Should I Set up My Business as a Look Through Company (LTC)?[1]

If you are a business owner or property investor, setting up a Look Through Company (LTC) enables you to transfer business profits and losses to your personal income. By doing this, you could pay less tax.

LTC for the Rental Property Investor

If you own one or more investment properties, setting up an LTC could save you money. This is because an LTC structure will allow you to transfer profits and losses from these properties to your personal income. When you offset any losses you make from your investment properties, against income you have earned from other sources, the rate of tax you pay can be reduced, saving you money.

LTC for the Small Business Owner

If you are a small business owner, setting up a Look Through Company could give you the benefit of lower tax rates, while you still enjoy the benefits of limited liability.

As the owner of a small business, you would need to earn close to $180,000 per year before your average income tax rate would exceed the company tax rate of 28 percent. So if you expect to be earning less than $180,000, setting up as an LTC could be your best option.

In addition to this, if you have set up a Look Through Company, the net profit or loss from your business will be shared by all the owners (shareholders) of the business, in proportion to their shareholding. While the LTC must still complete an income tax return (IR7), which includes a summary of the income and deductions attributable to each owner, the company itself isn't taxed. Instead, each owner is responsible for declaring their portion of the LTC's net profit or loss on their own income tax return.[2]

In this way, it is possible to reduce the total tax paid on behalf of the Look Through Company, by distributing the LTC's earnings amongst all its owners. This could enable each owner (for example, a husband and wife) to remain within a lower tax bracket for their total taxable income.

1 Information adapted chiefly from the Inland Revenue Department's guide, IR879 Look-through companies, dated May 2014.

2 For example, Charles holds 60% of the shares in Walnut Ltd and his wife Caroline holds the other 40%. Walnut Ltd's net profit for the year was $50,000. So in their individual tax returns for the year, Charles will declare business income from an LTC of $30,000 (60% of $50,000) and his wife Caroline will declare $20,000 (40% of $50,000).

LTCs Still Have Responsibilities

An LTC continues to be responsible as a company for its tax obligations under the:

- PAYE rules
- FBT rules
- RWT and NRWT rules
- RSCT and ESCT rules
- company amalgamation rules, and
- other tax Acts, e.g. GST.

This means, for example, that the LTC must still complete an income tax return (IR7), GST returns, company returns, employer monthly schedules, etc.

Who Can Become an LTC?

An LTC must satisfy a number of criteria for the whole of the income year, including:

- It must be a company
- The company must be a New Zealand tax resident
- Shareholders in an LTC must either be natural persons, trustees or another LTC
- It must not have more than five “look-through counted owners”[3]
- A company using the LTC rules must only have one class of shares with the same voting rights
- It must not be a flat-owning company.

Electing to Become an LTC

You can elect for your company to become an LTC by completing a Look-through company election (IR862) form, available on the IRD website. All owners of a look-through interest in the LTC at the date of election must sign the form. Otherwise, it won’t be valid.

New companies – A company can become an LTC from its incorporation date, provided it elects to do this by the due date for its first income tax return.

Existing companies – The effective LTC election date for companies that have previously traded will be from the start of the income year following the date they file the election. For example, a company with a standard balance date needs to make its election by 31 March 2016 to become an LTC for the 2016–17 income year.

3 See the Inland Revenue Department's guide, IR879 Look-through companies, for an explanation of “look-through counted owners”.

4 This disclaimer was created using an SEQ Legal template.