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| **Practice & Past MCQ Quiz Questions:** | **Answer** | **Explanation** |
| Your accounting Firm has employed an intern. The intern is a little confused about the core provisions framework for calculating taxable income (subpart BC ITA 2007). What is the correct formula for calculating taxable income under the core provisions  framework?  A Taxable income = Annual gross income – Annual total deductions –  Available tax loss  B Taxable income = Assessable income – Expenses – Income tax liability  C Taxable income = Cash receipts – Annual total deductions – Available tax loss | **A** | * The formula for calculating taxable income as per the core provisions framework in subpart BC ITA 2007 is: * Taxable income = Annual gross income − Annual total deductions − Available tax loss |
| Mixster Limited (Mixster), a New Zealand tax resident company, has derived royalty income from overseas from which foreign withholding tax has been deducted at its source. You are preparing Mixster’s New Zealand tax return and note that Mixster is in a net loss position  overall. The question arises whether Mixster can claim back the foreign withholding tax that has been withheld from the royalty income when it completes its New Zealand tax return. Which of the following statements are correct?  A As Mixster is in a tax loss position, the foreign tax paid is refundable.  B Mixster cannot claim credits for the tax paid as it was not paid in New Zealand.  C When there is a net loss, the income tax liability will be zero.  D A foreign tax credit is a non-refundable tax credit and, as there is no income tax liability for the year in this case, the tax credit is extinguished. | **C & D** | Under the Part B core provisions of ITA 2007, and particularly s. BC 6 ITA 2007, where a taxpayer’s calculated income tax liability is negative or zero, their  income tax liability for the year is zero. In other words, as there is a net loss, there is no income tax liability.  Section BC 8(1) ITA 2007 (use of tax credits to satisfy an income tax liability) refers us to Part L ITA 2007, which determines the order in which the credits  may be used. A foreign tax credit must be offset first before other tax credits. To the extent that a foreign tax credit cannot be used (i.e. there is no income  tax liability), it is a non-refundable tax credit and is extinguished under s. LA 5 ITA 2007. |
| Bill is a university student and member of the New Zealand Army Reserve. He currently lives at home and has borrowed money to acquire shares in NZ Power Co. Limited (NZ Power Co). His parents also give him some financial assistance. In preparing Bill’s income tax return, he provides you with the following information:  With reference to subpart BC ITA 2007,    With reference to subpart BC ITA 2007, what is Bill’s taxable income?  A $11,600.  B $11,500.  C $14,300.  D $12,000. | **A** | Bill’s taxable income is $11,600, calculated as:    Expenses incurred to derive employment or exempt income are not deductible under the employment (s. DA 2(4)) and exempt income (s. DA 2(3)) limitations respectively. The interest on money borrowed to derive assessable dividends is deductible under s. DB 6 ITA 2007, as the general permission is satisfied and none of the limitations apply. |
| In relation to whether expenses are revenue or capital expenditure, which of the following guiding principles is discussed in BP Australia Ltd v. FCT? Choose the correct response.  A An item of expenditure will not be deductible if it was incurred before the income-earning process commenced.  B The fact that expenditure is not payable until a future date does not destroy its nature as an existing obligation.  C Whether an amount of expenditure is revenue or capital will be determined by considering all the circumstances surrounding the expenditure.  D Classifying expenditure as capital or revenue is about ‘identifying the thing which satisfies a particular notion’. | **C** | In BP Australia Ltd v. FCT, the issue was whether certain sums expended in BP  Australia Limited’s business of marketing petrol were revenue or capital expenditure. Lord Pearce said (at para. 29): The solution to the problem is not to be found by any rigid test or description. It has to be derived from many aspects of the whole set of circumstances some of which may point in one direction, some in the other. One consideration may point so clearly that it dominates the other and vaguer indications in the contrary direction. It is a common sense appreciation of all the guiding features  which must provide the ultimate answer. Although the categories of capital and  income expenditure are distinct and easily ascertainable in obvious cases that  lie far from the boundary, the line of distinction is often hard to draw in border line cases and con􀃒icting considerations may produce a situation where the answer turns on questions of emphasis and degree. |
| Joanne owns the corner dairy and paid for a number of expenses from the business bank account. Which of the following expenses will be deductible for business purposes?  A Purchase of a PlayStation for her son to keep him entertained while Joanne is working at the dairy.  B Advertising for new staff after one of her employees had resigned.  C Sunglasses to wear while driving to and from the dairy.  D Running shoes to wear in the shop. | **B** | Only the advertising for new staff is connected with the dairy. There is a clear nexus between expenditure and the income earned under s. DA 1. All of the other items of expenditure are personal in nature and will be treated as drawings. Private expenditure will not be deductible as it will not meet the general permission test pursuant to s. DA 2(2). |
| With reference to s. DB 31 and Inland Revenue Public Ruling BR Pub 05/01, which of the following scenarios could give rise to a bad debt deduction for the income year ended 31 March 2020?  A On 31 December 2019, the accountant for Flute Limited (Flute) recorded a journal entry to create a bad debt provision of $20,000 for invoices outstanding from a customer that had gone into liquidation. By March 2020, the accountant reviewed the bad debt provision and decided that the amount is irrecoverable and so wrote  of the bad debt.  B A $500 debt is owed to Trombone Limited (Trombone). The amount has been outstanding for one year. Trombone has sent out numerous reminder letters and repeatedly telephoned the debtor. The amount is considered too small to justify the cost of legal action. Trombone writes o􀃖 the debt in its accounting software on 30 March 2020.  C Trumpet Limited makes a provision in its accounts for doubtful debts as at 31 March 2020. The company calculates this provision by estimating a percentage based on past history and applying that percentage to the total amount of debts owed to the business at balance date.  D In May 2020, the accountant for Bassoon Limited (Bassoon) reviews the company’s outstanding debtors as at 31 March 2020 and finds there is a debt that has been outstanding for more than 90 days. He passes this information on to Bassoon’s tax advisors who will prepare its tax return. | **A & B** | Flute's scenario is correct because it is reasonable to assume that a company in  liquidation will not pay its debts. In addition to the debt being bad, it must also be actually written of in the 2020 income year. The bad debt is deductible in the income year ending 31 March 2020 because the debt was written o􀃖 in  March 2020. Trombone's scenario is also correct, as when outstanding amounts are small, a  reasonably prudent commercial person is likely to make limited enquiries and take limited recovery action. Given the sum involved, the length of time it has been outstanding and the steps already taken, it is not unreasonable to draw the conclusion that the debt will not be paid, even if any or further recovery action is taken. The debt was written o􀃖 in the 2020 income year and so may be taken as a deduction in the year ended 31 March 2020. Trumpet's scenario is not a bad debt as it must be an individually identifiable debt that is unlikely to be recovered (in practical terms). The provision for doubtful debts is merely an estimate of the amount that may become bad debt in the future. In Bassoon's scenario, it is not clear that the debt is ‘bad’ and therefore that a deduction is allowed. The mere fact that it has been outstanding for 90 days is  not in itself enough to suggest that the debt is bad. A debt becomes ‘bad’ when a reasonably prudent commercial person would conclude that there is no reasonable likelihood that the debt will be paid. In addition, the debt must be written of as bad in the income year. Merely providing a list of bad debts is not sufficient, as no action has been taken in either the debtors ledger or the  double-entry accounts to physically write this debt off. |
| Bad Luck Limited (Bad Luck) has prepared its financial statements for the year ended 31 March 2020. This is Bad Luck’s first year of operation. Its net profit before tax is $150,000. A tax adjustment(s) may be required for the following items which have been included in the financial statements.  $17,000 for accrued long service leave, of which $5,000 was taken in April and May 2020.  An $8,000 provision for a possible redundancy that may occur before 30 September 2020.  A $20,000 expenditure in relation to an insurance contract that runs from 1 January 2020 until 31 December 2020.  Entertainment expenditure of $15,000 related to staff that attended an overseas conference in February 2020.  What is Bad Luck’s taxable income for the income year?  A $197,000.  B $185,000.  C $212,000.  D $220,000. | **B** | The taxable income of Bad Luck for the income year is $185,000, which is calculated as:    For the accrued long service leave the company chooses not to apply s. EA 4(1) (b)(ib) and treats $5,000 taken in April and May 2020 as deductible. The portion of the insurance that is unexpired for tax purposes is the nine-month  period that runs from 1 April 2020 to 31 December 2020. This amount of $15,000 must be added back to the net pro􀃑t before tax. Determination E12 does not apply as the total expenditure exceeds $12,000. The entertainment expenditure is not subject to the limitation rule because the entertainment was enjoyed outside of New Zealand (pursuant to s. DD 7). Therefore, the full deduction can be taken and no adjustment is required. |
| Which of the following expenses will be deductible to Barry, who has just completed his first year of trading as a baker?]  A Bulk purchase of ingredients for the bakery.  B Demographic information on the immediate surrounding area received prior to entering into a lease for his bakery premises.  C Tax return preparation fees charged by his accountant.  D Electricity costs for his bakery premises. | **A, C & D** | The purchase of ingredients for the bakery and electricity costs for the premises are deductible expenses as these are costs incurred in deriving  assessable income. There is a clear nexus between expenditure and the income earned under s. DA 1(1)(a)(i). Tax return preparation fees will be deductible under s. DB 3(1)(a). The demographic information is not a deductible expense as this was incurred before Barry’s business had commenced. There is no direct nexus to the income earning activity and, therefore, the general permission under s. DA 1(1) (a)(i) is not met. Business related expenses are only deductible under s. DA 1(1) (b)(i) where a business activity is being undertaken (refer to CIR v. Banks). Accordingly, ‘start-up’ costs or preparatory costs are not deductible as the business has not yet commenced. |
| Austin has set up his own accounting practice and wants to become a tax agent. He researches the rules about becoming and acting as a tax agent. Which of the following statements are accurate regarding the rules around becoming or acting as a tax agent?  A Inland Revenue (IR) will discuss a taxpayer’s affairs only with the taxpayer or the tax agent who has been appointed to act on behalf of that taxpayer.  B Anyone who completes a tax return on behalf of another person can become a tax agent.  C A person may be a tax agent if they prepare returns of income that are required to be completed and filed for 10 or more taxpayers, and satisfy other criteria.  D If a taxpayer uses a tax agent, they will not have to pay any short fall penalties. | **A & C** | A person may be a tax agent if they prepare returns of income that are required to be completed and filed for 10 or more tax payers, and they are: A practitioner carrying on a professional public practice; or A person carrying on a business or occupation in which annual returns of income are prepared; or The Maori Trustee (s. 34B(2) TAA 1994). A taxpayer who uses a tax agent may benefit only from a reduction in certain shortfall penalties (s. 141A(2B) TAA 1994). IR will discuss a taxpayer’s affairs only with the taxpayer or the tax agent who has been appointed to act on behalf of that taxpayer (s. 81(4)(l) TAA1994). |
| Lawrence has entered into a tax avoidance arrangement, and has been issued with an assessment for an additional tax liability of $60,000. His total tax figure for the income year was $300,000. He asks you what additional payments, including penalties, he might be liable to pay in respect of this assessment. Which of the following additional payments or penalties could Lawrence be liable to pay?  A 100% shortfall penalty for taking an abusive tax position.  B 20% shortfall penalty for taking an unacceptable tax position.  C 150% shortfall penalty for tax evasion.  D Use of money interest. | **A, B & D** | A tax shortfall will be liable for use of money interest (Part 7 TAA1994). The 20% shortfall penalty for taking an unacceptable tax position (s.141B TAA 1994) could be applied to a case of tax avoidance, as could the 100% shortfall penalty for taking an abusive tax position (s. 141DTAA 1994). The tax shortfall exceeds both the $50,000 threshold and 1% of the total tax figure for the ‘unacceptable tax position’ under s. 141B(2),so the penalty may be applied. The standard for applying the abusive tax position penalty is higher than merely having entered into a tax avoidance arrangement. A person is considered to have entered into a tax avoidance arrangement if the purpose or effect of avoiding tax is more than merely incidental. The abusive tax position penalty applies when a taxpayer has entered into an arrangement or interpreted or applied tax laws with a dominant purpose of taking tax positions that reduce or remove tax liabilities or give tax benefits (s. 141D(1) TAA 1994). Tax avoidance is not the same as tax evasion, and therefore the150% shortfall penalty for tax evasion will not apply. The penalties are not cumulative, so only one penalty would apply. |
| Donnie operates a small business that is registered for GST on an invoice basis, returning GST every six months. He has calculated that in the six months ending September 2019 he will be entitled to input tax credits of $10,000, while his output tax liability will be $20,000. The output tax liability will result from a single invoice to his only customer. In the normal course of events, Donnie would issue this invoice on 30 September2019 and would receive payment in 10 working days Donnie is short of cash, so he decides to delay issuing the invoice until 1 October2019. As a result, Donnie will receive a net GST refund of $10,000 for the six months ending September2019, instead of making a net GST payment of $10,000. Is the following statement true or false? Delaying the issue of the invoice so that he receives a GST refund rather than making a GST payment for the six months ending 30 September 2019 constitutes tax avoidance by Donnie.  A True  B False | **A** | The statement is true. Section 76 GSTA 1985 provides that ‘tax avoidance’ includes ‘a postponement in the liability of a registered person to pay tax’. By issuing the invoice later than he normally would, Donnie has postponed his liability to pay tax, as he will return the output tax arising from that invoice in the GST return for the six months ending31 March 2020, rather than in the GST return for the six month sending 30 September 2019. |
| Which of the following arrangements constitute tax avoidance?  A A registered person generates invoices for transactions that do not exist in order to claim a GST input tax credit.  B An individual invests in residential property with the intention of making a long-term capital gain, rather than investing in shares that will yield a dividend income, because the individual believes that the capital gain will not be taxable, whereas dividend income will be taxable.  C An employer uses PAYE tax deducted from employees’ salaries for one month to pay trade creditors, and does not 􀃑le the employer monthly schedule for that month with IR.  D A vendor of software artificially inflates the value of the software, and provides interest-free financing to a purchaser of the software, so that the purchaser can obtain a large GST input tax deduction upon the purchase of the software.  E A taxpayer participates in a scheme that enables them to make an upfront investment in a company of $1,000, and to be allocated tax losses from that company of $10,000 per annum for the next five years. | **D & E** | Choosing to invest in property rather than shares, on the assumption that the income earned would be taxed at a lower rate, is not tax avoidance. It is reasonable to conclude that using the particular legislative provisions that apply to the taxation of income from investing in property in this way would have been contemplated by Parliament at the time the legislation was enacted. A scheme in which a taxpayer makes a small upfront payment in exchange for being allocated a large loss in order to reduce their taxable income and a scheme that involves inflating the price of software to enable the purchaser of the software to claim a large input tax deduction would both meet the definition of tax avoidance in s. BG ITA 2007, as confirmed by the Supreme Court decision in Ben Nevis v. CIR, and by the Commissioner’s interpretation of s. BG 1 in IS13/01. The act of generating false invoices and the act of taking employees’ PAYE deductions would both constitute tax evasion under s. 143BTAA 1994. |
| Daisy has received a letter from her tax advisor, Jessica, advising her that a scheme she invested in is a tax avoidance arrangement. She will have a number of years' income tax returns reassessed, which will probably result in a substantial payment of income tax (as well as penalties and interest charges). Daisy didn’t take any legal or financial advice before investing in the scheme.  Daisy tells Jessica that she didn’t know any of the details of the scheme and that she had no idea that it was a tax avoidance arrangement. Is the following statement true or false?  The fact that Daisy did not know she was a party to a tax avoidance scheme may enable her to reduce the amount of tax she has to pay.  A True  B False | **B** | The statement is false. The Commissioner has broad powers to reconstruct an arrangement under s. GA 1 ITA 2007, including the ability to adjust the tax able income of any ‘person affected’ by the arrangement. A taxpayer maybe a ‘person affected’ even though they are not a party to the particular arrangement, or have no knowledge of the tax benefits of the arrangement (Ben Nevis v. CIR, BNZ Investments v. CIR (2001), Peterson v. CIR). |
| When a taxpayer is dissatisfied with the Commissioner’s assessment following the Part 4A dispute process, in which judicial bodies can they challenge that assessment?  A The High Court.  B The Court of Appeal.  C The District Court.  D The Taxation Review Authority. | **A & D** | A taxpayer can challenge an assessment by commencing proceedings in a ‘hearing authority’, which is defined in s. 3 TAA 1994to mean either the Taxation Review Authority or the High Court. |
| On which matters does the taxpayer have the burden of proof when a tax dispute under Part 8A is before a hearing authority?  A The shortfall penalty for evasion.  B All shortfall penalties other than evasion or similar acts.  C All matters relevant to the taxpayer’s liability.  D Deductions that have been disallowed. | **B, C & D** | Under s. 149A(2) TAA 1994, the onus of proof in civil proceedings depends on the nature of the proceedings. Where the proceedings relate to evasion or similar acts to which s. 141E applies, or relate to obstruction, the burden of proof rests with the Commissioner. On any other matter, the burden of proof rests with the taxpayer. |
| Kevin bought a section of land in Waipu. He acquired the land for the dual purposes of deriving rental income from it, and disposing of it at a future time. If Kevin’s dominant purpose in acquiring the land was to obtain rental income, will taxable income arise for him under s. CB 6 ITA 2007 when he eventually disposes of it?  A No, taxable income will not arise.  B Yes, taxable income will arise.  C There is not enough information to determine whether any taxable income will arise. | **B** | The proceeds from the disposal of the land will be taxable under s. CB 6 if one of the purposes or intentions of the person who acquired he land was to dispose of it. Unlike s. CB 4 (applicable to personal property acquired for the purpose of disposal), s. CB 6 applies even when this purpose or intention is not the dominant one. Accordingly, as Kevin acquired the land with the purpose of disposing of it (albeit not his dominant purpose), s. CB 6 will apply. |
| Fred is a natural person who carries on a land development business. He acquired a large section of land on 31 March 2012 for the purpose of developing the land and selling it in the course of his business. He develops the land on 1August 2012 but later decides not to sell the land and instead retain it for some other purpose.  Which statement is true about the application of the ten-year sale rule in relation to any subsequent disposal of the land?  A Fred will pay tax on any sale of the land before 2 August 2022 under s. CB 10.  B If Fred ceases his development business then sells the land, he will not be liable to tax under ss CB 7 and CB 10 regardless of how long he has owned it.  C Tax will be payable on the sale of land regardless of when it is sold under s. CB 7. | **C** | Because the land was purchased for the purpose of Fred’s development business, any subsequent gain from disposal of the land will be taxable under s. CB 7 regardless of when the land is sold.  The 10 year rule under s. CB 10 runs from the date of acquisition of the land, not the date the land was developed. The proceeds of sale will only be taxable if disposed of before1 April 2022 under s. CB 10 – as this is 10 years after the date of acquisition.  Sections CB 7 and CB 10 will apply if the development business is carried on at the time the land is acquired. Ceasing the business at a later point in time will not impact the application of those sections. |
| John is a builder (i.e. a person who carries on a business of erecting buildings)who acquired a section of land on 31 March 2016 for reasons other than for the purpose of his business. He began building a house on that land on 1 June 2016,which he completed on 20 January 2017. What is the earliest time at which John can sell his land without taxable income arising for him under s. CB 11 ITA 2007?  A 1 April 2026.  B Tax is always payable under s. CB 11, therefore it does not matter when John sells his land.  C Tax is not payable under s. CB 11, therefore John can sell his land at any time.  D 21 January 2027. | **D** | Section CB 11(1) applies as John is in the business of erecting buildings at the time he began making improvements to the land. However, Section CB 11 will apply only if John sells the land within 10years of completing the improvements. As John completed the improvements on 20 January 2017, he must wait until 10 years have elapsed (i.e. 21 January 2027) before he can sell his land without s. CB 11 applying. |
| Graham and Kate are a married couple, and are getting divorced. As part of the relationship property settlement, Kate and Graham have agreed that Kate will transfer her house to Graham. Kate purchased the house in December 2012 for$600,000. At the date of its transfer to Graham (January 2018), the house has a market value of $1 million. For tax purposes, when will Graham be deemed to acquire the house, and at what value?  A Graham will be deemed to have acquired the house in January2018 for $600,000.  B Graham will be deemed to have acquired the house in January2018 for $1,000,000.  C Graham will be deemed to have acquired the house in December2012 for $1,000,000.  D Graham will be deemed to have acquired the house in December2012 for $600,000. | **D** | Section FB 3 applies in situations where land is transferred on a settlement of relationship property (includes divorce). Under s. FB 3, Graham will be deemed to have acquired the house on the date that Kate acquired it (December 2012), at a value equal |
| Mary is the sole trustee of the Olive Trust. Bill is the sole trustee of the Oil Trust. The settlor of both the Olive Trust and Oil Trust is James. Are Mary and Bill (as trustees of their respective trusts) associated persons?  A There is not enough information to determine whether Mary and Bill are associated persons.  B No, Mary and Bill are not associated persons.  C Yes, Mary and Bill are associated persons. | **C** | Under s. YB 7, the trustees of two separate trusts are deemed to be associated where both trusts have the same settlor. Because James is the settlor of both the Olive Trust and the Oil Trust, the trustees of each trust (i.e. Mary and Bill) are associated persons. |
| Rebecca has a 30% shareholding in Watch Limited, and is also the settlor of the Phone Trust. Will Watch Limited and Melissa (a trustee of the Phone Trust) be associated persons for the purposes of the land tax ?  A Yes, Watch Limited and Melissa are associated persons.  B No, Watch Limited and Melissa are not associated persons.  C There is not enough information to determine whether Watch Limited and Melissa are associated persons. | **A** | Rebecca will be associated with Melissa under the Trustee and Settlor test in s. YB 8. Rebecca will also be associated with Watch Limited under the person/company test in s. YB 3 due to her 30%shareholding exceeding the 25% threshold. Section YB 3(3) states that when two people are related under s. YB 8(or the other listed provisions in that section), the two people are deemed to hold each other’s shares. This means that Melissa will be deemed to hold Rebecca’s 30% shareholding in Watch Limited, and so therefore Melissa will be associated with Watch Limited under the person/company test. |
| A chocolate importer has a large quantity of obsolete stock, which has a market value of approximately 10% of cost. The importer gifts this obsolete stock to a regular wholesale customer after performing an annual cleanout of its warehouse. This is a one-off transaction, outside the ordinary course of business. The customer subsequently sells the stock at a factory outlet. What will be the result of the gift transaction?  A The wholesaler having taxable income of the cost of the item, and the importer being allowed a deduction for the cost of the item.  B A deemed disposal and acquisition at the lower of cost and market value.  C A deemed disposal and acquisition at market value.  D The wholesaler including a $nil amount in assessable income and the importer’s deduction being $nil. | **C** | The gift is a disposal outside the ordinary course of business. Accordingly, the taxpayer is required to bring to account, as assessable income, the market value of the items at the date of disposal, in accordance with s CB 2(3). Even if this was a disposal in the ordinary course of business, s GC 1 would still require market value to apply to the disposal, as the stock was disposed of for inadequate consideration. |
| Jade Limited (Jade) provides you with information relating to its trading stock for the 2020 income year. Jade is not a low-turnover taxpayer and all figures are GST-exclusive. Jade valued its trading stock at cost in all prior income years, and has continued to do so in its financial statements. No changes have been made to the relevant Accounting Standards recently.    Which of the following statements is true in relation to how Jade should value its closing stock for the 2020 income year?  A It does not matter how the 2019 closing stock is valued, as it does nota effect the taxable income in the 2020 income year.  B Closing stock should be valued at its replacement value.  C Closing stock should be valued at its market selling value.  D Closing stock should be valued at cost price. | **C** | As the marketing selling value is below cost, s. EB 11 applies. Jade should value trading stock at market selling value. The discounted selling price and replacement value methods are not available as they were not used to value trading stock in the financial statements under s. EB 9(1) and s. EB 10(1). |
| According to s. EB 2, which of the following items would satisfy the definition of‘ trading stock’?  A Cars sold by a car dealer.  B A guard dog for a petrol station.  C Gravel belonging to a road-making contractor.  D Fuel, oil and machine replacement parts stored by a manufacturer for use in its manufacturing process. | **A** | The definition of ‘trading stock’ in s. EB 2 includes anything acquired for the purpose of sale or exchange in the ordinary course of business. |
| Sparkle Limited (Sparkle) is a company that runs children’s parties. As a side business it sold party supplies. In April 2019, Sparkle sold the party supply business to Fairy Shoppe Limited (Fairy Shoppe), an unrelated company. At 31March 2019, Sparkle held trading stock that it valued at cost for tax purpose sunder s. EB 6. The trading stock cost $150,000 and had a market value of$200,000. Sparkle sold the entire party supply business for $300,000. Included within the sale price were a website used to sell party supplies, plus various fixed assets and advertising materials. Sparkle also assigned to the Fairy Shoppe the leases it held over the warehouse and office space. No apportionment was made in the sale and purchase agreement for any of the individual items Sparkle sold to Fairy Shoppe. Assume that Sparkle is not a low-turnover trader for the purposes of the trading stock rules. Disregard any income tax consequences of the sale other than those relating to trading stock. What are the tax consequences for Sparkle in relation to the sale of the trading stock for the income year ended 31 March 2020?  A Section EB 24 deems the trading stock to be disposed of at market value, and $50,000 is included in Sparkle’s assessable income.  B Section EB 5 applies, and both Sparkle and the Fairy Shoppe can choose how to value the trading stock.  C Section EB 6 deems the trading stock to be disposed of at cost, and the sale does not result in any assessable income to Sparkle.  D Section EB 24 deems the trading stock to be disposed of at market value, and a tax loss of $50,000 to Sparkle would result. | **A** | Section EB 24 applies. When a person sells trading stock together with other assets of a business to another person, the total amount received for the sale must be apportioned between the trading stock and the other assets to reflect the market value of all the assets. Therefore, the trading stock will be deemed to be disposed of for$200,000. As the opening trading stock was valued at $150,000, this results in Sparkle deriving assessable income of $50,000 from the sale of trading stock in the 2020 income year. |
| Jasper Limited (Jasper) provides you with information in relation to its trading stock for the 2020 income year. Jasper is not a low-turnover trader and all figures are GST-exclusive.  Jasper notes that it has paid for $20,000 worth of trading stock that was not delivered until April 2020 and has included this amount within total purchases and closing stock in the below figures.    What will be Jasper’s taxable income for the 2020 income year?  A $272,000.  B $148,000.  C $128,000.  D $292,000. | **C** | Jasper’s taxable income is $128,000. The taxable income calculation applies the trading stock rules. Sales are recorded as assessable income (they are a disposal in the ordinary course of business), and purchases are recorded as a deduction. Jasper can take a deduction for trading stock purchases paid for during the income year but not received by balance date. The combination of the deduction for opening stock and the income recorded for closing stock results in a further deduction, as opening stock is greater than closing stock. |
| Andrew owns Big Tractors Limited (BTL), and as he is approaching retirement he has started to wind down the business. Although he had turnover of $5 million in the 2019 income year, at the end of the 2020 income year he has reduced the turnover to only $2 million. Andrew asks you if this will change the way he values his trading stock. Which of the following valuation methods can BTL use to value its trading stock for the 2020 income year?  A The low-turnover valuation methods in ss EB 13–EB 22.  B The standard valuation methods in ss EB 6–EB 12.  C Any of the valuation methods in ss EB 6–EB 22. | **C** | Section EB 13 provides that a low-turnover trader may value their trading stock by using either the standard valuation methods in ss EB 6–EB 12, or by using the low-turnover valuation methods in ss EB13–EB 22. A low-turnover trader is one that has a turnover of no greater than $3 million. As BTL has a turnover during the 2020income year of $2 million, it has the option of using any of the valuation methods specified in ss EB 6–EB 22. |
| Andrew, the owner of Big Tractors Limited (BTL), is retiring and is winding down the business. By the middle of the 2020 income year BTL has sold almost all it stranding stock, and has only one tractor left in the showroom. BTL bought the tractor for $55,000 and it has a market value of $80,000. Andrew has decided that he wants to retire to his lifestyle block in Queenstown and will take the tractor with him, to use in managing the gorse on the property. On 10 February 2020 he takes possession of the tractor by driving it to his home. Andrew has had some experience of taking trading stock from his business before, so he knows that this is treated as a disposal by BTL to himself, but doesn’t know how much income BTL is deemed to have received for the tractor. Disregarding the deduction that BTL would have received when it bought the tractor, how much income is BTL deemed to receive on transferring the tractor to Andrew?  A $55,000.  B $80,000.  C Nil. | **B** | When Andrew, as a business owner, takes trading stock for private use, this is treated as the sale of the stock at market value under ss CD 6, FC 1 and FC 2. The market value of the tractor is $80,000;therefore, BTL is deemed to have received $80,000 for the deemed sale of the tractor to Andrew. |
| Pete owns a golf equipment retail business. During the income year, Pete purchased golf clubs sets for trading stock with a cost of $600 per set. The retail value is $1,900 per set. Pete records the sets as trading stock then later in the year decides to use one set from his trading stock as a shop demonstration set. Pete no longer intends to sell this set in the ordinary course of his business and intends to use the clubs as an asset in the business for the long-term. What is the tax implication of the transaction in relation to the disposal of trading stock?  A Net income of $1,300 arises.  B Net loss of $600 occurs.  C Net income of $1,900 arises.  D Net loss of $1,300 occurs. | **A** | The golf clubs no longer meet the definition of ‘trading stock’ in s EB2 as Pete no longer has the purpose of selling the set of clubs in the ordinary course of business. If Pete’s use of the clubs as a demonstration set was a temporary measure, with the purpose of selling the demonstration set at a later time (at a discounted price),the set would still be considered ‘trading stock’. As the set of clubs are no longer ‘trading stock’, there has been a disposal of the set of clubs in the ordinary course of business, which will be income under s CB 1. As no consideration was paid, the disposal is deemed to have been made at market value(s GC 1). Net income to Pete of $1,300 arises from this disposal ($1,900 market value less $600 cost). |
| Sally & Co Limited (Sally & Co) is a New Zealand tax resident company that produces beaded jewellery for sale online and at local markets and fairs. In the year to 31 March 2020 Sally & Co made sales totalling $56,000. At 1 April 2019,Sally & Co had jewellery on hand that had a cost of $5,000 and a market value of$5,500. Due to a slow summer trade, the cost of the stock at 31 March 2020 was$8,000, which had a market value of $7,000. Which of the following amounts should be used by Sally & Co as their closing stock value for the year ended 31 March 2020, in order to minimise its taxable income?  A $8,000  B $5,500  C $5,000  D $7,000 | **C** | Sally & Co is a low turn-over trader because its annual turnover is less than $1.3 million, and the value of its trading stock is reasonably estimated to be below $10,000. Therefore, the closing stock can be valued at its opening value for tax purposes (s. EB 23). In this case, the use of the concession minimises Sally & Co’s taxable income. |
| Fabulous Frenzy Limited (FFL) is a New Zealand tax resident company operating a small gift shop in Auckland. The sole shareholder is Hayden, and he is responsible for calculating the stock values for FFL. Which of the below items should be included in the calculation of trading stock on hand for FFL at 31 March 2020?  1. Gift wrap and ribbon used by the staff members to wrap purchases at the request of customers.  2. Stock that Hayden ordered on 15 March 2020 that was in transit to the store at year end.  3. Stock placed in the store on consignment by a local supplier. If the stock does not sell it will be returned to the supplier.  4. Plants purchased from a local nursery that Hayden sells along with decorative pots.  A 1, 3 and 4.  B 2 and 4.  C 1, 2 and 3.  D 1, 2, 3 and 4. | **B** | 1. Gift wrap should not be included in trading stock where it is not part of the product sold, as it is considered a consumable aid and therefore excluded from the definition of trading stock under s. EB 2.  2. Where stock has not been delivered by balance date, but it would have been treated as trading stock if it had been delivered by balance date, the stock is included within stock on hand at balance date (s. EB 2(2)(c)).  3. The consignment stock remains the property of the supplier until it is sold, therefore it is not the property of FFL and should not be included within stock on hand.  4. Plants held in pots are classified as items of trading stock under Case T1. |
| Cloudy Breweries Limited (Cloudy) acquires the following equipment on 4November 2019:  50 kegs costing $2,500 ($50 each).  30 barrels costing $7,500 ($250 each).  2 stainless steel bins costing $10,100 ($5,050 each).  All amounts shown are GST-exclusive, and Cloudy would like to minimise compliance costs for these assets by using the pool method where possible. Cloudy is GST-registered and has a 31 March balance date. Which is the best option for Cloudy to both minimise compliance costs and maximise the depreciation loss calculation?  A Set up three separate pools for each category of asset.  B Depreciate all assets individually using the diminishing value (DV) method.  C Set up two pools – one each for the kegs and barrels, and depreciate the stainless steel bins outside of the pool method.  D Set up one pool for the kegs and barrels, and depreciate the stainless steel bins outside of the pool method. | **C** | The best option for Cloudy is setting up two pools, one each for kegs and barrels. The pool method can only be used for the kegs and barrels as the individual cost of the stainless steel bins is greater than the maximum pooling value of $5,000. Also, by setting up two separate pools, each pool would use its own depreciation rate (20%DV and 40% DV respectively); however, if they were put into one pool, the lower rate of 20% DV must be used across that one pool. Depreciating all assets individually using the DV method is not the best option for Cloudy due to the high compliance cost of individually tracking and accounting for each item. |
| Beta Fission Limited (Beta) is a manufacturer. On 1 June 2019, Beta sold its building to an unrelated party for $610,000. The building cost $750,000, with an adjusted tax value of $615,000 at 1 April 2019. Its market value on 1 April 2019was $620,000. The building has steel framing and an estimated useful life of 50years. All amounts shown are GST-exclusive and Beta has a 31 March balance date. Which amount would be included in Beta’s taxable income calculation for the2020 income year?  A $5,000 deductible loss on disposal.  B Nil.  C $3,750 deductible depreciation loss.  D $5,000 assessable depreciation recovered. | **B** | Nil is included in Beta’s taxable income calculation for the 2020income year as no adjustment will arise. Depreciation to the date of sale cannot be claimed in respect of buildings with an estimated useful life of 50 years or more with effect from the 2012 income year. A loss on the disposal of a building is generally not able to be claimed (except if irreparably damaged and s. EE 48(3) applies). Depreciation recovery income can arise to the extent that consideration received for a building exceeds the adjusted tax value, however, this does not apply to these facts. |
| Shapxi Shoes Limited (Shapxi) has entered into a new lease to rent a retail shop in the 2020 income year. The fit-out will cost $80,000, of which the landlord has agreed to contribute $30,000. Which of the following statements are true in relation to this scenario?  A Shapxi could treat the $30,000 as income to be spread over the current and next nine years, and claim depreciation on the full $80,000 fit-out cost.  B Shapxi could elect to treat the $30,000 as non-taxable income, reduce the cost of the $80,000 fit-out by the contribution of $30,000 and claim depreciation on the $50,000 balance.  C Shapxi could elect to treat the $30,000 as non-taxable income and claim depreciation on the full $80,000 fit-out cost.  D Shapxi could treat the $30,000 as income to be returned wholly in the year of receipt and claim depreciation on the full $80,000 fit-out cost. | **A & B** | Section CG 8 provides that a capital contribution received (as defined) is treated as income in the year of receipt and in the nine following years. This is the default treatment for capital contribution receipts on or after 20 May 2010. A person may instead reduce the item’s base value so that depreciation would not be claimable on the portion of assets that have been paid for by a capital contribution. This is a valid option for receipts on or after 20 May 2010. |
| On 1 April 2019, Carsten Limited (Carsten) acquired a concrete mixing truck from Thorsten Limited (Thorsten), an associated company, for $60,000. Thorsten had purchased the truck brand new in April 2010 for $100,000 and depreciated it using a 19.2% DV rate. The adjusted tax value at 31 March 2019 is $14,679. The concrete truck’s market value on 1 April 2019 is $20,000. Which of the following statements is true in relation to the 2020 income year?  A Carsten would use the cost base of $60,000 and a DV rate of 16% or an equivalent SL rate of 10.5%.  B Carsten would use the market value of $20,000 as the cost base on which to calculate depreciation and a DV rate of 16% or an equivalent SL rate of 10.5%.  C Carsten would use the adjusted tax value of $14,679 as the cost base on which to calculate depreciation and the same DV depreciation rate(or an equivalent SL depreciation rate) that Thorsten used – i.e. 19.2%DV or the equivalent SL rate of 12.6%.  D Carsten would use $60,000 as the cost base and the same DV depreciation rate (or an equivalent straight line (SL) depreciation rate)that Thorsten used – i.e. 19.2% DV or the equivalent SL rate of 12.6%. | **A** | The cost base Carsten must use is $60,000 (being the lesser of the cost of the item to Carsten or the vendor’s cost) and the DV rate is either 16% or an equivalent SL rate of 10.5%. Section EE 40(9)(a)provides that the rate used by Carsten must be no more than the rate used by the vendor (Thorsten). The depreciation rate used by Thorsten included the 20% loading factor as the truck was originally acquired prior to 20 May 2010. The loading factor no longer applies to assets acquired after 20 May 2010 (s. EE 31 (3A)), and therefore Carsten cannot use the 19.2% DV rate. Carsten would use either the base depreciation rate of 16% DV or 10.5% SL.  Adjusted tax value is not an option under s. EE 40 and therefore this is not the correct base to use. Market value is not the correct base in this circumstance as s. EE40(7)(b) applies. The lesser of market value or cost is used when s. EE58 applies. |
| Fexu Manufacturing Limited (Fexu) owns machinery (i.e. plant) that was purchased in December 2018 for $45,000, for which an 8.5% SL rate was used in the 2019 income year.  In May 2019, the machinery was disassembled in order to find a fault and was out of action for three months. Fexu is registered for GST and has a 31 March balance date, and all figures shown are GST-exclusive. What is the maximum depreciation loss deduction available for this asset for the2020 income year? Type your response in the field, to the nearest dollar. The maximum depreciation loss available for this asset is $ [x]  A $5,684  B 5,684  C $5684  D 5684 | **A** | Depreciation claim for 2020 = $43,725 × 13% = $5,684. This is calculated by switching to the DV method and using a rate of 13% to maximise depreciation. The equivalent DV rate can be ascertained by referring to Schedule 10 ITA 2007 (or by looking up the default class for machinery). When switching methods, the adjusted tax value at the end of the prior year is used. The machinery being out of action for three months is ignored as s. EE 10 would apply, and so the property is treated as being available as if it was used or available for use immediately before going for repair. Opening adjusted tax value is $45,000 × 8.5% SL × 4 ÷ 12 months = $1,275,leaving an adjusted tax value of $45,000 − $1,275 = $43,725. |
| Mary owns a residential rental property which was acquired in 2019 and she is unsure of the depreciation rules that apply. Which of the following statements are true?  A The building 􀃑t-out default class within the depreciation rate determination could be used to find a depreciation rate for the rental property’s fitted wardrobes and internal walls.  B Blinds, carpets and curtains can all be depreciated as separate assets from the building.  C The commercial 􀃑t-out rules can be applied to residential rental buildings.  D The Commissioner of Inland Revenue (the Commissioner) applies a three-step test in order to determine whether a particular item is separately depreciable or is considered part of the building. | **B & D** | The Commissioner’s interpretation statement IS 10/01 Residential Rental Properties – Depreciation of Items of Depreciable Property prescribes a three-step test for determining whether an item is part of the building (and therefore depreciable at 0% rate) or whether it can be separately depreciated. Blinds, carpets and curtains can all be depreciated as separate assets from the building. These items are all listed in the Commissioner’s general depreciation determination DEP80Residential Rental Property Chattels, issued to apply from the 2012income year. The building fit-out default class cannot be used to find out the depreciation value of fitted wardrobes and internal walls as these are considered to be part of the building under the three-step test. The definition of ‘commercial fit-out’ excludes a fit-out used inside a ‘dwelling’, which in turn is defined as any place predominantly used as a place of residence or abode. |
| Low-rider Engineering Limited (Low-rider) has carried out a depreciation review for the 2020 income year and has discovered that depreciation has not been claimed on a piece of machinery since its acquisition in July 2017 . The machinery was purchased for $50,000 and is eligible for a 10% DV or 7% SL rate of depreciation. Low-rider is reviewing its options in 2020 with respect to this situation. Low-rider has a 31 March balance date. Which of the following statements are true?  A The adjusted tax book value of this asset at 31 March 2019 is either$41,625 (assuming a 10% DV rate) or $43,875 (assuming a 7% SL rate).  B If no election is made, and the asset is sold in the 2020 income year for$45,000, depreciation recovery income will arise.  C Low-rider can claim all of the missed depreciation from the earlier years in 2020.  D It is possible to make a retrospective election in the 2020 income year that this machinery not be depreciable property. | **A, B & D** | Depreciation for the prior income years must not be claimed in the2020 year. Low-rider may request the Commissioner to reopen the prior year returns to include the deemed depreciation or it may make an election that the machinery not be depreciable property. If the election is made, no depreciation recovery (or loss on disposal)will arise when the asset is disposed of. Depreciation is a mandatory charge and is deemed to have been claimed unless an election is made to not treat this item as depreciable property. |
| Bob started a lawn mowing business on 1 April 2019. Prior to setting up this business he owned a ride-on lawnmower which he will use 100% in his business. He had originally paid $7,495 for his lawnmower in April 2018. Which cost base will Bob use to calculate depreciation from 1 April 2019?  A Opening adjusted tax value at 1 April 2019 as if depreciation has been claimed since acquisition.  B The lower of original cost or market value at 1 April 2019.  C Market value at 1 April 2019.  D Original cost. | **C** | Section EE 58 applies to provide that the base value of an item is the item’s market value when the person starts to use an asset that has only been previously used for a private purpose and is converted to business use. |
| Raymonza Limited pays a premium of $90,000 on the grant of a lease for premises in a highly valued shopping area for a period of seven years, with a right to automatically renew for a further three years. Which of the following statements are true for this payment?  A The premium paid is fixed life intangible property because the item has a legal life that can reasonably be expected to be the same as the estimated useful life.  B The premium paid is not depreciable property because there is no finite useful life.  C The premium paid is depreciable intangible property.  D The premium is not depreciable property because such property is not expected to decline in value while used in carrying on a business. | **A & C** | The lease premium is depreciable intangible property if it has a finite useful life that can be estimated with a reasonable degree of certainty on its acquisition and it falls within Schedule 14 ITA 2007(which it does, being the right to use land). The useful life of this premium is 10 years.  The lease premium is also fixed life intangible property as there is a legal life of 10 years. The legal life is defined in s. EE 67 as the number of years, months and days for which an owner’s interest in an item of intangible property exists under the contract that creates the owner’s interest, assuming the owner exercises any rights of renewal that are either unconditional or conditional on the payment of predetermined fees. Fixed life intangible property is a subset of depreciable intangible property for which only the straight line method may be used. |
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