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Commentary, opinion and intelligence for the New Zealand business community

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Time to raise your procurement game: Forget output, think outcomes

It’s been one year since the Government introduced its new procurement rules – swinging its $42 billion wallet in the direction of sustainable, socially responsible spending.

Is that massive spending power starting to pull our economy in the direction the Government wants? We’ve recently conducted research into how much progress is being made within agencies, to get a sense of how successfully the new rules are being implemented.

Collaborative contracts for existing solutions are a winner; elsewhere suppliers are still playing catch up.

Our research revealed:

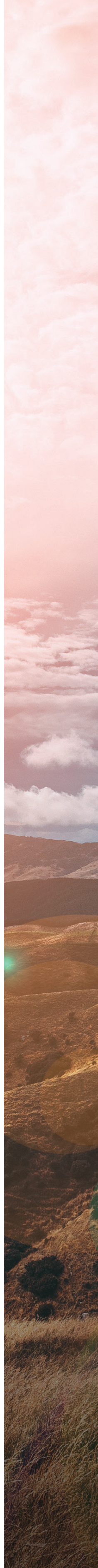
Agencies are doing very well at knocking off the low-hanging fruit by joining collaborative contracts. The areas that have progressed the fastest have well defined solutions in the market and agencies are advancing these with relative ease. Collective agreements with built in sustainable options are allowing them to make significant progress in areas like fleet emissions.

Strategies are working. This might sound obvious, but it’s nice to have evidence and a proven pathway for those still catching up. The more planning and stakeholder engagement up front, the more progress agencies have been able to make.

Procurements are now focused more on delivering social outcomes and that takes planning, effort and sometimes more money. This causes difficulties when stakeholders want a quick turnaround or are fixed on the quickest, cheapest way to get an output.

The COVID-19 pandemic has caused both headwinds and tailwinds.

Suppliers are still playing catch up as they start to learn the fundamentals of the new procurement rules; however, this can prevent agencies from making bigger strides.



Aiming for outcomes, not outputs.

The Government knows what it wants: the ‘nice to haves’ are now ‘must haves’ or differentiators. All those aspects previously considered warm and fuzzy non-essentials are now front and centre. The response from industry has been, ‘Okay, but we’re not completely sure how to do this.’ Businesses which have previously used some vague green-washing in their bids are discovering this is no longer sufficient.

Instead of thinking in terms of outputs, there is a shift to thinking about outcomes. It’s no longer about how many widgets you need to deliver to the Beehive. Now it’s about more: is the widget being made in New Zealand from sustainable sources? Are the people delivering it being paid the living wage rate? And is your business contributing a net gain to our country in more than just dollar terms?

Even if your supplier says the widget is being made sustainably in New Zealand, and you believe it, in the future you can be expected to prove that right back to the forest where the trees were planted to create the widgets. The longer these procurement rules are in place, the more thorough agencies will be in their supplier reporting and auditing.

Contents

Setting yourself up for success as a Government supplier.

Here are four ways your business can raise its game to meet the Government's procurement goals:

1 Take stock

You don't know what you don't know. Look across your whole business to assess how well you deliver social outcomes through what you do and establish a baseline for improvement.

2 Define your aspiration

Our research clearly demonstrates the value of good strategy and planning. Set targets for where you'd like to get to. Map out what the journey looks like to achieve the Government's procurement goals. Make sure your entire team also understands what this means for your everyday operations.

3 State your intent

Go public with what you would like to achieve and what your journey will be to get there. Invite suppliers and public customers to help you achieve your aspirations.

4 Be accountable

Develop your own reporting and auditing systems so you can easily demonstrate your processes and practices. Publish your progress and socialise it internally. This proves how serious your organisation is about social outcomes, and it's a great precursor for future success.

If your business is struggling, there are people out there who can help, including business networks, consultants and many open-source resources.

COVID-19 has caused headwinds and tailwinds.

Obviously COVID-19 has created significant challenges for agencies and suppliers. The recession means there's been less money to spend, putting the pursuit of broader outcomes in conflict with tighter budgets.

However, the pandemic has also changed New Zealand in ways that support the goals of the procurement rules:

Almost everyone has been thinking hard about their priorities this year, and we inevitably discover that we value the environment, taking care of each other and preventing negative outcomes like homelessness and poverty. At every level people are engaging more with the ideals reflected in the procurement rules.

The 'Buy New Zealand Made' resurgence has been felt not only by consumers, but also by agencies. They've taken it up a notch, procuring from local communities for local projects. Suppliers who source not just nationally, but locally, will benefit.

Suppliers and agencies now know how fast they can change if they really want to, thanks to the dramatic shifts in working from home and online operations under lockdown.

The pandemic has changed New Zealand in ways that support the procurement rules.

Boosting NZ Inc: Productivity, profitability and people.

One of the major barriers to productivity in New Zealand is our propensity to throw cheap labour at jobs, rather than investing in innovation and systems. Now, the Government is driving improved training for Kiwis, and that's going to be compounded by a likely shortage of cheap labour, at least as long as our borders remain closed.

For the time being, with the Government pushing for the living wage, it no longer becomes economical to keep employing low-skilled employees. Instead, our businesses will need to invest in better systems and technology.

Theoretically, that should improve New Zealand's productivity, which has long been too low, and raise the average skill level of our workers. It would be wonderful if these procurement rules were a step along the road to a NZ Inc. that exports more high-value technology, ideas and innovation to the rest of the world. Over time we can make that happen – lifting our standard of living, reducing poverty and making this country into a tiny engine of prosperity and ingenuity.

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Significant GST changes on the way for Not for Profit organisations

Registered New Zealand Not for Profit organisations can access a range of tax concessions compared to their for Profit counterparts. GST registered New Zealand Not for Profit organisations can claim GST credits on all of their assets and on related ongoing costs even if those assets are not used in their GST taxable activity.

This concession is available to Not for Profits, however it comes with a future downside, via a full GST liability when assets that are not part of the GST activity are eventually sold or when the GST activity ends.

Put simply, if a Not for Profit organisation has claimed GST credits for the maintenance or purchase of an asset that does not form part of its GST activity and then sells that asset in the future, the sale proceeds will be subject to GST even though the asset has not been used in the GST taxable activity unless zero-rating rules apply to the sale.

A concession has been introduced to allow GST registered Not for Profits to remove assets not forming part of their GST activity from the GST tax net. However, the concession requires an election to be made by 31 March 2021. The benefit of taking the concession is to eliminate a larger GST liability in the future, especially for land assets that have appreciated substantially in value. The concession is also available on a limited retrospective basis and can be applied to asset sales completed on or after 15 May 2018. This could result in the recovery of GST output tax already paid on disposals of assets that were not part of the GST activity, or the removal of audit risk, if GST has not been correctly accounted for. The new rules could also apply to many other instances of asset disposal including insurance claims paid on an asset, as this is treated as a sale for GST purposes.

There is a limited opportunity for organisations to act prior to 31 March 2021 to ensure that GST is not payable on any future sale of the assets that are not part of GST activity.

Case study

For example, a church historically purchased a hall next to its premises for the use of parishioners as well as the public for a small fee; fees collected have never exceeded the $60,000 compulsory GST registration threshold. The GST input credit for the purchase, ongoing maintenance, and operating costs of both the hall and the church have been claimed under the voluntary GST registration of the church. The GST taxable activity is the hall hire, and the GST registration was historically made on a voluntary registration basis as the hall hire fees are well under the $60,000 compulsory GST registration threshold. The church building is used for worship and this generates no revenue (donations are excluded) and the church building does not form part of the organisation's GST activity, but GST claims are available for this building and have been taken by the organisation.

If the church is sold, then long-standing GST rules mean that GST will be payable. The church asset has increased in value over the years, and the organisation has chosen to make an election by 31 March 2021 to remove the church building from the GST net. Their rationale for the election is that the GST claims for the church building and land were made when the church asset had a much lower value, whereas the value today is much higher due to the significant increases in land values in the area. The election is a chance to repay the relatively low GST refunds on this asset, and avoid a significantly larger GST liability that would be payable in the future if the asset was sold or the GST activity (hall hire) ended.

The church therefore makes an election to the IRD (prior to 31 March 2021). As part of this election, the church has calculated the GST repayable which is:

- the GST input tax claimed for the initial purchase of the church
- the GST input tax claimed relating to the operating costs to maintain the church over the past seven-year period.

The IRD accepts this election and the GST repayable under the calculation is included in the next GST return filed by the church. GST will not be payable on the eventual sale of the church.

Next steps

There's still time for Not for Profit organisations to protect their existing assets which are not part of their GST activity from future GST output liabilities, but they will need to act quickly. Prior to 31 March 2021, NFPs will need to ensure they won't be charged GST output at the time of future asset disposal by determining:

- the extent of their taxable activity
- the applicable assets that do not form part of their GST taxable activity and determining the merit of making an election now to isolate their non GST activity assets from the GST net by repaying previous GST input deductions, versus the longer term and potentially much larger GST output tax liability that will arise in the future if an election is not made.

The amount of repayable GST if an election is made on or before 31 March 2021, is the amount equal to all input tax claimed for the capital cost of the asset (or an estimate thereof if records are not held), plus all input tax claimed relating to the operating costs of the asset in the past seven-year period.

Again, it's critical that Not for Profit organisations act quickly, so please contact your Grant Thornton advisor if you wish to expedite a high level GST review to determine if an election by 31 March 2021 is of merit.

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NZ's tax psyche set to change

All things tax will get more attention from business owners, entrepreneurs and sole traders as the recently elected Government will raise the income tax rate from 33% to 39% for those earning over $180k.

The new tax threshold comes into effect on 1 April 2021 and is intended to affect only 2% of the taxpaying population; a large portion of those people are on salaries or wages with little ability to change how they earn their income, however, this "wealth tax" will have a significant and unexpected impact on the psyche of taxpayers in general.

The danger of this psyche shift we're about to see is the poor decisions people will make to avoid higher taxes – many people, particularly entrepreneurs and sole traders will be thinking to themselves, 'why should I bust my hump just to pay more tax?.'

Taxpayers need to seek the right advice as making assumptions and misunderstanding their obligations can actually cost more money.

When the National Government returned the income tax rate to 33% in 2010, the business community deemed this as fair – and of course "fairness" is one of the fundamental pillars of an effective tax system.

Subsequently, given this relatively flat structure, advisors around the country saw business owners' focus shift away from how to effectively structure and save tax, to growing their businesses and generating wealth, which has beneficial flow-on effects to their employees and the economy in general.

Now, the change in the headline rate will bring tax back onto the agenda for many businesses, regardless of whether they actually face the increased tax charge or not.

Naturally, most businesses want to maximise tax opportunities and minimise the amount they pay, but going forward, it shouldn't be the sole focus for contributing to healthy revenue generation.

Businesses need to take a holistic approach by also focussing on meaningful revenue generating strategies and activity.

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39%

income tax rate will rise from 33% to 39% for those earning over $180k.

COVID-19 impact on NZ tax residence rules

New Zealand's swift decision to close its border to everyone except NZ citizens and permanent residents has made the country feel like a safe haven for people who ordinarily would not live here full time. However, staying in NZ for longer than usual can have some unexpected tax consequences for people who have decided to extend their stay - either for health reasons or because it is not desirable to return to their home country right now.

183 days

An individual who spends an aggregate total of more than 183 days in New Zealand within any 12-month period will be regarded as NZ tax resident.

New Zealand's tax residence rules state that an individual who spends an aggregate total of more than 183 days in New Zealand within any 12-month period will be regarded as NZ tax resident. Separately, individuals who have a home available to them in New Zealand may also be regarded as tax resident of New Zealand, irrespective of their presence in New Zealand. This New Zealand home could be in a range of forms including a personally owned home, or a rented home or a home made available for use by another party.

The consequence of having New Zealand tax residence status is the liability to New Zealand tax on world-wide income. Although treaty concessions and the Transitional Resident concession may mitigate that exposure to New Zealand tax, any concession will depend on specific case by case circumstances.

This exposure to New Zealand tax may come as a bit of a shock for those individuals who have stayed here longer than intended due to the pandemic and they may not realise that their extended stay has tax consequences.

Inland Revenue has recognised that many people are stranded here during the country-wide lockdown and that this may have had unintended consequences via their NZ tax residence status. Inland Revenue has issued a statement that for the purpose of the 183-day count test individuals can ignore the extra days spent in New Zealand when they were unable to leave. This is provided that the individual leaves New Zealand as soon as is reasonably possible to do so. However, people who have stayed here longer than they needed to by choice will not be able to take advantage of this concession. The concession will not assist people who are separately New Zealand tax resident by having a home in New Zealand.

Similar concessions will also apply to overseas companies where the director is exercising control here, while they have been stranded. The foreign company will not change its tax residence status just because a director is exercising management and control of the company from NZ temporarily, provided they do not usually carry out their director's duties here.

New Zealand has a number of double tax treaties with other countries which provide tie breaker tests when the individual is simultaneously resident in two countries. These tests typically look at where the person has a permanent home and to which country they are more closely linked. The uncertainty of when the pandemic will peak across the globe is contributing to the uncertainty of where people will spend the majority of their time in the future and where they will be tax resident going forward. The consequence of this uncertainty for individuals who are eligible to use a New Zealand tax treaty is that tax rights that are shared between New Zealand and the other tax treaty country may vary and a greater liability to New Zealand tax may unexpectedly arise.

If this could impact someone you know, it is essential that they seek professional advice to ensure that future potential tax liabilities are identified early and that tax exposures are not unknowingly triggered.

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Paige Cuthbert appointed Chair of Grant Thornton New Zealand

We are delighted to announce that Paige Cuthbert has been appointed as Chair of Grant Thornton New Zealand's Board effective immediately.

Based in Christchurch, Paige is a highly experienced advisor and has over 30 years' experience working closely with South Island businesses. Her extensive industry expertise includes agri-business, manufacturing and processing, fisheries, professional services, construction, and retail.

Paige is a fantastic leader who has made a tremendous contribution to our firm's people experience and culture since joining Grant Thornton in 2017.

Paige says that strong leadership and good governance are cornerstones of any successful business and there has never been a time when these have been more important. Kiwi businesses are facing unprecedented challenges and she will play a pivotal role in helping them navigate their way through the current environment.

Paige also says that this appointment will give her a broader focus both personally and professionally, and she is looking forward to playing her part in both the firm's and our clients' continued success.

Prior to this appointment, she was a Board member and previously sat on the Grant Thornton executive committee.

Paige is replacing Murray Brewer who is stepping down as Chair after serving the maximum term on the Board.

Murray has made a significant contribution to the firm's strategy, its culture, and the growth of our people and clients over this time. He will continue to be a valued senior partner within our firm and a source of knowledge and expertise for our Board.

If you require further information about any of these topics or would like details on other accounting or advisory matters, contact your local Grant Thornton office:

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