

# **Income Tax Bill**

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*Commentary on the Bill*

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# CHAPTER 1

## Introduction

The task of rewriting the Income Tax Act has been undertaken in four stages. The first stage was the reorganisation of the Income Tax Act 1976, which resulted in the enactment of the Income Tax Act 1994. The second stage, the rewrite of the core provisions of the Act, was completed in 1996. The third stage involved the rewrite of Parts C to E of the Act, which was completed in 2004. This bill represents the fourth and final stage, and it rewrites Parts F to the end of the Act.

The key aim of the rewrite project is to reduce compliance costs by producing tax legislation that is clear, uses plain language and is structurally consistent. Clear legislation makes an important contribution to increasing voluntary compliance with tax laws because it makes it easier for readers to identify and observe their income tax obligations.

The objective is to make the legislation clear while minimising changes to the effect of the legislation and associated compliance requirements of the current Act. The bill also introduces a small number of intended changes to the legislation, all of which have been presented for public consultation in recent years. They are discussed in chapter 3.

The bill rewrites Parts F, G, H, I, K, L, M, N, O, Y and the schedules to the Act. It also consolidates the Income Tax (Withholding Payments) Regulations 1979 into the Income Tax Act. Some provisions in Part B, which relate to Parts I and L, are also consequentially amended.

The bill re-enacts and consolidates, but does not rewrite (except for limited consequential changes), Parts A, C, D and E. It also renumbers various sections within Parts C, D and E as a result of:

- new provisions enacted since the 2004 Act came into force; and
- the movement into these Parts of income, deduction and allocation rules from other areas of the Act.

The new Act is to apply to income derived in the 2008-09 and later income years.

A careful process was adopted in the development of the bill to ensure that its provisions have the same outcomes as those of the current Act, except in those few cases when a change is intended. The government has indicated that it will promote a remedial amendment to correct any provision in the new Act which is found to produce a different result from that which would have been produced under the 2004 Act, provided no change was intended. That remedial change would apply from the date of effect of the new legislation.

The re-enactment of the Act is for the benefit of users. The options for the bill were to:

- amend the current Act by replacing Parts F to end of the Act with rewritten Parts; or
- produce a new Act containing rewritten Parts F to the end of the Act, including the schedules and consolidated parts A to E.

The second option was chosen and is supported by the Rewrite Advisory Panel. The main benefit of adopting this option is that it minimises confusion over the numbering of sections

For example, the differences between the two options can be compared by reference to section FC 1 of the 2004 Act. This section is about the tax treatment of profit-related debentures. In the bill, the subject matter of clause FC 1 is quite different from the content of section FC 1 of the Act. Clause FC 1 of the bill describes the operation of subpart FC, which is about the income tax treatment of transfers of certain property on death. Therefore:

- If the option to amend the 2004 Act was preferred, readers would have needed to distinguish between two provisions bearing the same reference in the 2004 Act. For example, in referring to section FC 1 of the Income Tax Act 2004, the reader would need to make it clear whether the reference is to section FC 1 of the Act before it was amended or section FC 1 of the Act as inserted by the amendment.
- Under the option of a new Income Tax Act, readers can identify the provision as section FC 1 of the Income Tax Act 2004 or section FA 2 of the Income Tax Act 2006.

## CHAPTER 2

### Structure of the new Act

This chapter sets out the approach that has been taken to the structure and organisation of the legislation, based on the broad role of each part.

As a result of clarifying the role for each of these Parts, a number of provisions have been moved to and from the various Parts. This movement of provisions was set out in the exposure draft of legislation for each part that was released for public consultation.

Parts A to E are being re-enacted, although some consequential amendments are required in subpart BC and in a limited number of other places. As well, Parts C to E have been renumbered as a result of insertions in the Act since it came into force in 2004, and the movement of provisions from other parts of the Act.

Parts F to Z contain a variety of rules:

- Part F deals with the taxation treatment of certain transactions or arrangements.
- Part G is concerned with avoidance issues.
- Part H deals with the taxation treatment of certain types of entities.
- Part I deals with the carrying forward and use of tax losses.
- Part L contains the rules defining when tax credits arise, the amount of the tax credit a person has, and when and how a tax credit is used.
- Part M deals with tax credits for families.
- Part O deals with the memorandum account rules, which identify amounts of tax or other payments that are linked to the tax credit system.
- Part R sets out the rules stipulating how all taxes and other payment obligations are calculated and the time at which they are satisfied.
- Part Y contains the definitions for the Act.
- Part Z contains transitional rules.

The general structural principles adopted in the rewritten legislation are:

- Organising the legislation from the most generally applicable Part to the more specifically applicable Parts. Each Part, subpart, and (in some cases) section generally begins with more widely applicable rules and concludes with the rules having more specific application.
- Using general rules to perform a pivotal role.
- Using general rules to overarch more specific rules, with the tax loss rules presented in subpart IA of the bill being an example. This approach helps users to identify the inter-relationships between the provisions and any common policy intent.

- Minimising overlap, to make the categories used to group items as self-contained as possible.
- Grouping like with like. Functions or subject matter that are the same have been grouped together to assist the reader.
- Reducing repetition to minimise duplication. Applying common sets of rules is one technique that has been used to achieve this.
- Using a consistent format. This aids accessibility by improving the flow of the text.
- Linking the Parts back to the core provisions.
- Placing terminating provisions into a separate subpart at the end of each part. This is a continuation from the current Act, although the contents of the “Z” subparts have been culled because many of the provisions are either spent or are unlikely to have future relevance. Omitting these provisions does not remove their application to relevant past situations, but it does reduce the size of the Act.
- Leaving “gaps” between Parts and subparts to facilitate future drafting. This occurs throughout Parts F to R. For example, in part F, subpart FC is followed by subpart FE, and in part I, subpart IA is followed by subpart IC. These gaps reserve subpart numbers for future drafting to help overcome or at least defer the three-letter numbering of subparts (and potentially two-letter numbering of Parts) that has been necessary in recently enacted policy measures. Examples of this are the PAYE and RWT intermediary rules, which were inserted in the 2004 Act as subparts NBA and NBB.

The following overview of each Part lists subparts as they are presented in the bill, and gaps in the numbering represent subpart numbering reserved for future drafting.

### **Part F of the bill**

Part F of the 2004 Act contains a range of provisions, including:

- apportionment rules for cross-border transactions;
- modifications to the interest deductibility rules for certain types of debentures and, under the thin capitalisation rules, some foreign-owned organisations and banks;
- rules for consolidated companies when calculating their income tax liability for a tax year;
- rules for determining how groups of companies use imputation credits; and
- modification of the tax treatment of certain transfers of property and financial arrangements under a relationship agreement or upon death.

Part F contains provisions that modify the calculation of taxable income for a tax year for persons entering into certain arrangements or transactions. A rule in Part F will generally lead to a taxation effect that is different from that which would be produced under Parts C to E if this rule did not exist.

However, many of the apportionment provisions in Part F of the 2004 Act have been moved closer to their relevant provisions. This reflects the more specific role of Part F in the new Act. Two examples of apportionment rules in the 2004 Act moved to a different location in the bill are:

- Section FB 2, which contains an apportionment rule for tax credits for foreign income tax and a source rule. The apportionment rule for tax credits has been moved to subpart YD (Residence and source in New Zealand).
- Section FB 7, which is an apportionment rule relating to depreciation, has been moved to subpart EE, making this rule easier to access.

The thin capitalisation rules, which restrict the amount of interest allowed as a deduction, are an example of the apportionment rules that have been retained within Part F. The complexity and detail of these rules has led to their retention within that Part, rather than moving them to Parts C and D and cluttering their structure.

The rules relating to consolidated groups of companies are located in more than one place in the 2004 Act. Some of these rules have been moved to Part F and consolidated together in subpart FM to provide easier access.

Subpart FA contains rules that alter the tax treatment of certain commercial arrangements by either recharacterising the nature of (or amounts derived under) the arrangement or by providing a different form of tax treatment for the parties to the arrangement.

- Section FA 2 is an example of a rule that recharacterises the nature of the arrangement by treating a debenture as shares for income tax purposes.
- Section FA 5 is an example of a rule that alters the tax treatment of the party to the transaction. This rule is intended to claw back deductions for lease payments that are effectively payments of the purchase price of the lease asset. This rule applies when an asset is leased under an operating lease, and the lessee acquires the asset at the end of the lease, and then sells the asset to a third party. As a result of this sale, the lessee has an amount of income equal to the amount of deductions allowed for the lease payments but only to the extent of any profit derived on that sale.

Subparts FB and FC contain the rules that provide for the income tax treatment on transfers of certain property. Subpart FB deals with transfers made under certain relationship agreement settlements, and subpart FC is about the tax treatment of certain transfers of property after death of the owner.

Subpart FE contains the thin capitalisation rules that apportion certain interest expenditure between income derived from New Zealand and other income for:

- a New Zealand taxpayer subject to a certain level or type of foreign control; and
- a foreign-owned bank with a lower than prescribed level of equity.

Subpart FF operates to restrict the conduit tax relief for a company by an amount that correctly reflects the interest deductions of the company that relate to the assets that produce the conduit tax-relieved income.

Subpart FL contains the rules addressing the income tax consequences when a New Zealand-resident company changes its residence to another country and loses its New Zealand residence.

Subpart FM draws together most of the rules for entry into a consolidated group and the tax treatment of certain transactions between member companies of a consolidated group. However, tax loss rules for consolidated groups are located in subpart ID because of their inter-relationship to the more general loss rules in Part I. The application of some specific anti-avoidance rules to a consolidated group has been retained in subpart GB. The consolidated group rules relating to memorandum accounts have been retained in Part O (Memorandum accounts) as they are so closely related with the general rules in that Part.

Subpart FN applies when two or more companies that are part of a wholly owned group of companies form an imputation group to enable a company in the imputation group to pay an imputed dividend when another company in the imputation group has a credit for New Zealand tax paid. This subpart also includes the rules relating to trans-Tasman imputation groups.

Subpart FO applies to amalgamations involving only New Zealand-resident companies that are not dual resident and do not derive only exempt income. These rules generally provide for no income tax consequences on the transfer of property and novation for liabilities that occur under the amalgamation.

Subpart FZ has been retained for a range of terminating provisions.

## **Part G of the bill**

Part G of the 2004 Act has a wide impact across the Act because of the scope of its provisions. It contains two types of provisions:

- those dealing with avoidance; and
- those dealing with certain transactions treated as taking place at market value.

Two structural issues were identified in rewriting Part G:

- It was not entirely clear in what circumstances a provision's anti-avoidance nature merited locating it in Part G. This point arises because, in many cases, other existing technical base-maintenance remedial provisions could be viewed as dealing with matters of avoidance.
- As other Parts of the Act also contain many provisions treating transactions as occurring at market value, the rationale for having valuation provisions in Part G was unclear.

As a result, the provisions proposed to be retained in Part G are those which have an anti-avoidance element or do not have a suitable alternative location. The bill retains, in subparts GA and GB, only those provisions that, in broad terms, apply to arrangements having a purpose or effect of generally defeating the purpose of the Act or specific provisions in other Parts of the Act.

As has occurred with rules in other Parts, when a rule in Part G has an effect on the amount of income or a deduction and the allocation of that amount, a link is now made to its related rules in Part C, D, or E. As in other Parts, this drafting approach assists readers in their understanding of the relationship between a rule in Part G and other Parts of the Act.

## **Part H of the bill**

Part H of the Income Tax Act 2004 contains groups of rules that modify the calculation of taxable income for a tax year for certain persons and entities. Some provisions within Part H also affect provisions in Parts F to N of the Act.

Subpart HA contains the rules for attributing and loss-attributing companies. These are new terms replacing “qualifying company” and “loss attributing qualifying company.” As the term “qualifying” is used in the 2004 Act in many different ways, it is preferable to use terms that are more representative of the underlying policy.

Most of the trust rules are set out in subpart HC. These rules provide for the taxation of distributions from trusts and the taxation of undistributed income derived by trustees. Trusts are classified as complying trusts, foreign trusts and non-complying trusts. Again, these terms have been chosen because they better reflect the policy of the rules.

The agency rules are set out in subpart HD. They set out the circumstances in which a person is treated as an agent of another person in relation to the tax obligations of that other person for income tax and tax administration purposes.

Subpart HE sets out the rules that apply to transactions between a mutual association and its members. These rules provide for the income tax treatment of income derived by a mutual association and also of distributions to members.

The rules for Māori authorities are contained in subpart HF. These rules set out the taxation treatment for income derived by a Māori authority and distributions made from these authorities. The relationship with other Māori authority rules (tax credits, memorandum accounts, refunds, tax rates and administration rules) are also identified.

Subpart HR contains rules for a variety of entities, such as partnerships, joint ventures, group investment funds, the Government Superannuation Fund and airport operators.

Subpart HZ has been retained for terminating provisions.

## **Part I of the bill**

Part I contains the loss rules. Since these rules were first introduced, many additions have been made to the rules, including ring-fenced losses for mining, and CFC and FIF holdings. Over time, the Act has also extended the way in which a tax loss is used for purposes other than offsetting against net income of a future tax year. The new subpart IA now provides clear links to the core provisions, as well as signposts to specific rules setting out the different ways in which a tax loss may be used.

The Part is structured to ensure that persons with tax losses carried forward must first use those losses by subtracting them from their net income for the tax year before they can make use of the variety of elective uses for tax losses. New terms central to these rules are “tax loss component”, “tax loss”, and “loss balance”.

Subpart IA is a key part of the restructured Part I. It sets out the rules within the Act that allow a person with a tax loss to use that loss. This subpart also contains the general rules for carrying forward a tax loss, which are located in subparts IE and IF of the 2004 Act.

Subparts IC to IE deal with the main company-related loss rules. The loss grouping rules for companies are in subpart IC. Subpart ID sets out how the loss grouping rules are applied to a consolidated group of companies. The loss rules that apply to companies in certain amalgamations are set out in subpart IE.

The rules in subpart IP set out how losses may be used when the general loss rules and loss grouping rules are breached part-way through an income year. A breach of these rules occurs through a loss of continuity or commonality (as applicable).

Subparts IQ to IT deal with how ring-fenced tax losses may be used. These losses include attributed CFC net losses, FIF net losses, mining and petroleum mining net losses and life insurance policyholder net losses.

Subpart IV contains the rules restricting the amount of a tax loss that a supplementary dividend holding company may use.

Subpart IW sets out the circumstances in which a tax loss may be used to satisfy shortfall penalties.

Subpart IZ contains terminating provisions that apply to persons with certain types of tax losses from prior years that have restrictions on their use.

## **Part L of the bill**

The rewritten Part L contains most of the tax credit rules. It has been expanded to include rebates that are located in Part K, other than the tax credits for families (retained in a separate Part – Part M). The term “tax credit” is used to represent every type of tax credit.

Subpart LA contains the general rules relating to the use of tax credits and includes aspects of the rules contained in sections BC 8 to BC 10 of the 2004 Act. In particular, subpart LA identifies when a tax credit arises, and sets out how the Act applies a tax credit to satisfy a person's obligations under section BB 2. It also sets out how family scheme credits are used.

Subpart LB contains a list of provisions describing the amount and time at which a person has a tax credit for PAYE, provisional tax, RWT, NRWT, under the family scheme, and for caregivers.

Subpart LC lists the tax credit rules that relate to amounts that are rebates in subpart KC of the 2004 Act. This subpart describes the amount and time at which a person has the tax credit, as well as the adjustment rules for part-year residency and a change in balance date.

Tax credits for donations are dealt with in subpart LD. The use of imputation credits as a tax credit is dealt with in subpart LE, and the use of FDP credits for tax credit purposes is set out in subpart LF.

Subpart LJ has the rules that determine the amount of a tax credit a New Zealand resident has for foreign taxes paid on income sourced outside New Zealand. These rules more clearly identify the segmental approach to the calculation of the maximum tax credit for income from a particular source or of a particular nature.

Subpart LK contains rules covering a variety of tax credits, including tax credits relating to attributed CFC income, consolidated companies and companies that have amalgamated.

The underlying foreign tax credit rules are set out in subpart LL. Subpart LO sets out when Māori authority tax credits arise and when they can be used. Subparts LP and LQ deal with the tax credit rules for supplementary dividends and conduit relief. Policyholder tax credits for life insurers are dealt with in subpart LR.

Again, subpart LZ has been retained for terminating provisions, and includes the tax credit rules for home vendor mortgages and special home ownership accounts.

## **Part M of the bill**

Part M of the bill contains only the rules relating to the entitlements under what is referred to in the draft legislation as the "family scheme". These rules have been retained within a separate Part because they mostly relate to the delivery of tax credits to eligible people on an interim basis during a tax year. This Part of the bill provides for the calculation of the various family scheme credits, which are then dealt with under Part L.

Subparts MA to MC contain the general provisions for the family scheme rules. Subpart MB provides the rules for calculating the amount of family scheme income on which the family scheme tax credit is based. Subpart MC lists the rules under which a person may be entitled to a family scheme tax credit.

Subparts MD to MF provide for the calculation and delivery of the various family scheme credits. Subpart MZ contains some terminating provisions relating to past aspects of the family scheme.

## **Part O of the bill**

Part O of the bill contains the rules relating to memorandum accounts. “Memorandum account” is a new, generic term used in general rules that relate to imputation credit accounts, FDP accounts, CTR accounts, branch equivalent tax accounts, ASC accounts, Māori authority credit accounts and policyholder credit accounts.

The main purpose of Part O is to provide a way of tracking payments of tax, tax relief amounts and other types of payment made by or to certain entities in a way that enables the subsequent delivery of an amount of a tax credit under Part L or other tax benefits to people having interests in these entities. As a result, Part O indirectly relates to the core provisions via Part L and other provisions.

This Part draws common rules together and sets out separate tables for credits and debits that summarise the credit and debit rules for each type of memorandum account. These tables follow subpart OZ.

Subpart OA contains the general rules that apply to all memorandum accounts. Examples of general rules include how to determine the balance of a memorandum account at any time, continuity rules that must be satisfied to preserve the carry-forward of credits, within corporate entities, from one tax year to the next, and how to calculate a maximum permitted ratio for attachment of certain credits to certain distributions.

Each of the subparts from subpart OB to OK contains the specific rules for each type of memorandum account. These specific rules detail the amount of a credit or debit and the time at which they arise. Each subpart also quantifies the amount of a credit that may be attached to a distribution from the entity.

Each subpart also states the consequence of an account having a debit balance at 31 March and the additional amounts that may be payable as a result. Subpart OB deals with imputation credit accounts, OC with FDP accounts, OD with CTR accounts, OE with BETA accounts, OF with ASC accounts, OJ with policyholder credit accounts, and OK with Māori authority credit accounts.

Subpart OP contains the rules that set out how a consolidated group of companies applies the individual and general memorandum account rules. It also sets out specific memorandum account rules that apply just to a consolidated group of companies.

Subpart OZ contains terminating provisions.

## **Part R of the bill**

Part R consolidates the rules that set out how and when persons satisfy their obligations for amounts imposed under Part BB. The rules relating to tax payments and refunds from subparts MB to MD of the 2004 Act have been moved to Part R. Those rules in subparts MB to MD of the 2004 Act related to terminal tax, provisional tax, PAYE intermediaries, tax pooling, early payment discounts and the use of tax refunds.

Subpart RA draws together the general rules that relate to several different payment types. In particular, Part R provides a clear link from the obligations imposed under section BB 2 to the detailed rules for each payment type in the relevant subparts within Part R.

This Part also rationalises common rules – for example, the date by which payment is required – and the treatment of amounts withheld by the payer as being received by the payee. The Income Tax (Withholding Payments) Regulations 1979 have been moved to and consolidated with associated provisions in subpart RD. Administrative rules (which mainly relate to information and notification requirements) have been moved to the Tax Administration Act 1994.

Subpart RB contains the rules that relate to the satisfaction of person’s terminal tax under section BC 8. This subpart also incorporates section NG 3 of the 2004 Act, which applies to a person with non-resident passive income when the NRWT withheld by the payer of the income is treated as the income tax liability in relation to that income.

The provisional tax rules are set out in subpart RC. These rules describe the circumstances in which a person has a provisional tax obligation, the methods for calculating the amount of provisional tax payable for a tax year, and the payment methods relating to a person’s provisional tax liability for a tax year.

The PAYE and ESCT rules are now located in subpart RD because of the similarity in their operation. These rules define the PAYE rules and list the types of payments to which they apply. They also show how an employer calculates the amount of PAYE or ESCT to be withheld and when the amount withheld is to be paid to the Commissioner.

Subparts RE, RF and RG set out the rules describing when and how amounts are withheld from payments consisting of resident and non-resident passive income, as well as amounts in relation to foreign dividends received by a New Zealand company. These subparts also describe when and how these amounts are paid to the Commissioner or are treated as being paid.

Subpart RM consolidates the rules dealing with refunds of overpayments of taxes and other obligations under the Act. Subpart RP sets out the rules relating to PAYE intermediaries and tax pooling accounts. Subpart RZ has been retained for certain terminating provisions relating to provisional tax and withdrawal tax.

## **Part Y of the bill**

Definitions continue to be located at the end of the Act, but immediately before transitional provisions. Subpart YA contains the list of defined terms, and whether the substance of a definition is set out in Part Y or is located close to its operating rules. An example of this latter approach is the definitions of the different types of trusts:

- “Complying trust” is in clause HC 10.
- “Foreign trust” is in clause HC 11.
- “Non-complying trust” is in clause HC 12.

Subpart YB contains the definition of “associated person”. This definition has been restructured to better communicate the concepts underlying the various codes within the 2004 Act which define “association”.

The meaning of “control” is set out in subpart YC, and includes the voting interest and market value interest rules. Subpart YD sets out the rules relating to residence and source. Subpart YE contains the rules describing how references to balance dates and years are intended to be read throughout the Act.

### **Part Z of the bill**

Part Z contains the transitional rules, and it is intended that the transitional rules have the same function as the equivalent rules set out in Part Y of the 2004 Act. These transitional rules are intended to apply from the beginning of the 2008-09 income year that corresponds to the 2008-09 tax year.

## **CHAPTER 3**

### **Intended changes in the legislation**

Making the law clearer has been achieved by using plain language within a consistent structure. The objective is to do this without substantively changing the policy content and associated compliance requirements of the current Act. Care has been taken to ensure that, apart from minor policy clarifications, the bill produces the same outcome as the existing law.

The intended changes in the legislation made in the bill are of a minor nature and have been presented for public consultation in recent years. These changes are supported by the Rewrite Advisory Panel.

#### **Clause FA 3 – Share dealing**

Clause FA 3 rewrites section FC 3 of the 2004 Act. This rule deals with the situation where a person enters into an arrangement to buy shares on revenue account, strips out a dividend from those shares, and then sells them. In the absence of section FC 3, this person would be able to generate, for income tax purposes, a loss on the sale of those shares. This rule was originally enacted in 1959 (as section 136A of the Land and Income Tax Act 1954) to prevent this outcome, but also to ensure that the dividend continues to be treated as it normally would (for tax purposes) under the dividend rules.

A drafting issue identified in the rewrite of this provision is an ambiguity in the proviso. This ambiguity potentially allows the “stripped-out” dividend to be counted twice in applying the proviso, and would result in the rule being largely ineffective. Clarifying this ambiguity to count the “stripped-out” dividend only once in applying the rule ensures that the provision should continue to operate as intended.

#### **Clauses FA 5(6) and FA 9(3) – Finance leases and operating leases**

The lease rules in sections FC 5 and FC 8E of the 2004 Act provide that when a leased asset is disposed of to an associated person of the lessee of that asset, and that associated person then disposes of the asset, the lessee is taxed on any profit on disposal. The policy of this rule is to ensure that the disposal rules applying to the lessee cannot be circumvented through transactions with associated persons. However, these rules are not clear about when the test of association applies.

Clauses FA 5(6) and FA 9(3) place this test of association at the time the leased asset is disposed of to the associated person.

### **Clauses FC 2 to FC 6 – Transfer of property on death**

The transfer of property from a deceased person to the beneficiaries of the estate legally involves two transactions involving that property. The rules in subpart FI of the 2004 Act are intended to provide rollover relief for income tax purposes on transmission of certain types of property from the deceased person to his or her beneficiaries.

Submissions to the exposure draft for this Part identified that the drafting in subpart FI of the 2004 Act could be interpreted as applying only to the transfer from the deceased person to the administrator or executor of the deceased person's estate. As a result, clauses FC 2 to FC 8 have been clarified to ensure that they apply to the transfer of certain property to the executor or administrator of a deceased person's estate, as well as the subsequent distribution of property to the beneficiaries of the estate.

### **Clause GB 27(2)(c) – Attribution rule for personal services**

The current rule in section GB 14B(2)(c) is ambiguous as to whether the threshold of \$60,000 should include income that is available for attribution or not.

The rewritten provision confirms the policy intention that the threshold amount of \$60,000 net income includes amounts that would be attributed under the attribution rule.

### **Clauses GB 35(2)(d) and GB 42(2)(d) – Multiple purposes in arrangements**

Sections GC 22(1)(a)(iv) and GC 27A(1)(d) of the 2004 Act refer to an arrangement that has "the purpose" of obtaining a tax advantage. The context of these rules is that this purpose should not be an incidental purpose, indicating that the section actually contemplates there may be more than one purpose for the arrangement. The use of "the purpose" is thus inconsistent with the context and application of the drafting and is linguistically incorrect.

It is clear from the drafting of these two sections that they are intended to apply when one purpose of the arrangement is to obtain a tax advantage, irrespective of the number of purposes of the arrangement. However, the section is not to apply when the purpose giving rise to the tax advantage is incidental to the arrangement. As a result, in both rewritten provisions, the term "the purpose" has been clarified as "a purpose".

### **Clause HC 34(2) – Taxable distributions from a non-complying trust**

Section HH 3 of the Act treats taxable distributions from a non-complying trust as a special class of income that is not included in the annual return of income. These distributions are derived from trust funds when the trustees have not complied with their New Zealand tax obligations.

A taxable distribution of this nature is subject to a special tax rate, but the rules do not expressly contain a due date for payment of that tax. The current practice is to require the payment of this special tax by the terminal tax date of the person liable for the tax on the distribution. (Either the trustee or the beneficiary can be liable.) Clause HC 34(2) provides that the due date for payment of tax on a taxable distribution from a non-complying trust is the same as the due date for the payment of terminal tax of the person liable to make the payment of the tax on this distribution.

#### **Clause IA 4(1) – Tax losses**

The relationship between the tax loss carry-forward and the grouping rules is unclear. A potential ambiguity exists as to whether losses carried forward by a person should be applied to the person's own net income before the grouping rules can be applied.

The policy intention is that, when persons carry forward tax losses, they must first use these tax losses to offset against their own net income. In other words, other uses of tax losses carried forward from a prior tax year (including grouping of losses) are elective actions that can be made only if carried-forward losses exceed a person's net income for the current tax year.

Therefore clause IA 4 clarifies that a person who carries forward tax losses from one tax year to the next tax year must first use that carried forward loss balance to reduce net income for that next tax year. It also clarifies that a person can apply the elective loss rules only to losses carried forward from the previous tax year if the balance of carried-forward tax losses exceeds the net income of the current tax year.

#### **Clauses LA 1 to LA 10 – Tax credits and rebates**

The rewritten Parts K and L consolidate the concepts of rebate and tax credit. The rationalisation of these terms and the restructuring of these rules gives rise to a minor adjustment in the use of rebates and tax credits.

The 2004 Act takes an inconsistent approach to the time at which tax credits arise and the tax year in which those tax credits are used to satisfy an obligation under the Act, particularly in a business context. The restructuring of the tax credit rules achieves a matching of the income year in which the tax credits arise to the corresponding tax year. This change overcomes timing problems inherent in some of the tax credit rules and better reflects the policy intention.

However, the clarification does not apply to credits of tax that arise under subparts KC (individual rebates) or KD (Tax credits for family support and family plus) of the 2004 Act as these credits can only arise and be used in relation to a tax year.

## **Clause YA 1 – Definition of “natural resource”**

The concept of “natural resource” is found in two definitions in the Act and is also a term used in many of New Zealand’s double taxation agreements. The 2004 Act does not define this term, and as part of the Rewrite project’s objective is to provide clear legislation, it is desirable to define it.

The new definition of “natural resource” is derived from a review of all natural resource-related definitions within other New Zealand legislation. The definition in clause YA 1 includes land, water, air, soil or subsoil, minerals, geographic or geologic features, electromagnetic spectrum, forms of energy, living organisms, ecosystems and any rights or interest in any of these things mentioned.

## **The use of the defined term “tax year” in business related rules**

In the rewrite of Parts F to O, officials identified a number of provisions that refer to the defined term “tax year” (31 March year), when the context of these rules indicate that the reference should be to the defined term “income year” (balance date-related). This is particularly evident in rules relating to commercial activity.

The term “tax year” in the provisions listed below has been either omitted from the rule, as the term is unnecessary in the context of the rule, or has been rewritten to better reflect the income year context of the rule. This list in the left-hand column (Clause in new Act or in TAA section) is set out as an appendix to schedule 51.

| <b>Clause in new Act or TAA section</b> | <b>2004 Act section</b> |
|---|-------------------------|
| CS 18                                   | GD 6                    |
| DB 56                                   | GD 4                    |
| EY 11                                   | GD 8                    |
| FA 3                                    | FC 3                    |
| FA 5                                    | FC 5                    |
| FA 8, FA 9, FA 10                       | FC 8B                   |
| FA 9                                    | FC 8E                   |
| FA 10                                   | FC 8D                   |
| FA 11                                   | FC 8H, FC 8I            |
| FB 2                                    | FF 4                    |
| FB 8                                    | FF 8                    |
| FB 13                                   | FF 13                   |
| FB 19                                   | FF 14                   |

| <b>Clause in new Act or TAA section</b> | <b>2004 Act section</b>              |
|---|--------------------------------------|
| FB 20                                   | FF 19                                |
| FC 4(2)(c)                              | FI 5(2)(c)                           |
| FE 2                                    | FG 2                                 |
| FE 5                                    | FG 3                                 |
| FE 7, FE 8                              | FG 8B(2)                             |
| FE 21, FE 22                            | FG 8G<br>Item TXB, Items FTC and CRT |
| FE 37                                   | FG 8D                                |
| FF 2                                    | FH 1(1)                              |
| FF 5                                    | FH 5                                 |
| FF 6                                    | FH 6, FH 7                           |
| FF 7                                    | FH 8                                 |
| FF 9                                    | FH 3                                 |
| FF 10                                   | FH 4                                 |
| FM 14                                   | FD 9                                 |
| FN 14                                   | FDA 6(9)                             |
| FO 4                                    | FE 8                                 |
| FO 7, FO 9                              | FE 4                                 |
| FO 12 – FO 14, FO 16                    | FE 6(5)(iv), FE 7(1)                 |
| FO 19, FO 20                            | FE 10                                |
| GB 1                                    | GB 1(3)                              |
| GB 4                                    | GC 4                                 |
| GB 23, GB 24                            | GD 3(3)                              |
| GB 27                                   | GC 14B                               |
| GB 28                                   | GC 14C                               |
| GB 29                                   | GC 14D                               |
| GC 5                                    | GD 10(3)                             |
| GC 9(1)                                 | GD 13(10)                            |
| HA 42                                   | HG 12                                |
| HC 7                                    | HH 1)(7)                             |
| HC 8                                    | HH 8                                 |
| HC 10                                   | HH 2(2)                              |

| <b>Clause in new Act or TAA section</b>                        | <b>2004 Act section</b>     |
|--|-----------------------------|
| HC 13  | HH 1(5), (6)                |
| HC 15  | OB 1 “Taxable distribution” |
| HC 15, HC 16   | HH 6                        |
| HC 17, HC 18, CV 13(a)   | HH 3(1)                     |
| HC 19, HC 22,  | HH 3(4)                     |
| HC 20, CW 52   | HH 3(5)                     |
| HC 21, CV 14   | HH 3(5A)                    |
| HC 25  | HH 4(3), (3A), (6)          |
| HC 26(1), CW 53  | HH 4(3B)                    |
| HC 29  | HC 4(4), (5)                |
| HC 30(6)   | HH 2(4)                     |
| HC 31  | HH 5                        |
| HC 32(1)   | HH 3(2)                     |
| HC 35(4)(a)  | HH 3B                       |
| HC 36(3)   | HH 3D(1)(b), (c)            |
| HD 5   | HK 5                        |
| HF 7   | HI 5(2)                     |
| RD 3   | OB 2                        |
| RF 2   | NG 3                        |
| RG 7(4), (7)   | NH 7(2), (3)                |
| YA 1 index entry “Category A income”,<br>definition in HR 3(1) | OB 1 “Category A income”    |
| YA 1 index entry “Category B income”,<br>definition in HR 3(3) | OB 1 “Category B income”    |
| YA 1 index entry “Current value”,<br>definition in HR 3(4)     | OB 1 “Current value”        |
| YA 1 “First business day”                                      | OB 1 “First business day”   |
| YA 1 “Herd livestock”  | OB 1 “Herd livestock”       |
| TAA 93B  | HH 7                        |

## CHAPTER 4

### Minor drafting changes

This chapter explains some of the drafting changes that have been made to individual rules.

#### Core provisions

Clause BC 4 of the bill now reflects the wide range of uses to which a net loss may be put.

Sections BC 6 to BC 10 of the 2004 Act provide a framework for determining the income tax liability of a person and how the Act uses tax credits to satisfy this liability. As this framework has been more closely integrated with the detailed tax credit rules in Parts L and M of the bill, these sections have been simplified and harmonised with Part L. As a result, clauses BC 6 to BC 8 and subpart LA of the bill now cover the same subject matter as sections BC 6 to BC 10 of the 2004 Act.

#### Parts C to E of the bill

Some provisions in Parts F to Z have been moved to a new location within Parts C to E. For example, clauses CV 16, CV 17, and DW 3 in the bill are the new location for the operative aspects of sections FC 18 to FC 21 of the 2004 Act.

The transitional rules in the 2004 Act relating to Parts yet to be rewritten have been omitted from the rewritten bill. These transitional rules are sections CW 51, CX 45, CY 1, DY 1 and DY 2. However, sections BD 3(2) and BD 4(2) operate to permit rules located in Parts F to I of the Act to have a timing effect. These rules are retained in the bill to ensure that any timing rule retained within Parts F to Part I can continue to have an operative effect.

However, when a provision in Parts F to the end of the Act have an effect on income or a deduction (including, in some instances, a timing effect), a new rule has been inserted into Parts C or D. The insertion is made either within an existing rule or as a new section that has an overriding effect on the related rule. Examples of these new rules in the bill include:

- clause CB 2 (which relates to amounts received on disposal of business assets that include trading stock);
- clauses CC 11 to CC 13 (which relate to finance leases and hire purchase agreements);
- clause CD 11 (which relates to various avoidance arrangements);
- clause DB 11 (which relates to profit-related or substituting debentures); and
- clauses DB 56 to DB 58 and DC 5 (which relate to various avoidance arrangements).

## Part F of the bill

As the apportionment function is better related to the main rules relating to the subject matter, Part F in the bill no longer deals with apportionment. This has led to a number of provisions being moved from Part F to other Parts of the Act, for example:

- Section FB 2, which apportions tax credits, has been merged with the source rule in YD 5. Under subpart LJ of the bill, the calculation of a tax credit on foreign income is linked to the amount of the foreign income. Consequently, the amount of tax paid on foreign income is expected to be determined by the relationship between subpart LJ and the source rule in clause YD 5.
- Section FB 3 has been moved to clause CB 2, as this provision is an apportionment rule that is better aligned with the business income and trading stock rules.
- Section FB 4A has been moved to clause DB 30 as this provision is an apportionment rule related to the land sale rules.
- Section FB 7 has been moved to clause EE 52 as it is an apportionment rule that is better aligned with the depreciation rules.

Some income and deduction rules have been moved to other parts in the bill. For example:

- Sections FC 13 to FC 15 and FC 18 to FC 21, relating to non-resident insurers, shippers and film renters, have been moved to Parts C, D, and Y. The new provisions are in, respectively, clauses CR 3, CV 16 and CV 17, DW 3, and YD6 to YD 8. This move ensures that these income and deduction prohibitions and the attribution of a New Zealand source to that income are appropriately treated in the scheme of the Act.
- Sections FC 16 and FC 17 have been moved to clauses HD 16 and HD 17 to reflect the agency relationship that arises on payment of certain insurance premiums to non-resident insurers.

The relationship between the provisions in Part F and those in other Parts of the Act are signalled with new provisions. Examples of rules relating to this approach include:

- clauses CC 11 to CC 13, which relate to the finance lease and hire purchase agreement rules;
- clause CH 9, which relates to the downward adjustment to the income tax liability for deductions under section FG 8B of the Act as this rule is in essence a “negative deduction”, clause CH 9 ensures that this adjustment is more consistent with the manner in which the Act addresses other “negative deductions”;
- clause DB 10, which relates to the limitation on deductibility of interest in certain thin capitalisation situations;
- clause DB 26, which relates to the cost of cancelled shares when the shares were held as revenue account property;
- clause DV 15, which relates to the amalgamation rules; and
- clause EB 24, which relates to the valuation of trading stock.

Rules moved to subpart FZ of the bill, as terminating provision, are:

- sections FC 6 to FC 8, relating to the specified lease rules, which have been moved to clauses FZ 2 to FZ 4;
- section FF 5, relating to commercial bills, which has been moved to clause FZ 6;
- section FF 18, relating to specified activities carried on before 11 October 1982, which has been moved to clause FZ 5; and
- sections FI 9 and FI 10 of the 2004 Act, being transitional rules applying to transfers of property on death, which have been moved to, and combined in, clause FZ 7.

### **Part G of the bill**

Rules in which a discretion of the Commissioner has been replaced with an objective test are clauses GB 4, GB 6, GB 31, GB 36(1), GZ 1, and Schedule 5, Part A, Clause 4.

The relationship between some rules in Part G and other parts of the Act are now signalled clearly, and include:

- clause CD 11, which relates to the treatment of dividends as a result of an avoidance arrangement;
- clause CH 7, which relates to an adjustment to arising as a result of an avoidance arrangement;
- clauses CH 8 and DB 58, which relate to the disposal of trading stock and the valuation of lease rentals at other than market value
- clause CW 62, which relates to adjustments for exempt income as a result of an avoidance arrangement;
- clause CX 18, which relates to benefits provided to associates of both employees and shareholders;
- clause CX 54, which relates to adjustments for excluded income as a result of an avoidance arrangement;
- clause DB 57, which relates to adjustments to the amount of a deduction as a result of an avoidance arrangement; and
- clause EJ 9, which relates to an adjustment to the allocation of certain film expenditure as a result of an avoidance arrangement.

Provisions moved from Part G to other Parts are:

- subsections GC 15(3) and (4), which have been moved to clause CX 18;
- section GD 4, which has been moved to clause DC 5; and
- section GC 9, which has been moved to clause EX 3.

Omissions from Part G are:

- section GC 14D(6), as clause GB 29(4) incorporates its effect;
- section GC 14F(2), as its effect is dealt with in the definition of “arrangement” in section OB 1;
- section GC 19, as it duplicates the effect of clause RA 2 (section NF 13 of the 2004 Act) and is therefore unnecessary;
- sections GC 18, GC 20, which are unnecessary as public policy law operates to void any agreement that does not comply with New Zealand legislation;
- section GC 27A(6)(d), which has been removed as it is unnecessary because the Commissioner chooses which of subsection (5) or (6) applies, so both subsections cannot apply at the same time;
- section GD 3(3), which has been removed as its effect is taken up in clause GB 23(1) to (3);
- section GD 10(3), which is omitted as its effect is incorporated in subclauses GD 5(1) and (2); and
- sections GC 17(a), GE 1, and GZ 1, which have been omitted on the basis they are spent provisions.

## **Part H of the bill**

Terminology changes in Part H are:

- “Qualifying company” is now an “attributing company” and, similarly, a “loss attributing qualifying company” becomes a “loss-attributing company”. The term “attributing” reflects the dictionary meaning of the term “attribute”, being “regard as belonging to; ascribe to”.
- “Qualifying trust” and “non-qualifying trust” have been renamed, respectively, as “complying trust” and “non-complying trust”. This reflects that policy of the legislation for trusts that comply with their taxation obligations which is that they are able to make distributions to beneficiaries (other than beneficiary income) without further income tax consequences for the beneficiary.
- The concept of transfer of value is applied to the definition of distributions, as the concepts in the definition of “distribution” in the 2004 Act have extensive similarities with the definition of “transfer of value” used in subpart CD (Dividends) of the Act.

The relationship of various rules in Part H to the scheme of the Act, particularly in relation to Parts C to E have been clarified. Examples of this type of clarification include:

- clause CB 32, which lists income from mutual transactions as income (section HF 1(1) of the 2004 Act);
- clause CB 33, which applies to distributions (including rebates) made to members of mutual associations (section HF 1 of the 2004 Act);

- clause CD 12, which ensures that when a superannuation scheme that is a unit trust becomes a superannuation fund, the loss of the company status is treated as a liquidation, which clarifies how the change in status of the unit trust relates to the dividend rules, as intended by section HH 1(9) of the 2004 Act;
- clause CD 37, which ensures that a Māori authority distribution is not a dividend (section HI 4(2) of the 2004 Act);
- clause CV 11, which lists certain distributions from a Māori authority as income (section HI 4, HI 5 and HI 7 of the 2004 Act);
- clause CV 12, which relates to amounts received by a trustee after a person's death in relation to clause HC 8 (section HH 8 of the 2004 Act);
- clause CV 13, which lists as income an amount of beneficiary income, a taxable distribution from a foreign trust and certain settlements of property on trust, the list relating to sections HH 1(7), HH 3(1) of the 2004 Act;
- clause CV 14, which relates to section HH 3(5A) of the 2004 Act and the treatment of distributions from a community trust;
- clause CV 15, which provides for certain amounts to be income of a beneficiary of a trust on the day a person regains New Zealand residence for tax purposes (section HH 3(3) of the 2004 Act);
- clause CW 14, which lists as income certain dividends derived by an attributing company (section HG 10 of the 2004 Act);
- clause CW 15, in which distributions from an attributing company are either treated as fully imputed dividends or as exempt income (section HG 13 of the 2004 Act);
- clause CW 52, which ensures that distributions that are not beneficiary income derived from a complying trust are not included in the calculation of a beneficiary's taxable income an example of a distribution to which this provision applies being a payment of a pension from a superannuation fund;
- clause CW 53, which relates to income derived by trustees of a trust with no resident settlor (subsection HH 4(3B) of the 2004 Act);
- clause CW 54, which provides for certain distributions from a Māori authority to be exempt income, as set out in section HI 5(1) of the 2004 Act;
- clause CX 55, which treats income derived by a trustee in relation to minors as excluded income of the minors (sections HH 3A to HH 3F of the 2004 Act);
- clause CX 56, which lists as excluded income, a taxable distribution from a non-complying trust, which is consistent with the "stand-alone" tax treatment in Part H for these taxable distributions (section HH 3 of the 2004 Act);
- clause DB 9, which rewrites section HG 9(3) to (5) of the 2004 Act to restrict the amount of deduction a person is allowed for interest incurred on money borrowed to finance the acquisition of shares in an attributing company;
- clause DV 19, which lists the conditions under which a mutual association has a deduction for a rebate paid to a member of the association (section HF 1 of the 2004 Act).

Provisions moved in or out of Part H include:

- The requirements set out in section OB 3 of the 2004 Act for attributing companies have been moved to subpart HA.
- Most of the rules relating to a consolidated group of companies have been moved to subpart FM of the bill.
- Section HK 18 of the Act, which relates to an administrative relationship between Customs officers and the Commissioner has been moved to draft section 166B of the Tax Administration Act 1994 (schedule 50 of the bill).

### **Part I of the bill**

Sections IH 4(1) and IH 5 of the 2004 Act have been omitted as they are historic in nature and are redundant. Section IG 1(4) also has been omitted on the basis that it is no longer necessary within the structure of the Act.

Sections IE 2, IF 1(5), IF 1(6), IF 2, IG 2(2)(c), (d)(ii)(B), IH 1(2), and IH 2(1) of the 2004 Act have been moved to subpart IZ as, respectively, clauses IZ 1, IZ 4, IZ 5, IZ 6, IZ 7, IZ 3, IZ 2.

### **Parts L and M of the bill**

Sections BC 9 and BC 10 of the 2004 Act are now largely contained in subpart LA of the bill. This drafting provides a clear relationship between the core provisions and the various tax credit rules.

Subpart KD has been relabelled as Part M in the bill, apart from:

- the rule providing for the use of the family tax credit, which is located in clause LB 4 of the bill; and
- sections KD 5(9), KD 6, and KD 7, which have been moved to the Tax Administration Act 1994 (see schedule 50, draft sections 80KI to 80KW).

Other provisions moved from Part K are:

- subparts KB, KC, and KE to KZ, which have been moved to Part L of the bill; and
- section KB 3, which has been moved to clause MA 4.

Provisions moved to subpart LZ include:

- section LF 6(1) and (3), which have been moved to clause LZ 1;
- section KE 1, which has been moved to clauses LZ 6, LZ 7 and LZ 8; and
- section KG 1, which has been moved to clauses LZ 9 to LZ 11.

## **Part O of the bill**

Part M of the 2004 Act has been relabelled Part O. A major improvement in the redrafting of Part M is the presentation of all debit and credit rules in summary form in a series of tables at the end of Part M.

Two consequential changes have been made to the Tax Administration Act 1994 that relate to the new term “memorandum account”. These changes insert a reference to “memorandum account” and are made in the definition of “tax position” in section 3, and also in section 22(2) of that Act.

The reference to Māori authorities in the imputation credit account rules has been omitted from the bill. Following the enactment of section ME 1(2)(j) in the 2004 Act by the Taxation (Māori Organisations, Taxpayer Compliance and Miscellaneous Provisions) Act 2003, a Māori authority may not maintain an imputation credit account.

Provisions moved from Part M of the 2004 Act to Part R of the bill are subparts MB, MBA, MBB, MC and MD.

Provisions moved from Part M of the 2004 Act to subpart OZ of the bill include:

- section ME 4(1)(viii), which has been moved to clause OZ 1;
- section ME 5(1)(e), which has been moved to clause OZ 2;
- section ME 5(1)(n), which has been moved to clause OZ 3;
- sections ME 5(4), MG 5(4), which have been moved to clause OZ 4;
- section MJ 4, which has been moved to clause OZ 5; and
- section MJ 7, which has been moved to clause OZ 6.

## **Part R of the bill**

Part R of the bill contains the rules that set out how and when persons satisfy obligations imposed on them under Part B of the Act. The relationship of the rules relating to the conversion of credits to a tax loss component and their use are also linked with Part I.

Most of the Income Tax (Withholding Payments) Regulations 1979 have been moved into subpart RD of the bill. The Schedule to the regulations is moved to new Schedule 4.

Redundant provisions include:

- sections MB 11 and MB 26 of the 2004 Act, which relate to the change of taxable periods for GST periods and have been omitted because they duplicate rules that are also contained in the Goods and Services Tax Act;
- section MB 28, which has also been omitted as it duplicates provisions in the Tax Administration Act; and

- section NZ 1, which has been omitted on the basis that its historic nature renders it redundant.

Provisions moved to the Tax Administration Act (TAA) include:

- administrative rules in sections MBA 3 to MBA 6, MBA 8, and MBA 9 (relating to tax pooling), which have been moved to sections 15N to 15S and section 120OE of the TAA;
- administrative rules in sections NBA 1 to NBA 3, NBA 5, and NBA 8, which have been moved to sections 15C to 15F, and 15J to 15L of the TAA;
- administrative rules in sections NBB 2, NBB 3, NBB 4, NBB 5 and NBB 7, which have been moved to sections 15C, 15G to 15I and 15M of the TAA;
- PAYE rules in sections NC 7(1), (3), NC 8(1), (1AA), (2) to (4), (7), (9A), (10), (12), NC 8A, NC 9, NC 12A(1) to (3), NC 14 and NC 15(1) to (3), which have been moved to sections 24B to 24J, 24L and 24P of the TAA;
- FBT rules in sections ND 1(6), ND 2(3), ND 9(2), (3), ND 10(2) to (5), ND 11, ND 12, ND 13(5), (6), ND 14(5), (6), and ND 15(7), (8), which have been moved to sections 46B to 46E of the TAA;
- RWT rules in sections NF 2AA, NF 8(2) to (4), NF 9, NF 10(1)(a), (d), (3) and NF 11, which have been moved to sections 24K and 32E to 32L of the TAA;
- NRWT rules in sections NG 5 to NG 7 and NG 16(5), which have been moved to sections 32M and 165B of the TAA;
- administrative rules in sections NH 2(4), NH 3(6) and NH 4(5)(b), (c), which have been moved to sections 32N and 71B of the TAA; and
- Regulation 5 of the Income Tax (Withholding Payments) Regulations 1979, which has been moved to section 24M of the Tax Administration Act.

The appendix to Schedule 19 of the 2004 Act has been omitted on the basis that it serves no useful purpose. While an employer must withhold PAYE from employment income, the employer must also take into account obligations under other Acts, so the information in this appendix is of little assistance to employers.

## **Part Y of the bill**

Part O of the 2004 Act is relabelled Part Y.

Although retained in clause YA 1 as index entries, the substance of a number of definitions has been moved closer to their related provisions, including:

- OB 1 “absentee”, which is moved to clause HD 18(2);
- OB 1 “beneficiary income”, which is moved to clauses HC 5 and HC 6(1) to (3);
- OB 1 “category A income”, which is moved to clause HR 3(1) and (2);

- OB 1 “category B income”, which is moved to clause HR 3(3);
- OB 1 “consideration”, “lessee’s acquisition cost”, “lessor’s disposition value,” which are moved to clause FA 7;
- OB 1 “consolidation rules”, which is moved to clause FM 2(2);
- OB 1 “corpus”, which is moved to clause HC 4;
- OB 1 “current value”, which is moved to clause HR 3(4);
- OB 1 “designated investment fund”, which is moved to clause HR 3(6);
- OB 1 “distribution”, which is moved to clause HC 14;
- OB 1 “dividend withholding payment rules”, which is moved to clause RG 1;
- OB 1 “effective interests”, which is moved to clause HA 43;
- OB 1 “eligible company”, which is moved to clause FM 31(1);
- OB 1 “foreign company”, which is moved to clause HA 6(2);
- OB 1 “foreign trust”, which is moved to clauses HC 10(2) to (4) and HC 11;
- OB 1 “full time earner”, which is moved to clause MA 7;
- OB 1 “fully conduit tax relief credited”, which is moved to clause RF 9(6);
- OB 1 “non-qualifying trust”, which is moved to clause HC 12;
- OB 1 “NRWT rules”, which is moved to clause RF 1;
- OB 1 “PAYE rules”, which is moved to clause RD 2(1), (2);
- OB 1 “provisional tax rules”, which is moved to clauses RC 2 and RC 3;
- OB 1 “qualifying person” (a)(ii), which is moved to clause MC 4;
- OB 1 “qualifying person” (a)(iii), which is moved to clause MC 5;
- OB 1 “qualifying trust”, which is moved to clause HC 10(1);
- OB 1 “resident imputation subgroup” and “trans-Tasman imputation group”, which are moved to clause FN 8;
- OB 1 “settlor”, which is moved to clauses HC 27 and HC 28;
- OB 1 “specified period” and “eligible period”, which are moved to clause MC 11;
- OB 1 “taxable distribution”, which is moved to clause HC 15; and
- OB 1 “trustee income”, which is moved to clauses HC 5 and HC 7(1).

Provisions moved out of Part O include:

- OB 2, which is moved to clause RD 3(1) to (4);
- OB 3(1)(a), (b) and (g), which is moved to clause HA 6;
- OB 3(1)(f), which is moved to clause HA 5(2);

- OC 1(2), which is moved to clause HR 5;
- OC 1(2)-(6), which are moved to clause HR 6;
- OC 1(6), which is moved to clause HR 7; and
- OF 2, which is moved to clause HC 6(4) and (5).

Some definitions in clause YA 1 that have been rationalised and updated are:

- “applicable basic tax rate”, which is changed to “basic tax rate”;
- paragraph (a) in the definition of “land”, which reverts to an operative rule in clause CB 6(3);
- the definitions of “pay” and “payment”, which are rationalised and consolidated;
- the definitions of “resident withholding income” and “non-resident withholding income”, which become “resident passive income” and “non-resident passive income” respectively;
- “rebate”, which is replaced by “tax credit” and other terms referring to a type of “rebate” are omitted;
- the definition of “trading stock”, which is simplified;
- “source deduction payment”, which becomes the new term “PAYE income payment”.

A number of definitions have been omitted as they are no longer required or are outdated terms relating to repealed legislation or relate to rules moved to the TAA. This list of defined terms being omitted includes:

- Acquisition of control or income interests
- Adjusted income tax liability
- Allocation debit
- Allocation deficit debit
- Allowable rebate
- Amount of the debenture
- At all relevant times
- Base ratio
- Basis of exemption
- Body
- Commencement date
- Commission agency contract
- Commission agent
- Communal home
- Controlled foreign company tax credit
- Co-operative marketing company
- Corporation
- Council

- Council-controlled trading organisation
- Current grower
- Director election
- Disposal of control or income interests
- District committee
- Dual resident company
- Effective date
- Eligible company
- Farm ownership requirements
- Fishing vessel ownership requirements
- Foreign company aggregates
- Full employment
- Gross tax deductions
- Group quarter day
- Grower
- Imputation return
- Imputation year
- Insurance premium
- Land owned
- Lessee's acquisition cost
- Lessee's outstanding balance
- Lessor's disposition value
- Lessor's outstanding balance
- Licence area
- Low tax jurisdiction company
- Māori authority distribution penalty tax
- Measurement day
- National
- Net balance due
- Net specified income
- Nil period
- Nominee
- Non-resident petroleum mining operator
- Notional income tax liability
- Overseas company
- Part E timing rules
- Payment
- Preceding year
- Primary employment earnings
- Protected amount
- Provisional taxpayer
- Qualifying payments

- Qualifying superannuation scheme
- Reconciliation statement
- Reduced deduction
- Refundable rebate
- Relevant associate
- Relevant time
- Repealed provision
- Resident withholding tax deduction reconciliation statement
- Return of the taxpayer's income
- Scheduler income subject to final withholding
- Secondary employment earnings
- Serving employee
- Shareholder election
- Special farm ownership account
- Special fishing vessel ownership account
- Special tax code certificate
- Specified foreign social security pension
- Specified fund
- Specified income
- Specified preference shares
- Specified value
- Start date
- Sufficient interest
- Tax code certificate
- Tax code declaration
- Tax rate
- Taxation Review Authority
- Unadjusted income tax liability
- Variation in control or income interests
- Year of determination

## **CHAPTER 5**

### **Transition to the new Act**

The new Act comes into force on 1 April 2008 and first applies to income derived in the 2008-09 income year. For amendments to other Acts, such as the Tax Administration Act, the commencement date of these rules is related to the 2008-09 income year.

#### **Transitional provisions**

Clause ZA 3 of the bill sets out the transitional provisions. These provisions ensure that a reference in any Act or document to the new Income Tax Act can be read as a reference to the 2004, 1994 or 1976 Acts, and a reference to one of those Acts can be read as a reference to the new Act.

Clause ZA 3(3) to (5) provides that the new Act and relevant Tax Administration Act provisions are intended to represent the 2004 Act in rewritten form, except where an intended change in the legislation is indicated in schedule 51 of the new Act. These provisions also highlight that, although the new Act has the force of law, if a rewritten provision is unclear or leads to an absurdity, the 2004 Act is to be used to determine the correct meaning of the new law.

#### **Saving of binding rulings**

Clause ZA 4 is designed to ensure that binding rulings continue to apply, despite the repeal of the 2004 Act. This continuation is to apply to binding rulings that were:

- based on the provisions of the Income Tax Act 2004 or earlier income tax legislation;
- intended to apply in one or more of the years following the date of effect of the new Act; and
- applied for before the beginning of a person's 2008-09 income year.

The clause provides that when a binding ruling has been issued about a provision in the Income Tax Act 2004 (or the 1994 or 1976 legislation), it will be treated as if it had been issued about the equivalent provision in the new Act at the time the new Act begins to apply. An equivalent provision is one that corresponds to the provision in any of the 2004, 1994 or 1976 Acts on which the ruling was based. If that provision in the new Act is subsequently amended, the provisions of section 91G of the Tax Administration Act (which can void the ruling) will apply in the same way as if the binding ruling had been made under the new Act.

Clause ZA 4(1)(c) uses the words “corresponds to the old law” to link the provision in the 2004 Act on which the ruling was based with the provision in the new Act which has the same effect. These words are designed to reflect the government’s intention that existing binding rulings should not be affected by the enactment of the new Act, but should continue to apply as if they had been made about provisions in that Act at the time it came into effect. Clause ZA 4 also provides that a binding ruling cannot be issued concerning the application of the new Act to an arrangement already governed by a binding ruling subject to the savings provision.

Therefore it is intended that the words used in these savings provision are given an appropriately purposive interpretation, so that taxpayers and Inland Revenue do not have to go to the effort of obtaining or issuing replacement binding rulings. In other words, the intention is that the requirement that the new law corresponds to the old law should not to be given any narrow, obstructive interpretation to prevent binding rulings being saved.

### **Saving of accrual determinations**

Clause ZA 5 is designed to ensure that accrual determinations which were based on the provisions of the Income Tax Act 2004 (or earlier income tax legislation), and were intended to apply in one or more of the years following the date the new Act came into force, will continue to apply. It applies to accrual determinations made before the beginning of the 2004 income year.

The clause provides that when an accrual determination has been issued about a provision in the Income Tax Act 2004 (or either of the Income Tax Act 1994 or the Income Tax Act 1976), it will be treated as if it had been issued about the equivalent provision of the new Act at the time the new Act began to apply. An equivalent provision is one that corresponds to the provision in the earlier Act on which the determination was based.

Clause ZA 5(1)(d) uses the words “corresponds to the old law” to link the provision in the earlier Act on which the determination was based with the provision in the new Act which has the same effect. These words are designed to reflect the government’s intention that existing accruals determinations should not be affected by the enactment of the new Act, but should be able to continue as if they had been made about a provision in that Act at the time it came into force. It will also be important that these words are not given a narrow interpretation that would prevent accrual determinations from being saved.

### **Depreciation determinations**

Depreciation determinations are made under the authority of section EE 25B of the 2004 Act. However, there is no provision in the 2004 Act or the Tax Administration Act 1994 that provides that these determinations cease to have effect on repeal of the 2004 Act. Therefore they continue to have effect by virtue of section 21 of the Interpretation Act 1999 as section EE 25B is to be replaced, without modification, by clause EE 26 of this bill.