



Inland Revenue
Te Tari Taake

IR289
May 2021

Provisional tax

Paying your income tax in instalments

COVID-19

Having difficulty paying taxes due to the impact of COVID-19?
We can help you – see ird.govt.nz/covid-19 for details.

Contents

About this guide	3	<hr/> <p>This guide is A5 and can be economically printed two pages per A4 sheet. If you're printing from a downloaded PDF, check the layout settings in your printer options to achieve this.</p> <hr/>
How provisional tax works	4	
Your options for calculating provisional tax	6	
Penalties	20	
Interest on provisional tax	22	
Your first year in business	29	
Budgeting for your provisional tax	32	
Terms we use	33	
How to contact Inland Revenue	36	
Privacy	37	
Inland Revenue's services	38	

The information in this guide is based on current tax laws at the time of printing.

About this guide

Provisional tax helps you manage your income tax. You pay it in instalments during the year instead of a lump sum at the end of the year.

You'll have to pay provisional tax if you had to pay more than \$5,000 (\$2,500 in 2019/20 and earlier years) tax at the end of the year from your last return.

This guide tells you how to manage your provisional tax instalments.

This guide covers:

- how provisional tax works
- who has to pay it
- how to calculate it
- when to pay it
- what happens if you do not pay
- budgeting for provisional tax
- a glossary to help you understand the tax terms we use.

We explain all the tax terms we use in this guide on pages 33-35.

How provisional tax works

Provisional tax is not a separate tax. It's income tax you pay during the year and helps you "spread the load" and avoid a big end-of-year tax bill.

You must pay provisional tax if, at the end of the previous year, you're left with tax to pay of more than \$5,000 (\$2,500 in 2019/20 and earlier years). We call this amount your "residual income tax" (RIT). Specifically, RIT is the amount of tax to pay on your taxable income, less any PAYE deducted and any other tax credits you may be entitled to (except Working for Families Tax Credits).

Your RIT may exceed \$5,000 (\$2,500 in 2019/20 and earlier years) if you earn untaxed income, or not enough tax has been deducted to cover your income tax for the year.

Examples are:

- self-employed or rental income
- schedular payments or salaries and wages with a low PAYE rate
- income from a partnership or look-through company
- income from an estate or trust
- overseas income.

In most cases, you pay provisional tax in three instalments during the year, based on what provisional tax option you choose.

When you complete your income tax return and calculate your tax for the year, you deduct the provisional tax you paid earlier.

Any taxpayer who pays income tax may have to pay provisional tax. This includes individuals, companies and trusts.

Provisional tax is income tax you pay during the year.

Provisional tax helps you spread the load.

RIT is the amount of tax to pay on your taxable income, less any PAYE deducted and any other tax credits you may be entitled to (except Working for Families Tax Credits).

Example

Matt earns a salary and also has self-employed income. Here's his 2020 income tax return:

Salary	\$ 14,800
Plus self-employed income (net profit)	\$ 47,600
Taxable income	\$62,400
Tax on taxable income	\$ 11,740
Less PAYE deducted from the salary (not including ACC earners' levy)	\$ 1,610
Residual income tax (RIT)	\$10,130

Matt's 2020 RIT is more than \$5,000 so he'll have to pay provisional tax for the 2021 tax year. When he files his 2021 return, he'll deduct the provisional tax from his RIT, leaving a refund or "end-of-year tax" to pay.

When to pay your instalments

When you pay your provisional tax instalments depends on your balance date - the last day of your tax year.

This guide assumes you have the standard balance date of 31 March. If you do not, you can use our "Tax due date calculator" to print a calendar of all the due dates that apply to you. Go to ird.govt.nz/provpaymentdates

Transitional year

If you change your balance date, you may need to calculate the provisional tax for your "transitional year" a bit differently. That's because your transitional year - the first year with the new balance date - will be for a period of more or less than 12 months.

Anyone wanting to change their balance date must get approval from Inland Revenue first. If we approve your new balance date, we'll tell you when your instalments are due.

Your options for calculating provisional tax

The idea behind provisional tax is simple. You're trying to calculate an amount that will closely match the RIT you expect for the year. That way, when you complete your tax return and deduct your provisional tax, you should only have a small amount of end-of-year tax left to pay. You may even receive a refund.

There are four ways to calculate provisional tax:

- the Accounting Income Method (AIM)
- the standard option
- the estimation option
- the ratio option.

Because most people do not know how much tax they'll need to pay next year, calculating provisional tax usually involves a certain amount of judgement. You'll need to decide which provisional tax option works best for you.

If you do not make a choice, the standard option will apply.

You can choose any option (except the Accounting Income Method) by completing a box in your income tax return, sending us a secure email in myIR, or calling us on 0800 377 774.

If you want to use AIM to calculate your provisional tax for the year, you need to send us a statement of activity using your AIM-capable software.

The Accounting Income Method (AIM) option

The Accounting Income Method (AIM) aligns your provisional tax payments with the periods in which you have income to work out your instalments. You will pay provisional tax under the AIM option while you're making a profit. If you're not making a profit, payments will not be required.

Choose the option that works best for you.

Your provisional tax payments are based on your tax profits for the period.

You need AIM-capable accounting software that will calculate your provisional tax payments (if any) for you using your accounting records.

If you're currently using the estimation option, you must submit your first statement of activity by your first provisional tax instalment date for the year.

If you're using the standard or ratio option, you can choose to use the AIM option at any time, provided that:

- you submit your first statement of activity before your final provisional tax instalment date for the year, and
- you have made all payments due under your current option up to the date you switch.

Once you choose to use AIM for the year you can not choose another option until next year.

Payments align with your GST due dates.

When your provisional tax is due

Your dues dates for AIM are generally the same as your GST due dates:

- monthly (if you're registered for monthly GST filing) or
- two-monthly (if you're registered for two or six-monthly GST filing)

If you're not registered for GST, your dates would be the two-monthly GST due dates that align to your balance date.

Qualifying for the AIM option

Aim is available to individuals and companies with a turnover under \$5m. If your turnover goes over \$5m during the year you can request to continue to use AIM.

You cannot use AIM in a year that you change your balance date.

AIM-capable accounting software

To use the AIM option you must have AIM-capable accounting software provided by an approved AIM provider.

You'll need AIM-capable accounting software

Calculating your provisional tax

At each due date your AIM-capable accounting software will work out your provisional tax payments and let you know how much to pay (if any).

Statement of activity

As well as working out your provisional tax, your software will also collate your income and expense information and send it to us in a Statement of Activity.

A Statement of Activity is not an income tax return.

Overpayments

If you have a drop in profit that means you may have overpaid your provisional tax during the year. Under the AIM option you can get a refund straight away. You can include instructions on what you would like done with the overpayment on your statement of activity. If you do not provide any instructions we will refund the overpaid amount.

You can get overpaid provisional tax refunded straight away.

The standard option

The standard option assumes your profit will increase from year to year.

The standard option assumes your income will increase from year to year.

When your provisional tax is due

Generally you'll pay three instalments on 28 August, 15 January and 7 May. But if you're registered for GST and you file six-monthly GST returns, you'll only pay two instalments, on 28 October and 7 May.

Example

Nicole earns schedular payments that have tax deducted at a flat rate of 20%. Because 20% is less than her average tax rate, Nicole has end-of-year tax to pay. In May 2020, Nicole completes her 2020 income tax return. These are her provisional tax calculations:

2020 RIT

(over \$5,000, so Nicole must pay provisional tax)	\$ 7,600
Plus 5%	\$ 380
Nicole's 2021 provisional tax	\$7,980

Her due dates are:

28 August 2020	\$ 2,660
15 January 2021	\$ 2,660
7 May 2021	\$ 2,660
	\$ 7,980

Nicole will pay the first two instalments of her 2020 provisional tax at the same time as she's earning her 2021 income. She's "spreading the load". The final instalment is due after the end of her 2021 tax year.

Filing your tax returns

When you use the standard option, your provisional tax is calculated from your previous year's RIT.

You need to file your tax return on time, so you'll know your RIT before your instalments are due.

If you do not have an extension of time to file your return, you'll need to file it by 7 July every year. That gives you time to work out how much provisional tax you need to pay, and prepare for your first instalment on 28 August.

If you file your returns late, you still need to pay your provisional tax instalments on time. Complete your return so you can work out how much you need to pay. Penalties and charges can apply if you pay an instalment after the due date.

Remember to file your returns on time.

Filing your return if you have an extension-of-time arrangement

If you have an extension of time to file your tax return, you could have to pay an instalment of provisional tax before you know what your RIT is.

In this situation, you'll calculate your provisional tax instalments using the RIT from two years ago, plus 10%.

When you file your return, you'll do a special "catch-up" calculation to take into account any earlier under or overpayments. The tables show how you'd do the calculation for the 2020 tax year.

If you're using a tax agent, they'll usually have an extension of time.

Instalment 1 (called "P1" in the other two tables)

2019 return filed	Instalment 1 (P1) due 28 August 2019
Between 28 August 2019 and 15 January 2020	$(2018 \text{ RIT} + 10\%) \div 3 = \text{amount to pay}$
After 15 January 2020	$(2018 \text{ RIT} + 10\%) \div 3 = \text{amount to pay}$

Instalment 2 (called "P2" in the table below)

2019 return filed	Instalment 2 (P2) due 15 January 2020
Between 28 August 2019 and 15 January 2020	$(2019 \text{ RIT} + 5\%) \times 2 \div 3 - (P1) = \text{amount to pay}$
After 15 January 2020	$(2018 \text{ RIT} + 10\%) \times 2 \div 3 - (P1) = \text{amount to pay}$

Instalment 3

2019 return filed	Instalment 3 due 7 May 2020
Between 28 August 2019 and 15 January 2020	$(2019 \text{ RIT} + 5\%) - (P1) - (P2) = \text{amount to pay}$
After 15 January 2020	$(2019 \text{ RIT} + 5\%) - (P1) - (P2) = \text{amount to pay}$

Even if you filed your return after 7 May, your provisional tax will still be based on your 2019 RIT.

Example

Ned's company, EJ Auto Services, has an extension-of-time arrangement. Its 2020 return does not have to be filed until 23 January 2021, so Ned will have to pay the company's first two instalments of 2021 provisional tax (due 28 August 2020 and 15 January 2021) before he knows how much the RIT will be. He goes back two years and looks at the company's 2019 RIT:

EJ Auto Services 2019 RIT	\$ 24,000
Add 10%	<u>\$ 2,400</u>
	\$ 26,400

Using the "catch-up" method, Ned pays the following instalments of provisional tax:

28 August 2020 \$8,800 $(\$24,000 + \$2,400) \div 3$

15 January 2020 \$8,800 $(\$24,000 + \$2,400) \div 3 \times 2$
– \$8,800

The company files its 2020 return on 23 January 2021 showing an RIT of \$23,740. The final catch-up instalment is: 7 May 2021 \$7,327 $(\$23,740 + 5\% [\$1,187] - \$8,800 - \$8,800)$

If your return for the previous year is assessed/ amended within 30 days of an instalment date

If the return for the previous year is either assessed (Inland Revenue changes the assessment amount) or amended within 30 days of a provisional tax instalment date, that provisional instalment will not change.

But if you file your return within 30 days before an instalment date then that instalment amount will be as calculated in the return you filed.

Example

John has filed his 2019 IR3 return on 7 July 2019. His provisional instalments for 2020 are:

28 August 2019: \$3,000

15 January 2020: \$3,000

7 May 2020: \$3,000

His return is then reassessed on 20 December 2019, creating an increase in his 2019 RIT. As there are less than 30 days between the reassessment his second provisional tax instalment date, the increase in the amount of provisional tax payable will be included in the third instalment as follows:

28 August 2019: \$3,000

15 January 2020: \$3,000

7 May 2020: \$5,500

If your income changes

When you are on the standard option and have paid all but your final instalment in full and on time you can make a payment for your final instalment that better reflects your income situation and remain on the standard option.

You can change from the standard option to the estimation option at any time up until the date your final instalment is due. After you've made the change, you cannot then change back to the standard option for the same tax year.

The estimation option

The estimation option could be right for you when your income is dropping. Using the standard option might mean you overpay your provisional tax.

Your provisional tax equals your estimated RIT for the year. It works like this.

- Add up all the taxable income you expect to receive next year.
- Calculate the tax on this figure.
- Deduct any PAYE and other tax credits (except Working for Families Tax Credits) you'll be entitled to.

The result is your estimated RIT, and this is your provisional tax for the year.

When your provisional tax is due

Generally you'll pay three instalments, due 28 August, 15 January, and 7 May. But if you're registered for GST and you file six-monthly GST returns, you'll only pay two instalments, due 28 October and 7 May.

The estimation option may be a good choice if your income is dropping.

Example

Hiwi is a property developer and a polytech lecturer. The property market is in a slump and Hiwi expects his net profit to decrease in the coming year. His tax agent advises him to switch to the estimation option to work out his 2020 provisional tax.

Hiwi's calculations:

Net profit from property sales	\$170,600
Plus polytech salary	\$ 78,000
Expected taxable income	<u>\$248,600</u>
Tax on taxable income	\$ 72,958
Less PAYE deducted from the salary (not including ACC earners' levy)	\$ 16,660
Estimated RIT for 2020	<u>\$ 56,298</u>

Hiwi's 2020 provisional tax is \$56,298 to be paid in three instalments on:

28 August 2019	\$ 18,766
15 January 2020	\$ 18,766
7 May 2020	\$ 18,766
	<u>\$ 56,298</u>

Underestimating your provisional tax

It pays to keep a close watch on your profits because you could be charged a penalty if your provisional tax estimation is unreasonably low, compared with your actual RIT once you file your return.

You'll need to tell us how much residual income tax you expect to pay. You can estimate:

- using the Estimate provisional tax service in myIR
- sending a secure mail in myIR
- by calling us
- by writing to us.

You may have to pay a penalty if you underestimate your provisional tax.

You can estimate your residual income tax as many times as you like up until your final instalment due date.

If you do re-estimate, you'll need to adjust later instalments to take into account any earlier under or overpayments.

Example

In February 2020, Hiwi realises his year is going better than he first thought. He re-estimates his 2020 provisional tax to \$65,000.

So far, he's paid two instalments:

28 August 2019	\$18,766
15 January 2020	\$18,766

His new estimate means these instalments are now too low. Hiwi's final instalment must cover this underpayment. His new calculation is:

Re-estimated provisional tax	\$65,000
Less instalments already paid	\$18,766
	<u>\$18,766</u>
	\$37,532
	<u>\$27,468</u>

Hiwi's final instalment, due 7 May 2020, is \$27,468.

The ratio option

This option can suit people whose income tends to go up and down during the year. You calculate your provisional tax by applying a ratio percentage to the taxable supplies in your GST returns so your provisional tax instalments align with your business cashflow.

We calculate your ratio percentage by dividing your RIT for the last tax year by your total GST taxable supplies for the same year. If your last year's figures are not available, we base the ratio on the RIT and total GST taxable figures from the previous year.

Changing options

Once you've selected the estimation option, you cannot change to the standard option during the same year.

The ratio option may be helpful if you have seasonal income.

When your provisional tax is due

Using the ratio option, you pay six instalments of provisional tax a year. If you have a 31 March balance date, your due dates are 28 June, 28 August, 28 October, 15 January, 28 February, and 7 May.

Qualifying for the ratio option

The ratio option is useful if your income varies or you have seasonal income. You must meet all these criteria to use it:

- You've been in business and registered for GST, for the whole of the previous tax year, and part of the tax year before that.
- Your residual income tax (RIT) for the previous year is greater than \$5,000 (\$2,500 in 2019/20 and earlier years)
- You file your GST returns monthly or 2-monthly.
- You're not a partnership.
- Your ratio percentage that we calculate for you is between 0 and 100% (we'll let you know if it's not).

The ratio percentage

You must let us know before the start of the tax year if you decide to use the ratio option. We'll calculate the ratio percentage for you, using information from your income tax and GST returns.

$$\text{GST ratio percentage} = \frac{\text{RIT from your latest income tax return}}{\text{total GST taxable supplies from the same tax year (less ratio percentage adjustments - see page 19)}} \times \frac{100}{1}$$

Only provisional tax payers registered for GST who file one-monthly or two-monthly returns can use the ratio option.

The ratio percentage will only work if your returns are up to date. We cannot calculate a ratio percentage using returns from a tax year more than two years earlier than the provisional tax year.

Example

Leonie is a kiwifruit grower in Te Puke. She files two monthly GST returns. On 20 February 2019, she applies to use the ratio option to work out her 2020 provisional tax. We approve this and review her latest returns, which are for the 2018 year. Her 2018 RIT is \$51,000, and her taxable supplies are \$2,114,723, broken down as follows:

GST return period	Taxable supplies (\$)
April - May 2017	690,025
June - July 2017	580,121
August - September 2017	145,859
October - November 2017	90,412
December 2017 - January 2018	152,681
February - March 2018	455,625
Total taxable supplies	\$2,114,723

Leonie's ratio percentage is: $\frac{\$51,000}{\$2,114,723} \times \frac{100}{1} = 2.4\%^*$

*Your ratio percentage is rounded down to one decimal place.

Calculating your provisional tax

We'll tell you your ratio percentage. Calculate your provisional tax instalments, following the steps on the back of your GST return.

You work out each instalment by applying the ratio percentage to the taxable supplies in each GST return (two-monthly filers) or every second GST return (one-monthly filers).

Leonie has approval to work out her 2019 provisional tax using a ratio percentage of 2.4%. She can now do the calculations.

GST return period	Taxable supplies (\$)	Ratio percentage	Provisional tax instalment (\$)	Payment and GST return due
April - May 2019	725,111	2.4%	17,402.66	28 June 2019
June - July 2019	625,456	2.4%	15,010.94	28 August 2019
Aug - Sept 2019	102,612	2.4%	2,462.68	28 October 2019
Oct - Nov 2019	72,558	2.4%	1,741.39	15 January 2020
Dec 2019 - Jan 2020	298,386	2.4%	7,161.26	28 Feb 2020
Feb - Mar 2020	422,899	2.4%	10,149.57	7 May 2020

Updating your ratio percentage

After you file an income tax return, we'll update your ratio percentage to match your income and tell you what it is. You can start using your new ratio percentage 30 days from the date of our letter.

Adjusting your ratio percentage

If you sell a fixed asset, you can ask us to adjust your ratio percentage. Enter your details under "Provisional tax" on the back of your GST return.

Because we treat sales of fixed assets differently in income tax and GST returns, you may pay too much provisional tax if your ratio percentage is not adjusted.

The value of the fixed asset you're selling must be the same or more than:

- \$1,000, or
- 5% of your total taxable supplies for the previous 12 months.

We'll use the larger amount.

A fixed asset is an item owned by the business that will generally be used in the business for more than a year, and is not for sale to customers, eg, buildings, vans, equipment.

Ceasing the ratio option

You can stop using the ratio option at any time. You just need to let us know by phone or email.

If you stop using it before the first payment due date, you can choose to use the standard or estimation option to calculate. The usual use of money interest rules will apply from this time.

If you stop using it after the first payment date, you must use the estimation option to calculate for the rest of the year.

You must stop using the ratio option if:

- you cease your GST registration
- any of your GST returns are overdue by 60 days or more
- your ratio percentage change is no longer between 0% and 100% (we'll let you know if it's not)
- you change your GST filing frequency to 6-monthly
- a return of income is filed or amended where the residual income tax is calculated at below \$5,000 (\$2,500 in 2019/20 and earlier years) or above \$150,000.

Penalties

We charge penalties on late or underpaid instalments of provisional tax.

When you make a payment, it will be applied to the earliest unpaid provisional tax instalments. Provisional tax amounts include any late payment penalties charged.

Late payment penalties

We charge late payment penalties (LPPs) on all overdue payments.

We charge the penalties in two stages. This means that the longer a payment remains overdue, the more penalties we'll add.

The stages are:

- 1% the day after the due date, and
- 4% seven days later.

We can stop some late payment penalties being added to your account if you set up a plan with us to pay your tax.

We charge penalties on late payments.

Example

Anthony had to pay provisional tax of \$7,600 on 7 May for the 2019 income year. He paid it on 10 July, over two months late. LPPs were added as follows:

Date	Amount owing (\$)	LPP	LPP added (\$)	New amount owing (\$)
8 May 2019	7,600.00	1%	76.00	7,676.00
14 May 2019	7,676.00	4%	307.04	7,983.04
Total			383.04	

Shortfall penalties

We may charge a shortfall penalty if you use the AIM or estimation options to calculate your provisional tax and your provisional tax is unreasonably low. We compare the provisional tax you paid to the RIT you calculate when you file your tax return, and apply the penalty to the underpaid amount. The amount of the shortfall penalty depends on the seriousness of the mistake.

Mistake	Shortfall penalty
Not taking reasonable care	20%
Unacceptable tax position	20%
Gross carelessness	40%
Abusive tax position	100%
Evasion	150%

When you need to pay your penalties

You must pay any penalties as soon as you get them. You must also pay any overdue provisional tax at the same time.

You cannot claim a deduction in your income tax or GST returns for any penalties you pay Inland Revenue.

Interest on provisional tax

We may charge interest for end-of-year tax paid late or unpaid end-of-year tax and provisional tax (see "Paying and receiving interest" below). Interest is a charge for the use of money. This means we may pay you interest if you overpay your provisional tax.

We calculate interest when you file your income tax return. We compare your RIT to the provisional tax you've paid. You may have to pay interest even if you've paid your instalments in full and on time, or if you did not have to pay provisional tax.

Interest is not a penalty
- it's a charge for the use
of money.

Paying and receiving interest

Not everyone will pay interest on underpaid provisional tax. And not everyone will receive interest if they've overpaid their provisional tax.

We'll calculate interest for:

- individuals and non-individuals who used the standard option, with RIT
- \$60,000 or more from the final instalment date.
- Individuals and non-individuals with RIT of less \$60,000 if payment not made by the terminal tax due date
- anyone who used the estimation option, with RIT over \$5,000
- anyone who chooses to use the AIM option but does not pay the provisional tax instalments their AIM-capable accounting software tells them to pay by the instalment date
- anyone whose RIT is \$5,000 or less who chose to be a provisional tax payer (individuals also need to have used the estimation option) - see "Choosing to be a provisional tax payer" on page 27.)
- IRD number on the online RWT exemption register.

Anyone choosing to be a provisional taxpayer has to use the estimation option.

We will not charge interest if the underpaid or overpaid tax is \$100 or less.

There is no change to debit or credit use-of-money interest when using the estimation option instalment(s) other than at the final instalment.

When using the standard option the start date of UOMI depends on your RIT (when all required payments are made in full and on time).

Provisional tax amount	End of year residual income tax (RIT)	Credit or debit UOMI	Calculated from
More than RIT amount	Less than \$60,000	Credit UOMI calculated on the difference between the provisional tax amount paid and the RIT	Terminal tax due date
More than RIT	\$60,000 or more	Credit UOMI calculated on the difference between the provisional tax amount paid and the RIT	Last instalment date
Less than RIT	\$60,000 or more	Debit UOMI calculated on the difference between the provisional tax amount paid and the RIT	Last instalment date
Less than RIT	Less than \$60,000	Debit UOMI calculated on the difference between the provisional tax amount paid and the RIT	Terminal tax due date

If you've paid all but your final instalment in full and on time using the standard option then UOMI will apply from the last instalment due date.

If you pay an instalment late or do not pay it at all, UOMI will be charged from the due date of the instalment on the lesser of:

- the amount of the instalment that was paid less the amount that should have paid, or
- your RIT divided by the number of instalments for the tax year less the amount paid.

If the previous year's return was not filed on or before a provisional tax due date, and you have an extension of time, the amount that should have been paid for that instalment will be the lesser of the 10% uplift amount (based on two years prior) or the 5% uplift amount (based on the previous year). This does not apply to the final instalment.

The above changes may not apply if:

- you're associated to specific persons or entities with one of you being a company and they are not covered by the above standard option rules or they do not use the GST ratio option, or
- you've entered an avoidance arrangement.

For interest under the AIM option refer to page 27.

How we calculate interest

We use this formula to calculate interest on provisional tax:

$$\frac{t \times r}{365} \times d$$

Where:

t = the underpaid or overpaid tax (including LPPs)

r = the current interest rate

d = the number of days where interest applies.

Different rates of interest apply to underpaid and overpaid tax. Interest rates change frequently.

We count both the first day that interest starts and the last day interest is payable when we calculate the number of days interest applies.

When you need to pay your interest

If we charge interest, you need to pay it by 7 February (or 7 April if you have a tax agent with an extension of time). Because interest is charged daily, you may want to pay before the due date. The longer you leave it, the more you'll pay.

The longer you leave it,
the more you'll pay.

You can claim a deduction in your income tax return for the amount you paid. If we pay you interest, you need to include it as income.

Interest is GST exempt, so you do not include interest (paid or received) in your GST returns.

Example

Example ABC Ltd is a construction firm. Karen, the finance manager, used the standard option to calculate provisional tax of \$24,000 for the 2019 tax year.

Instalments were due on:

28 August 2018	\$8,000
15 January 2019	\$8,000
7 May 2019	<u>\$8,000</u>
	\$24,000

The company only paid the first instalment on time. When Karen filed the company's 2019 tax return on 7 July 2019, she calculated RIT of \$38,400. The company had a total of \$30,400 still to pay.

Because the RIT was more than \$2,500 and the company did not pay all provisional tax instalments on time, the company had to pay interest.

We identify the lesser of the difference between the amount paid and:

the provisional tax assessed for each instalment, \$8,000 and the actual RIT payable for each instalment, $\$38,400 \div 3 = \$12,800$.

Instalment No.	Amount paid	Prov tax assessed	RIT instalment	Shortfall (lesser of)
1st	\$8,000	\$8,000	\$12,800	
2nd	\$0	\$8,000	\$12,800	\$8,000
3rd	\$0	\$8,000	\$12,800	\$8,000

Karen got the balance from her myIR secure online services account on 9 September 2019 and paid the end-of-year tax and interest right away. We calculated the interest at a rate of 9.21% to 7 May 2019 and then 8.27% after this:

Days interest applied	Amount interest calculated on (\$)	Interest calculation	Interest charged (\$)
16 Jan 2019 - 7 May 2019 (112 days)	\$8,000	$\$8,000 \times 0.0921 \times 112 \div 365$	\$ 226.08
8 May 2019 - 9 Sept 2019 (125 days)	\$8,000 + \$8,000	$\$16,000 \times 0.0827 \times 125 \div 365$	\$453.15
Total interest payable			\$679.23

Late payment penalty

2nd instalment

Initial penalty	16 January 2019	$\$8,000 \times 1\%$	=	\$ 80	
Further penalty	22 January 2019	$\$8,000 \times 4\%$	=	\$320	\$400.00

3rd instalment

Initial penalty	8 May 2019	$\$8,000 \times 1\%$	=	\$ 80	
Further penalty	14 May 2019	$\$8,000 \times 4\%$	=	\$320	\$400.00

Total late payment penalties **\$800.00**

Points to note from the example

- Karen's total payment of \$31,079.23 was made up of \$16,000 unpaid provisional tax, \$14,400 end-of-year tax and \$679.23 interest.
- The underpaid provisional tax was payable straight away.
- Interest was charged on the lesser of the difference between
 - the amount paid and the provisional tax assessed, and
 - the amount paid and the RIT instalment amount.
- Karen had until 7 February 2020 to pay the end-of-year tax, but she wanted to pay it early to avoid further interest.
- We charged late payment penalties, because Karen did not pay the second and third provisional tax instalments in full and on time.
- We charged interest because ABC Ltd had the use of the difference between the provisional tax due and the amount paid over the period 16 January 2019 - 9 September 2019.

Interest and the AIM option

You will not pay (or receive) interest on any of your provisional tax instalments if you use the AIM option as long as you make your payments in full and on time.

If the amount of a provisional tax instalment calculated by your AIM-capable accounting software is not paid on time, penalties and interest will apply to the underpayment. These will continue to apply until you make a payment.

Interest and the ratio option

You will not pay (or receive) interest on any of your provisional tax instalments if you use the ratio option for the full year.

But, we'll charge interest if you owe more than \$100 after your end-of-year tax due date (7 February, or 7 April if you have a tax agent with an extension of time).

Late payment penalties will apply to instalments paid late or not paid in full.

Choosing to be a provisional tax payer

You can choose to be a provisional tax payer if you're in this situation:

- your RIT works out to be \$5,000 or less (\$2,500 for 2019/20 and earlier years)
- you've made provisional payments of more than \$5,000
- you had a reasonable expectation, on the day you made your first payment, that you would have to pay provisional tax.

Talk to your tax agent first.

Then let us know when you file your tax return if you want to be treated as a provisional tax payer for the year.

We may calculate interest on your voluntary payments.

Individuals will need to estimate their provisional tax on or before their third instalment date to have interest calculated.

We can help if you're finding it hard to pay

Penalty and interest charges can increase your provisional tax payments quite quickly, so you'll save money if you pay your instalments in full and on time.

If you cannot pay, call us as soon as you can - before the due date, if possible. We'll work with you to develop a solution that takes into account your personal circumstances.

Do not let your debt get out of hand. Talk to us straight away.

You can pay your instalments electronically, by credit or debit card.

Find all the details of our payment options at **ird.govt.nz/pay**

Your first year in business

Your first year in business is not tax-free.

You'll need to file an income tax return at the end of your first year and pay tax on your net profit. You will not have to pay provisional tax during your first year in business unless your previous year's RIT was \$5,000 (\$2,500 for 2020 and earlier income years).

But, you can make voluntary payments of provisional tax. In your second year you may have to pay end-of-year tax for your first year, on top of provisional tax instalments for your second year. Your end-of-year tax could be a significant amount if you do not have any voluntary payments to deduct.

Voluntary payments will help if you need to pay interest, and may entitle you to an early payment discount.

Example

Isobel started her own business in October 2018. In June 2019, she sent in her first income tax return, for the year ended 31 March 2019. Her RIT (which is also her end-of-year tax) was \$75,000. Isobel used the standard option to work out her 2020 provisional tax of \$78,750.

RIT	\$75,000
Plus 5%	\$ 3,750
2020 provisional tax	\$78,750

Isobel's due dates and payments are:

Due date	Tax to pay	Amount
28 August 2019	2020 provisional tax	\$26,250
15 January 2020	2020 provisional tax	\$26,250
7 February 2020	2019 end-of-year tax	\$75,000
7 May 2020	2020 provisional tax	\$26,250

Because she made no voluntary payments for 2019 income tax, Isobel must pay her \$75,000 end-of-year tax as well as her \$78,750 2020 provisional tax during her second year in business.

Voluntary payments can help your cash flow.

You can opt into the Accounting Income Method (AIM) in your first year of business by sending us your first Statement of activity with your AIM capable software. By using AIM, you'll only pay provisional tax when you make a profit and your end-of-year-tax will be closer aligned. Find out more about AIM on page 6.

Early payment discount

In your first year in business, you could qualify for a discount of 6.7% if you make voluntary tax payments during the tax year before you need to pay provisional tax.

Individuals and partners in a partnership can claim the discount, but companies, trusts and other forms of business organisations do not qualify.

You can get the discount if you meet these conditions:

- Your income comes mainly from a business (not interest, dividends, royalties, rents or beneficiary income).
- You're not required to pay provisional tax during the year you make the voluntary payments, or for any of the prior four years.
- You make the voluntary payments on or before the end of your tax year.
- You apply for the discount on or before the date your tax return must be filed (tick the box in the return).

The discount is 6.7% of either:

- the total amount of your voluntary payments
- 105% of your RIT for that year.

We'll use the smaller amount.

The early payment discount is treated as a payment towards your RIT.

Further early payment discounts

You can receive another early payment discount in another year if:

- you have not had to pay provisional tax in any of the previous four tax years, and
- you have not had any business income in the four-year period since you last paid provisional tax or claimed the discount.

You may get a discount if you make voluntary payments.

New provisional tax payers

The rules may apply differently if you're a "new provisional tax payer". We may charge interest on a reduced number of instalments.

If you're an **individual**, we consider you're a new provisional tax payer if:

- your RIT for the current tax year is \$60,000 or more
- your RIT was \$5,000 (\$2,500 in 2019/20 and earlier years) or less in each of the four previous years, and
- during the current year, you stopped receiving income from employment and you then started to receive income from a taxable activity.

If you're a **non-individual** (eg, a company or a trust), the conditions are as follows:

- your RIT for the current tax year is \$60,000 or more
- you did not receive income from a taxable activity in any of the four previous years, and
- you started receiving income from a taxable activity during the current year.

Number of instalments

As a new provisional tax payer, you'll pay or receive interest on one to three provisional tax instalments, based on the date you started your taxable activity.

Taxable activity starts	Number of instalments
Before 29 July	3
On or after 29 July but before 16 December	2
On 16 December, or any time after that	1

You'll have different dates if you have a balance date other than 31 March, or you file six-monthly GST returns. Talk to us or your tax agent if you need more information.

Budgeting for your provisional tax

You need to know how much your provisional tax instalments are, and when you need to pay them.

A basic budgeting principle is to put aside some money each month so you can be ready when the due date rolls around.

It's important to budget for your provisional tax when you first start out in business because you may have to pay your first year's end-of-year tax bill during your second year, when you'll also have provisional instalments to pay. See page 29 for more information.

Budgeting will help you meet your deadlines - especially when you start out in business.

Terms we use

AIM capable accounting tax software.	Software provided by an approved AIM provider which calculates your provisional tax payments based on your accounting income for the period and year to date.
AIM option	A method of calculating your provisional tax based on your accounting income so you can make payments of provisional tax for the periods in which you have the cash to pay. You use approved AIM-capable software.
Approved AIM provider software	Software provider approved by Inland Revenue to provide AIM - provider.
Statement of activity	Set of information collated by AIM-capable accounting software and electronically submitted to Inland Revenue for each provisional tax instalment date when the AIM option is being used.
ACC earners' levy	Money paid by employees and self-employed people to ACC, to help cover the costs of non-work personal injuries.
Balance date	The last day of your income year.
Due date	The last day to file a return or make a payment.
Early payment discount	A reduction in your end-of-year tax when you pay provisional tax early.
End-of-year tax	The difference between the residual income tax and the provisional tax paid.
Extension of time	Inland Revenue allows you more time to file your income tax return.
Extension of time arrangement	Approval for a tax agent to file a client's return after the normal due date (7 July if you have a 31 March balance date).

Estimation option	A method of calculating your provisional tax, based on your estimation of what the current years residual income tax might be.
Fixed asset	An item owned by the business that will generally be used in the business for more than a year, and is not for sale to customers, eg, buildings, vans, equipment.
GST (goods and services tax)	A tax added to the sale price of most goods and services.
Income tax	A tax on income earned over the tax year.
Instalment plan	An agreement we make with you to pay your tax bill, either at a later date or in regular payments over time.
Interest	Money we charge on late or underpaid tax, or pay you for overpaid tax.
Late payment penalty (LPP)	May be charged on late-paid and underpaid instalments of provisional tax.
New provisional tax payer	Someone who starts earning income from a taxable activity during the year.
PAYE (pay-as-you-earn)	A combination of income tax and ACC earners' levy, deducted from an employee's salary or wages by an employer and paid to Inland Revenue.
Penalty	Money Inland Revenue charges when you do not keep to your tax obligations.
Provisional tax	Income tax paid as instalments during the year.
Ratio option	A method of accounting for provisional tax as you pay your GST.

Residual income tax (RIT)	The tax payable on your taxable income, less PAYE and any other income tax credits you may be entitled to (it does not include any provisional tax payments, voluntary payments, or any Working for Families Tax Credits).
Shortfall penalty	A charge for making an unreasonably low estimation.
Standard option	A method of calculating your provisional tax, based on your previous year's RIT plus 5% or 10%.
Tax agent	A person who manages your taxes on your behalf.
Tax credit	Covers tax that has been deducted or paid at source such as RWT deducted from interest or an entitlement you can deduct from your income tax, eg. the independent earner tax credit.
Tax year	1 April to 31 March.
Taxable income	The income you declare in your income tax return, after all allowable deductions and any losses brought forward.
Transitional year	The first year you start using a new balance date. You will need to calculate provisional tax differently for your transitional year.

How to contact Inland Revenue

How to get our forms and guides

You can get copies of our forms and guides at ird.govt.nz/forms-guides

Need to speak with us?

Have your IRD number ready and call us on one of these numbers.

General tax, tax credits and refunds	0800 775 247
Employer enquiries	0800 377 772
General business tax	0800 377 774
Overdue returns and payments	0800 377 771

We're open 8am to 8pm Monday to Friday, and 9am to 1pm Saturday. We record all calls.

Our self-service lines are open 7 days a week - except between 5am and 6am each day. They offer a range of automated options, especially if you're enrolled with voice ID.

Find out more at ird.govt.nz/contact-us

Privacy

Meeting your tax obligations means giving us accurate information so we can assess your tax and entitlements under the Acts we administer. We may charge penalties if you do not.

We may also exchange information about you with:

- some government agencies
- another country, if we have an information supply agreement with them, and
- Statistics New Zealand (for statistical purposes only).

You can ask for the personal information we hold about you. We'll give the information to you and correct any errors, unless we have a lawful reason not to. Find our full privacy policy at ird.govt.nz/privacy

Inland Revenue's services

myIR

Manage all your Inland Revenue matters securely online with a myIR account. Go to ird.govt.nz/myIR to find out more.

ird.govt.nz

Go to our website for information and to use our services and tools.

Follow us on Twitter

Follow [@NZInlandRevenue](https://twitter.com/NZInlandRevenue) for tweets on tax and social policy matters, including media releases, due dates and consultations.

Business Tax Update

Our Business Tax Update newsletter gives you updates on PAYE, GST, FBT and other relevant tax issues. Subscribe at ird.govt.nz/subscribebtu and we'll send you an email when we publish each issue.

Language Assistance – Ezispeak

When calling you can ask for a Language Assistance interpreter.

Language Assistance - Ezispeak is a free phone-based interpreter service for customers whose first or preferred language is not English.

There are 180+ languages available – go to www.ezispeak.nz/languages-we-speak/ for the full list.