

Welcome to the Winter edition of *Commercial eSpeaking*. In this issue we cover some key points in the May Budget which will affect all New Zealanders, as well as business items that will be useful to you in your day-to-day professional dealings.

To talk further with us on any of the topics in this newsletter – or any other legal matter – please be in touch. Our contact details are above.



Budget 2017 – An overview

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The Minister said the outlook for New Zealand's economy is positive and the Crown's books are steadily improving. We highlight some of the Budget's key points below.

Tax cuts

From 1 April 2018, there will be tax cuts for every working New Zealander with particular emphasis on lower to middle income earners.

Income that can be earned at the lowest tax rate of 10.5% will rise from \$14,000 to \$22,000 which means \$11 more a week. The 17.5% income tax rate will be raised from \$48,000 to \$52,000 giving an increase of \$20 a week.

There's no change to the 33% top tax rate income threshold of \$70,000. However, all taxpayers will pay less tax from 1 April next year due to the lower tax rate bands being raised.

Working for Families

From 1 April 2018 there will be changes to the Working for Families (WFF) regime. The maximum credit for the first child under 16 will be raised by \$9 a week, and for each subsequent child under 16 years old by between \$18–\$27/week. The abatement rate is increased to 25%. However for families earning at the top of the WFF income scale, the abatement threshold is reduced to \$35,000.

The Accommodation Supplement increases the maximum payment rates for a two-person household by between \$25 and \$75/week. For larger households, there will be increases of between \$40–\$80/week. With the Supplement being last increased in 2007, this boost will be very welcome for affected families.

Students living in high rent areas who are eligible for the Accommodation Benefit will be able to claim up to \$60/week, up from \$40/week.

The Independent Earner Tax Credit will be discontinued.

Increase for superannuitants

New Zealand Superannuation payments are pegged to after-tax wages. As a result of the wage increases relating to the tax

Shareholders' Agreements

Relationship property for companies

Shareholders' agreements are comparable to relationship property agreements (colloquially known as 'pre-nuptial agreements'), as the objective of each is to establish rules for relationship property – whether it's in your business or your personal life.

Not all relationships were built to last forever, and even the most stable

relationship amongst shareholders may waver. Issues may also arise unexpectedly, such as the death of a shareholder or the need for a shareholder to sell their shares. Planning in advance for these events can pre-empt a dispute, and save some costs for the respective parties.

Unlike a company constitution, a shareholders' agreement is not registered with the Companies Office and therefore it has a greater degree of confidentiality. Company constitutions generally contain the nuts and bolts provisions to operate the company that are not provided for in the Companies Act 1993.

Shareholders' agreements often have an overlap with the provisions of a

constitution. However, they usually they contain more sensitive information about company affairs such as the roles and remuneration of the shareholder employees, the dividend policy, funding of growth strategies, rules around compulsory selling of shares in certain circumstances along with dispute resolution provisions.

Dispute resolution

Dispute resolution provisions would include normal mediation and arbitration clauses but, for circumstances where the shareholders simply cannot continue in business together, a 'Russian roulette' or 'shot gun' clause (where each party puts forward a price for the other's shares and

the party who puts forward the highest price then purchases the other's shares at that price) gives finality. It's a quick method for managing the exit of a shareholder where a dispute cannot be resolved, but it obviously presents some elements of commercial risk.

Other relevant provisions to include are:

- » Options to purchase shares and how to calculate their value
- » Rules around shareholder employee's incapacity, bankruptcy and non-participation
- » Rules around company loans and guarantees, and
- » Security given over shares.

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Business Briefs

It will all come out in the wash: non-compliance with minimum employment standards

The Employment Relations Authority (ERA) has imposed a significant penalty of \$145,000 on Manukau Auto Valet Limited for its failure to pay minimum wages and/or holiday pay to at least 115 of its employees.¹ The penalty was imposed in addition to Manukau Auto Valet's reimbursement of \$96,451 to its employees, which was owed as a result of its non-compliance.

In total there were 322 separate breaches of employment law, each being capable of being penalised with a fine of up to \$20,000 that created a total potential liability of \$6,440,000. However, as is usual in situations like this, the ERA applied a globalised approach in respect of the breaches and considered other relevant matters such as Manukau Auto Valet's co-operation. The penalty was reduced to \$145,000, which is still a significant sum.

We remind employers to ensure that your payroll systems and record keeping meet all the relevant employment law requirements. Otherwise there could be an expensive lesson. ■

Further Takeovers Code relief on the way for small companies

The Takeovers Panel has recommended to the Minister of Commerce and Consumer Affairs that three substantive and numerous technical changes be made to the Takeovers Code.

The main change proposed is that the definition of 'Code Company' will only capture companies that, together with their subsidiaries, have a total annual revenue of at least \$15 million, or assets of \$30 million, at the end of the most recent accounting period. This will exclude small unlisted companies, and will remove the disproportionate cost of Code-compliance for them, while retaining appropriate restrictions for larger and listed companies.

Two other important changes are:

1. *'Days' in the Code*: Amending the Code to state timing obligations in 'working days' in line with other legislation, such as the Companies Act 1993, rather than in 'days.' Amending the timing rules to refer to 'working days', which will exclude weekends, public holidays and the Christmas/New Year period, will address practical issues, including

the potential for interested parties to be subject to tight timeframes where takeovers take place over holiday periods.

2. *Electronic access for shareholders*: Amending the Code to facilitate electronic communication and the public availability of Code documents by:
 - » Requiring target companies to provide offerors with the email addresses of shareholders who have provided them to the target for the purposes of receiving documents electronically
 - » Requiring that Code-regulated communications by a target or offeror are made electronically, subject to the target, the offeror or an affected shareholder having the right to request hard copy communications, and
 - » Allowing the Takeovers Panel to publish Code-regulated documents on the Panel's website. ■

Employee share schemes, your time is up

A great deal of Inland Revenue's recent work on employee share schemes has

culminated in the recently-introduced Taxation (Annual Rates for 2017–18, Employment and Investment Income, and Remedial Matters) Bill.

The Bill, which sets out the new rules for taxing employee share schemes, is very important – to both companies that have employee share schemes in place, and to those people who are currently participating in them.

Over the years, schemes have been put in place which ultimately provide non-taxable capital gains to employees. Usually they're structured by providing employees with the ability to buy company shares using a loan from the company. Essentially, under the Bill these types of schemes will be taxed on the same basis as employee option schemes, which is that employees are taxed on the difference between the strike price they pay to exercise their options and the value of the shares at the time of exercise.

If you're operating a business that currently has a share scheme that could be caught by the proposals, or you're a participant in such a scheme, you should talk with us for advice on the implications of the Bill. ■

¹ *Labour Inspector of the Ministry of Business, Innovation and Employment v Manukau Auto Valet Ltd* [2017] NZERA Auckland 85

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Shareholders' Agreements

Susan and Nancy

The case study below illustrates some benefits of a shareholders' agreement.

Siblings Nancy and Benjamin Button each hold a 50% share in Button Enterprises Limited (BEL); they are the company directors. There was no constitution or shareholders' agreement. Over the years they have managed their company successfully. Their only trouble seemed to be the poor relationship between Nancy and Benjamin's new wife, Susan.

Benjamin died unexpectedly, leaving his shares to Susan. At that time, Susan had large debts to pay for their lavish wedding so she desperately needed cash. Nancy wasn't prepared to issue dividends from the company as she and Benjamin had planned to reinvest the company's profits for growth.

The relationship between Susan and Nancy soured quickly – Nancy often could not get Susan to sign a 'special resolution' required for a company to undertake any 'major transaction (the Companies Act 1993 requires that at least 75% of shareholders endorse major transactions). As a result, BEL's profitability, and the shareholders' working relationship, suffered.

Nancy remains concerned that Susan could simply sell her shares to any third party – who knows who she would be working with then?

A shareholders' agreement would have helped in the Susan/Nancy situation. It would have improved their working relationship and given Nancy more certainty following Benjamin's death. The relevant clauses that would have helped Nancy include:

- >> On the death of a shareholder, their shares must be offered firstly to the existing shareholders
- >> Life insurance cross-cover for Nancy and Benjamin. This would have provided cash for Nancy to purchase Benjamin's shares on his death, and
- >> A clear dividend policy and a policy around reinvestment of profits into maintaining and expanding the business.

The good news is that even if your company is already up and running it's not too late to establish a shareholders' agreement. As you can see from the Susan/Nancy situation, a shareholders' agreement can be invaluable for any company, irrespective of its size or sector in which it operates. It doesn't need to be complex, and it can be tailored for your company's specific situation.

It's just like those who enter into a relationship property 'pre-nup', it can pay to set down rules in advance. ■

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cuts (see page 2), from 1 April next year couples receiving NZ Superannuation will get \$13.10 extra a week, \$7.90 more for a single person sharing, and \$8.50 for a person living alone.

Insurance premiums to rise

In November, home owners face an insurance premium rise of up to \$69/year. The earthquake levy will rise to 20c per \$100 worth of insurance cover, to a maximum of \$276/year. The current earthquake levy is 15c per \$100 worth of cover; the maximum being \$207/year.

These increases will help replenish the Earthquake Commission's Natural Disaster Fund that has been seriously depleted following the Christchurch and Kaikoura earthquakes.

Foreign tax loopholes to be closed

Foreign tax loopholes currently exploited by both multinationals and New Zealand corporates with offshore operations are to be closed over the next three years. More than \$250 million is expected to be gathered by the government over that period.

The gains are expected from three initiatives put out for discussion in the last nine months covering transfer pricing

and permanent establishment avoidance, interesting limitation relating mainly to related party debt, and hybrid financial instrument mismatches.

The latter allow companies to pack their New Zealand entities with tax-deductible debt arrangements and reduce tax here. In recent years, these have been subject to a string of successful challenges in the courts by the Inland Revenue.

'Black hole' expenditure

The Budget has addressed the contentious treatment of so-called 'black hole' expenditure, relating to expenses borne by a company exploring a commercial initiative that is later abandoned. At present this expenditure is neither immediately tax deductible nor depreciable, and falls into a so-called 'black hole.'

The issue was the subject of unsuccessful appeals all the way to the Supreme Court by electricity generator Trustpower, which sought relief for expenses related to a wind-farm development that did not go ahead.

Public feedback on *Black hole and feasibility expenditure* can be found [here](#) and is open until Thursday, 6 July.

*To read more about the Budget go to **Budget at a Glance** or to read more fiscal material, go [here](#).* ■