Finance team, who has never prepared the GST return, to follow the document to correctly prepare and file the GST return.</p>	

Area of focus	Our observation	Our recommendation	Action taken by Council
Rates in advance	<p>Council collects its rates via a shared invoicing arrangement with a number of TAs in the region, and the TAs also collect the rates on behalf of Council. The TAs advise Council, on a monthly basis, of the value of rates collected during the period.</p> <p>Council returns GST on rates based on the information provided by the TAs. The breakdown provided to Council shows the amount of rates invoiced and the amount of rates received for the period; however, no further breakdown is given regarding how much of the rates were received in advance of an invoice being issued. In this regard, Council does not return GST on rates received in advance.</p> <p>Rates has special GST time of supply rules, but is generally triggered at the earlier of the rates instalment tax invoice being issued or any receipt of payment. Where rates are received in advance of the rates instalment invoice, GST should be accounted for on those 'pre-paid' rates in the GST return in which the payment is made by the ratepayer.</p> <p>While we appreciate Council's reliance on the information provided by the TAs, Council has a time of supply exposure as GST on rates is being returned later than required.</p>	<p>We recommend that Council request that the TAs provide a breakdown of the rates received in advance of an invoice being issued, in addition to the information requested. Council should then ensure GST output tax is also returned on those rates.</p>	

Area of focus	Our observation	Our recommendation	Action taken by Council
Rates on residential properties	<p>Council owns a small number of residential properties across its region. As part of the TA rating process, rates (including its own rates) is charged to its residential properties.</p> <p>Technically, Council cannot make a supply to itself and therefore, should not charge GST to itself on rates in relation to those properties.</p> <p>Whilst Council receives the relevant information to make the GST adjustment, Council does not claim GST on those rates as it relates to an exempt supply for GST purposes.</p>	<p>We recommend that Council include an adjustment in its GST returns to correct this error, prospectively.</p> <p>Further, we recommend that Council quantify the GST over-returned on rates charged on Council-owned residential properties over the last four years⁶ and submit a voluntary disclosure to Inland Revenue to have the over-returned GST refunded with use-of-money-interest.</p>	

⁶ New proposed tax legislation may allow Council to claim back GST output tax on rates charged to Council-owned properties for an additional four-year period.

Area of focus	Our observation	Our recommendation	Action taken by Council
Apportionment on overheads	<p>Council has an agreed GST apportionment methodology with Inland Revenue in relation to overhead costs that relate partially to making exempt supplies (Letter from Inland Revenue dated 5 March 2014).</p> <p>Council is required to undertake a monthly GST adjustment and an annual GST 'wash-up' calculation in June each year to ensure the net amount of GST has been claimed on overhead expenditure for the year. The result of the 'wash-up' will also determine the adjustment for the upcoming year.</p> <p>Council has not adjusted its GST apportionment calculation since the agreed methodology was first agreed, nor has it been completing the annual 'wash-up' calculation.</p> <p>This potentially exposes Council to a GST risk as the incorrect GST apportionment adjustments have been recurring in its GST returns since June 2014.</p>	<p>We recommend that Council:</p> <ul style="list-style-type: none"> • Undertake a re-calculation exercise based on the approved apportionment methodology to determine the appropriate GST adjustments that should have been made. • Council may wish to consider submitting a voluntary disclosure to Inland Revenue, if appropriate; • Incorporate the 'annual wash up' calculation in the GST return procedures and procedural documentation; and • Update the calculation of the apportionment adjustments for the current year based on a renewed 'wash up' calculation and approved apportionment methodology. 	
GST group	<p>As this was a high-level review, from the transactions we reviewed, we observed that Council is correctly returning GST on group income and correctly claiming GST on group expenditure (excluding intragroup transactions).</p>	<p>Council should ensure that it maintains its current practice.</p>	

Area of focus	Our observation	Our recommendation	Action taken by Council
Residential rental income	<p>Jigsaw provides property services to Council. Jigsaw (via Council's finance system) correctly accounts for GST output tax on residential rental income received from mixed-use residential property (i.e. property that is ultimately held for Council's taxable activity, but in the interim, is used for making exempt supplies of residential rental income).</p> <p>When these properties are sold, Council will need to ensure it reviews the GST position of these properties to ensure that it meets the requirements of the SOLGM agreement.</p>	<p>Council should ensure it continues to track the GST adjustments returned, on a per property basis, so that it is able to claim the full value of GST returned when a property's use changes from mixed-use to <i>fully taxable use</i> (eg Council demolishes building to commence flood protection).</p> <p>As a separate piece of work PwC has prepared a property guide for the Hutt River flood protection work. This guide provides more information on the SOLGM agreement.</p>	
Residential property	<p>Council correctly 'blocks' GST from being claimed on expenditure relating to its residential property (i.e. making exempt supplies).</p>	<p>Council should ensure that it maintains its current practice.</p>	
Property sales	<p>Our review of sample Sale and Purchase agreements indicated that Council has correctly accounted for GST on its property disposals.</p>	<p>Council should ensure that it maintains its current practice.</p>	
Property purchases	<p>Council is about to begin its flood protection project, requiring Council to purchase a large number of properties in along the Hutt Riverbank. Council has taken proactive steps to obtain a GST guide from PwC to assist in determining the correct GST treatment of the property transactions.</p> <p>Our review of the first sale and purchase agreement in relation to the flood protection project indicated that Council has correctly accounted for GST on this property purchase.</p>	<p>Council should ensure that it maintains its current practice and seek assistance on non-standard transactions, as required.</p>	

Area of focus	Our observation	Our recommendation	Action taken by Council
Cutting rights	Council received a 10% 'deposit' for the sale of cutting rights. As 'cutting rights' in this instance relate to an interest in land, Council has correctly applied the zero-rating rules to the deposit received.	No action required.	
Train sales (zero-rated)	<p>Council recently sold a tranche of trains to a company in Africa. Council did not return GST on the income as it was treated as a zero-rated supply of exported goods (ordinarily requires export within 28 days).</p> <p>On the basis that Council exported the trains in accordance with the allowable Customs timeframes, Council has correctly accounted for GST on this transaction.</p>	Council should ensure that it declares these sales as zero-rated supplies in Box 6 of the GST return in the month in which these transactions occur.	
Train purchases	<p>Council recently purchased 'new' trains from a supplier in Korea. Given the significant expenditure related to this purchase, we reviewed the transaction from a GST perspective. The invoice received is from a New Zealand entity and has New Zealand GST charged on it.</p> <p>We consider that Council has correctly claimed GST input tax on the purchase of the trains.</p>	Council should ensure it maintains its current practice.	
Staff reimbursements	Council correctly claims GST on staff reimbursements of business expenditure reimbursed through payroll.	Council should ensure it maintains its current practice.	

Area of focus	Our observation	Our recommendation	Action taken by Council
PAYE/WHHT			
Overnight allowance to Biosecurity and Parks staff	<p>Council treats the 'overnight allowance' paid to Biosecurity staff as a non-taxable allowance. It is unclear whether Council has sufficient evidence to support the payment on this allowance on a tax-free basis.</p> <p>Please refer to 'Section 3.2' for further comments.</p>	<p>Please refer to 'Section 3.2' for further comments.</p>	
Porirua property	<p>We understand that Council provides free full time accommodation to one employee who would ordinarily be required to travel a considerable distance to undertake their employment duties in areas near Porirua. Council does not return PAYE on the market value of the accommodation provided.</p> <p>Council has a PAYE exposure as it has not returned PAYE on the provision of this accommodation to this employee.</p>	<p>We recommend that Council reviews the basis upon which the accommodation is provided, and formalise the arrangement. Following this, we recommend that Council determine whether PAYE should be returned.</p> <p>We are happy to assist in this determination if appropriate.</p>	
Payments made under section 123 of the ERA	<p>Council has advised us that there have been no tax-free payments made under section 123 of the ERA since our previous tax compliance review was undertaken in February 2013.</p> <p>We recognise that Council has recently undergone a significant restructure and in such instances we often find tax-free payments under section 123 of the ERA.</p>	<p>We recommend that Council confirm that no such payments have been made in response to Council's significant restructuring.</p> <p>We also recommend that Council remain vigilant to ensure that any future tax-free payments made under section 123 of the ERA in the future are carefully considered to determine whether it is genuine compensation for 'hurt and humiliation suffered' by the employee.</p> <p>Please refer to 'Appendix Three' for comment on Inland Revenue's four criteria in respect of payments made under section 123 of the ERA.</p>	

Area of focus	Our observation	Our recommendation	Action taken by Council
Employee/ contractor distinction	<p>Business Unit managers have discretion to engage individuals, as required. Council utilises the PwC employee-contractor distinction test checklist to ensure appropriate consideration is given to their determination.</p> <p>Council was unable to provide a list of contractors engaged but we note that Human Resources and Procurement teams are in the process of developing a database of contractors⁷.</p> <p>Based on discussions, whilst there may be a risk that 'smaller' contractors may incorrectly be classified, we consider that the overall risk to be relatively low in respect to the large number of contractors engaged.</p>	<p>Council should ensure that as part of the contract engagement project, support should be held for each contractor engaged to support Council's determination.</p>	
Relocation payments	<p>On occasions, Council will contribute towards the cost of an employee relocation.</p> <p>Based on our discussions, we understand that these payments are processed through Accounts Payable as a non-taxable payment, and Council holds appropriate documentation to support the position taken.</p>	<p>Council should ensure that appropriate consideration is given to the Inland Revenue's Relocation Determination (<i>Determination 09/04: Eligible Relocation Expenditure</i>) regarding eligible relocation expenses and relevant expenditure timeframes.</p>	
Ranger accommodation allowance	<p>Certain rangers are afforded discounted accommodation by Council. Council pays a 'grossed-up' allowance, equivalent to the 25% discount 'grossed-up' for PAYE, and takes a 25% deduction after tax.</p> <p>Council is correctly treating the accommodation allowance paid to rangers as a taxable allowance.</p>	<p>Council should ensure that it maintains its current practice.</p>	

⁷ Largely driven due to recent health and safety legislation changes.

Area of focus	Our observation	Our recommendation	Action taken by Council
Superannuation allowance	Council pays a taxable super allowance (up to 3%) for those employees that forgo additional employer superannuation contributions.	Council should ensure that it maintains its current practice.	
Payments of extra pay	Council is correctly treating 'bonus payments', 'cashed-up' annual leave and annual leave on final pay as extra pay, and taxing them at the respective employees' marginal tax rate.	Council should ensure that it maintains its current practice.	
WHT on Commissioners	Council is correctly deducting WHT at the rate of 33% on payments made for services provided by Commissioners, and correctly, does not apply WHT on mileage reimbursements.	Council should ensure that it maintains its current practice.	
NRCT	Council engages with non-resident suppliers to provide services in New Zealand as required (eg TechnologyOne consultants). Council personnel have a good understanding of the NRCT rules, and have resources available ⁸ assist in determining whether NRCT applies.	Council should continue to remain vigilant when engaging non-resident contractors to ensure NRCT is appropriately considered.	

⁸ Eg. NRCT flow chart for payments made to non-resident contractors.

Area of focus	Our observation	Our recommendation	Action taken by Council
FBT			
Trauma insurance	<p>Council incorrectly classified trauma insurance as an unclassified fringe benefit for FBT purposes, rather than a 'classified' fringe benefit; this has likely lead to Council over-returning FBT on unclassified benefits for the quarters ended 31 December 2014 to 30 September 2015.</p> <p>Please refer to 'Section 3.3' for further comments.</p>	<p>Please refer to 'Section 3.3' for further comments.</p>	
Income protection insurance	<p>Council is currently returning FBT on the provision of income protection insurance to employees. As this type of insurance is excluded from being a fringe benefit⁹, Council has over-returned FBT on the provision of this 'benefit' to its employees.</p> <p>Please refer to 'Section 3.3' for further comments.</p>	<p>Please refer to 'Section 3.3' for further comments.</p>	

⁹ Provided the receipt of the insurance proceeds is considered taxable income of the employee.

Area of focus	Our observation	Our recommendation	Action taken by Council
Procedures	<p>Council has a formal procedural document for the preparation of Council's FBT return; however, it currently does not accurately reflect the current process as it has evolved.</p> <p>It is pleasing to see that Council has acted upon our recommendation outlined in our previous tax compliance report to implement a procedural document for the preparation and filing of Council's FBT returns.</p> <p>It is important to ensure that this document is reviewed and kept up to date as processes and/or procedures continue to develop over time.</p>	<p>We recommend that Council update its FBT procedural document to ensure that the document reflects the current procedure for preparing and filing its FBT returns.</p>	
Private use letter	<p>Council allows certain employees the use of a 'work-related motor vehicle'¹⁰. We understand Council does not issue annual 'refresher' letters to all employees reaffirming that private use of those vehicles is prohibited.</p> <p>Inland Revenue would expect such letters to be issued to all employees that drive work-related motor vehicles.</p>	<p>We recommend that Council ensure all employees who are assigned a 'work-related motor vehicle' are issued with an annual 'refresher' letter reaffirming their private use restrictions.</p>	

¹⁰ With such motor vehicle fitting the 'work-related motor vehicle' criteria, and quarterly spot checks being undertaken.

Area of focus	Our observation	Our recommendation	Action taken by Council
Tracking unclassified benefits	<p>Council uses 'FBT partner' for the preparation of its FBT return, which includes the functionality to track the value of unclassified benefits provided against the <i>de minimis</i>¹¹ threshold.</p> <p>We identified one instance¹² where Council has likely over-returned FBT on the provision of unclassified benefits to employees; this being Council FBT return for the quarter ended 31 December 2015.</p> <p>Our manual track of the <i>de minimis</i> threshold outlined that Council did not appear to have breached this threshold as the value of all unclassified benefits provided during that current and previous three quarters did not exceed \$22,500. In this regard, Council has over-returned FBT on unclassified benefits provided to employees during the quarter ended 31 December 2015.</p>	<p>We recommend that Council:</p> <ul style="list-style-type: none"> Consider whether it is appropriate to include a procedure to manually track the <i>de minimis</i> threshold, so as to confirm 'FBT partner's' conclusion. Should cease to return FBT on <i>all</i> unclassified benefits provided in instances where the value of unclassified benefits does not breach the <i>de minimis</i> threshold; and Quantify the FBT over returned on unclassified benefit for those quarters, and consider submitting a voluntary disclosure to Inland Revenue to correct prior FBT periods. 	
Car parks	<p>Council affords use of car parks to certain employees. As these are located on Council premises, they meet the 'on-premises' exemption, and are not subject to FBT.</p>	<p>Council should ensure that it maintains its current practice.</p>	

¹¹ Being \$300 per employee per quarter, or \$22,500 for all employees for the current and previous three quarters.

¹² Other than those referred to in 'Section 3.3 FBT on trauma insurance and income protection insurance' above.

Area of focus	Our observation	Our recommendation	Action taken by Council
Credit cards	<p>Council maintains a policy in relation to the use of Council-issued credit cards which stipulates that no private expenditure is permitted.</p> <p>No FBT implications arise from this arrangement.</p>	<p>Council should ensure that it maintains its current practice.</p>	
Monitoring private use of motor vehicles	<p>Council is undertaking a best practice approach in regards to monitoring the private use of motor vehicles; which involves performing a quarterly and random odometer spot checks and includes this within the FBT return work papers. This information is used to raise queries if there is any private use of the motor vehicle.</p> <p>We note that Council's vehicles are also 'fitted-out' with a sophisticated vehicle monitoring system. Council may wish to explore the use of this functionality for FBT purposes, in the future.</p>	<p>Council should ensure that it maintains its current practice.</p>	

Appendix Two - Key personnel

Person	Title
Mark Ford	Strategic Finance Manager
Shane Mercer	Team Leader Accounting
Shirely Long	Senior Financial Accountant
Neil Wong	Assistant Accountant Corporate
Sarah Colquhoun	Senior Human Resources Advisor
Candi Webb	Senior Payroll & Accounts Officer
Ahmed Rehman	Systems Analyst Human Resources
Kevin Joe	Team Leader Financial Services
Joszef Bognor	Jigsaw Property Consultancy Limited
Tim Penwarden	Jigsaw Property Consultancy Limited
Samantha Gain	Manager, Legal and Procurement

Appendix Three – Inland Revenue requirements for payments made under section 123 of the ERA

Inland Revenue has expressed its view that the following four factors must be present for a tax-free payment made under section 123 of the ERA to be considered genuine.

- **The existence of a personal grievance** – To be genuine compensation for hurt or humiliation suffered, there must first be evidence of a personal grievance being raised by the employee. What constitutes ‘evidence’ is not prescribed, but we would ordinarily expect either a written grievance from the employee or records of the conversation where an employee claimed they had a grievance.
- **Fair and reasonable** – The employee must have a genuine personal grievance that justifies a compensatory payment. The question that must be answered is whether the actions of the employer were fair and reasonable. If the employer acted in a fair and reasonable way; for example, the performance management of the employee (in terms of section 103A of the ERA), there would have been no “*unjustified dismissal*” or “*unjustified actions*” on the part of the employer, and there would be no genuine personal grievance (in terms of sections 103 of the ERA).
- **Quantum** – Inland Revenue will look at whether the quantum of the payment is appropriate to the personal grievance and ‘suffering’ of the individual. Inland Revenue will consider this in light of court awarded amounts, and will want to be satisfied that the hurt and humiliation payment is in addition to, and not substitute for, other statutory entitlements due to the employee.
- **Documentation** – Inland Revenue will consider whether sufficient evidence of hurt or humiliation exists to substantiate a genuine payment under section 123 of the ERA. This is typically where we see the hurt and humiliation payments challenged by Inland Revenue (i.e. there is not enough evidence on file to prove that a payment is genuine).