Hon Peter Dunne

Minister of Revenue

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Multinational investors – paying fair share of tax

Changes to the thin capitalisation rules will help ensure multinational companies investing in New Zealand pay their fair share of tax, Revenue Minister Peter Dunne says.

The changes flow from an issues paper released earlier this year.

“New Zealand welcomes foreign investors, but we expect everyone participating in the New Zealand economy to contribute their share of tax,” Mr Dunne says.

The thin capitalisation rules are designed to address the situation where non-resident investors can artificially load debt into their New Zealand investments to limit their tax exposure, so limiting interest deductions for foreign-owned firms.

However, they currently apply only where one non-resident owns 50 per cent or more of a New Zealand investment. This means that the rules apply to traditional multinational companies, but not to other types of non-resident investors, such as private equity investors.

“If other types of investors have the ability to take excessive interest deductions which reduce their tax liability, then that is not fair. The thin capitalisation rules should apply,” Mr Dunne says.

The Government has therefore decided to extend these rules to where non-residents are acting together, and together have a controlling interest of a New Zealand investment. This change is expected to generate $20 million over three years from 2014/15.

Another area of concern is around the issue of shareholder debt, which can allow companies operating in New Zealand to have excessive levels of debt without the thin capitalisation rules applying.

“This defeats the intent of the rules, so we have decided shareholder debt should be excluded from the worldwide group safe harbour debt calculations.

“And this also means that groups with high levels of external debt should not be affected by these changes.

“Some technical issues still need to be resolved, including defining the ‘acting together’ test and making sure that extending the application of the rules to trusts does not inadvertently affect benign structures, Mr Dunne says.

“My officials will continue to work with interested parties to ensure the legislation works in practice.”

Legislation for the changes is expected to be introduced later this year, and the changes will apply from the start of the 2015/16 income year.

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Fact sheet – thin capitalisation changes

The thin capitalisation rules form part of New Zealand's international tax rules that protect our tax base. Debt incurred in earning income can be used to offset income, thereby reducing tax liability. The thin capitalisation rules are designed to address the situation where non-resident investors can artificially load debt into their New Zealand investments in order to limit their tax exposure.

What is changing?

- The thin capitalisation rules currently apply only when a single non-resident owns 50 per cent or more of a New Zealand investment. The rules are being extended so they will also apply when a group of non-resident taxpayers are acting together and collectively own 50 per cent or more of a New Zealand investment.

- Shareholder debt will also be excluded from a company's worldwide group safe harbour debt calculations. This will help to discourage shareholders from recharacterising dividends into interest, but it will also make sure the thin cap rules do not impact businesses with high levels of genuine third-party debt.

- These changes follow an officials' issues paper that was released in January this year with proposals to tighten the thin capitalisation rules.

- Some technical details of these changes, such as what constitutes acting together, are still being worked through. Additionally, decisions have not yet been made on the other issues discussed in the issues paper. Officials are working with interested parties to ensure that the resulting legislation effectively targets the areas of most concern, but does not impact benign business structures.

- These changes will be included in a bill later in the year and will apply from the beginning of the 2015/16 year.

Why are these changes being made?

These changes to the thin capitalisation rules respond to techniques and structures that can defeat the intention of the rules. The changes will help ensure the thin capitalisation rules continue to protect New Zealand's tax base.