

Editorial

Welcome to our Xmas Holiday newsletter which is packed with useful information and tips.

In particular the article talking about the E-Myth and the concept of working on your business rather than in your business provides good food for thought at this time of the year, when we perhaps have a few seconds to ponder life whilst lying on a beach in tropical Wellington.

Life is trucking on at Taylor Associates and we are starting to get on top of our workflows and see the benefits of the 'Accountants Toolbox' workflow scheduling system we implemented this year.

We have been continuing our search to find the right people to work for us and earlier this month we welcomed Tala Staples to Taylor Associates. Tala joins us from another accounting firm on the Kapiti coast. You can find out all about Tala under the "our people" section of the website.

Finally from all the team at Taylor Associates we would like to thank you for your business during the year and we wish you and your families a happy and safe holiday period.

Cheers,

Todrick

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Times up!

THE IRD is entitled to reopen your tax returns for four years after the year in which the department has issued you with a notice (called an assessment) showing the amount of tax you have to pay. So long as you have not wilfully understated your income, the department may not go any further back in time.

Tax mistakes can be terribly expensive. Taxpayers may unwittingly understate income or overclaim an expense, genuinely not knowing they are wrong.

The Commissioner is said to be "statute barred" from correcting a mistake, once his time has expired. The public needs this protection of knowing when they are no longer exposed to risk. Years ago a client claimed overseas travelling expenses amounting to \$2000.

The Inland Revenue Department inspected his books. They asked about the travelling expenses. After negotiating, the client and department agreed to a claim of \$800. As it happened, the tax inspector found only one other mistake which favoured the taxpayer and resulted in a refund for a more recent year.

Three years later our client met the tax inspector at a party. He asked why IRD had not claimed the tax on the disallowed travelling expenses. The inspector replied: "By the time we got around to issuing an amended tax assessment notice that claim had become statute barred."

A reminder about work vehicles

IF you have a work related vehicle (one not designed primarily to carry passengers) and need to garage it at home, IRD requires it to be sign written. This must not be detachable and must be easy to read.

Blueprint for small business

HAVE you ever read *The E-myth*, published by HarperCollins Publishers Inc? It is the story of a lady who makes pies. The author, Michael Gerber, has used this to illustrate the life cycle of a typical business, which leads from initial success and concludes in disaster. He then walks his pie maker through the steps to get out of trouble and provides her with a blueprint for her business.

Gerber's methods have universal application. You could apply his techniques to your business. A business is a money-making machine which will work without you having to be present. If it will not run without you, you do not have a business. You are self-employed.

Gerber says a business person has three roles – the entrepreneur (the ideas person); the technician (the lady who makes the pies); and the manager (who organises the business and creates the systems). You need to perform all these roles. If one is missing, the business might get into difficulty.

The book explains it is relatively easy to be the entrepreneur and then make the pies. The new business person has a saleable product and is good at what she does. Her business expands, staff are employed. They make mistakes and things go wrong. In desperation she gets rid of them. Consequently, she has to work long hours. She finds herself trapped in her business. She now sees the business as a disaster.

Gerber says, to avoid this happening become the manager, not just the entrepreneur and the technician. While this will take some work, it is, he says, essential. To become the manager he advises: "Start with a picture of the customer for whom the business is created." Clients often tell us their business is to sell to everybody. We ask them if they really mean they can sell to rich and poor throughout the country. Get a clear picture of your customers and develop smart ways to sell to them. Focus on a precise group.

An electrician made an excellent living out of a dozen manufacturing plants. He worked from nine to five weekdays only.

The manager develops the business strategies. This includes how to get your message to prospective customers – the marketing strategy. There are many techniques. The manager must choose the best.

In 1990 our economy was going through a recession. A young builder had been unemployed for two years. His accountant suggested he approach schools for maintenance work. He developed a strategy and created his own business offering services only to schools. He was most successful. He charged \$20 per hour. In due course he was asked for quotes which he costed at double that rate. They were frequently successful. His customers were a defined group. He acquired a reputation and gathered more customers at no cost. He knew the special needs of schools requiring maintenance work. He became an expert.

"The business must also ... do things in a predictable, uniform way," Gerber says. This means systems. They should be documented as though the business were going to be franchised, the author explains. You will be aiming to employ the person with the least skill possible, as you will have the systems in place for this. Does this sound like McDonald's to you? It should do. Gerber's famous observation is "go to work on your business not in it." I agree.

If you wish to succeed, get off the tools and spend time on developing your business.

TAX TRAPS

Are you paying yourself enough?

TAX case W 33 has become famous in accounting circles.

A dentist was in partnership. He decided to transfer his share of the business into a family trust. In 1996 the trust/business made a profit of \$211,000. His trust paid him a salary of \$80,000. He distributed the balance of the profits to beneficiaries of his trust. Inland Revenue accused him of tax avoidance because the change resulted in him paying a lot less tax.

The judge said his salary was too low. It should have been \$120,000. Apart from that alteration, he let the arrangement stand.

This is what we call a landmark case. The interpretationThere are two calls on your business profit. One is your salary and the other is the return to the business on the money invested in it. This includes the value of the goodwill you have built up and never recorded in the books. For small businesses the return should be quite large as they are relatively more risky than big businesses. If you can establish the salary you pay yourself is a realistic one, the remainder is company or trust profit.

of tax law has been changed. No one expected the judge would allow the dentist to reduce his tax by switching ownership to a trust.

Some people have most of their company shares owned by their family trust. If the business income exceeds \$60,000 they leave some of the profit in the company and pay tax at 33 per cent instead of making it their wages and paying 39 per cent tax. The after-tax profit is passed on to the trust, as a dividend. The trust pays no more tax.

We think Inland Revenue will use this case to challenge inadequate company salaries. The dentist's salary was \$40,000 too low. This equates to a minimum of \$2,400 short paid tax.

Be sure to pay yourself an adequate salary. How much should it be? We think it is the amount you would pay someone else to do your job, including the business administration. You may be able to get an employment agency to help determine this for you. Be sure to keep evidence to support the salary figure, in case IRD ever visits you.

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Speak naturally when advertising

WE were recently handed a copy of a Vodafone business marketing letter. It went to an extreme. The chatty letter had a number of intentional mistakes in it. These were crossed out but left so they could still be read. Often the adjustments were amusing. The letter was personalised. Personalising correspondence is very effective. Try to achieve this. At the bottom there was a PS and also a PPS. Most people pay particular attention to PSs. Use them. The eye travels to them.

The chatty style enticed me to read every word.

Dentist's wisdom

YOU no longer need to shut your eyes when your dentist drills a tooth. A firm of dentists who have installed television screens above their dental chairs to entertain their patients while inflicting their customary pain. We are not saying a dentist who has a television over the chair is any better than one who does not. However, if you want to attract higher prices or new customers, look for innovative ideas. Oscar Wilde said there is one thing worse than people talking about you. It is people not talking about you.

Golly what a price!

"I WAS after a gollywog for my niece," said our intrepid shopper. "I went into Kirkcaldie & Stains in Wellington and found a collector's one for a little over \$100. It has lovely soft furry hair. I am sure my niece will love the feel of it.

"Do you remember that cold snap at the end of August?" she continued. "I timed it beautifully to go and help the Sydney economy. I went into a shop and saw almost the identical gollywog. It was priced at \$262 and that was Australian currency! Don't you think I did well at Kirks?"

Setting a selling price is never easy. Base it on how much you think people are willing to pay. If you are selling into two different markets, so long as you are not likely to damage your business, set different prices. If you are exporting, you may be able to get a better price than locally. The chances of a customer comparing the price in New Zealand with that in Australia are reasonably remote. Would it matter anyway? We hope the New Zealand manufacturer shared in the extra profit!

Golly what a price!

How to Improve your cashflow - Part 2

Some ideas for short-term borrowing.

Bank

Many clients assume they should use hire purchase to buy their vehicles. They keep their bank accounts permanently in credit. If they were to use an overdraft for such purchases and fluctuate in and out of credit they could save significant amounts of interest. Surplus cash in the bank provides a comfortable feeling. However, using your surplus cash costs nothing and interest on the overdraft is a cheap source of money. Avoid using your overdraft to its limit. The unused credit limit is a quick source of cash in emergency.

Creditors

If you are having a temporary cash flow problem, approach a major supplier for some extended credit. If you habitually pay your creditors on time, you are more likely to be trusted with special credit terms. You could ask for 90 days to pay. This extended credit will often be interest free. There's no cheaper source of funds. If you have to forgo a discount, this could be an expensive way of financing. Use it sparingly.

Credit cards

A credit card has the potential to be a quick source of money. It can be useful to handle a surprise ACC or tax bill. The interest rate is high but the loan may be quite short term so the total interest you pay will be small. It is a hassle free source. There are no extra bank fees and it is on demand. See credit card borrowing as your last choice for quick cash. The interest will cost you less than IRD penalties and is tax deductible. Drive up your credit card limit as high as possible in case it is required for that rainy day. Do it now or you will never get round to it. Another way to use your credit card is for business purchases. Provided you pay on time, there is no interest.

How to Improve your cashflow - Part 2 continued.

Life Insurance

It usually takes a few days to arrange a loan on life insurance policies. The interest rate is comparable with the bank and insurance companies do not usually charge a fee. This is another way to finance a vehicle. You can borrow at much lower rates than hire purchase and enter into a similar instalment arrangement for repaying the debt.

Contact Us

Please use the following information to get in touch, should you have any enquiries:

Email enquiries@taylorassoc.co.nz
Web www.taylorassoc.co.nz
Phone 04 384 4161
Fax 04 384 4171