Regulatory Impact Statement

Executive summary

Trans-Tasman portability of retirement savings

The creation of retirement savings portability between Australia and New Zealand is expected to improve labour market mobility between the two countries and assist individuals to consolidate their financial affairs in their country of residence.

The portability arrangements will apply to retirement savings held in the New Zealand KiwiSaver scheme and the Australian complying superannuation scheme. As these schemes have similar preservation requirements, the rules of the host country will generally be applied to any transferred savings. However there are several areas where the source country policies will continue to apply to these savings. On 16 July 2009, the Minister of Finance and the Australian Treasurer signed an Arrangement to record the intention of both governments to allow retirement savings portability.

KiwiSaver: enrolment of under 18 year olds

There is a lack of clarity about who can enrol children in Kiwi-Saver. The KiwiSaver Act does not prescribe who can contract with a scheme provider on behalf of a child under 18 years old. It is at the discretion of the provider whether or not an application is accepted. This has led to complaints and disputes from parents and guardians, as well as from children who have been enrolled without their consent.

The preferred option is to create new rules governing the enrolment of children under 18, to provide clarity about who can enrol children in KiwiSaver. The proposed new rules provide that:

- Children under 16 years old may be enrolled only by their legal guardian(s); they may not enrol themselves in KiwiSaver.
- Children aged 16 to 17 with a legal guardian must co-sign with their guardian to enrol in KiwiSaver; they may not enrol themselves, nor can they be enrolled by their guardian without their consent.
- Children aged 16 to 17 without a legal guardian may opt in to KiwiSaver by contracting directly with a scheme provider. This means that such children, who are married, in a civil union or living with a de facto partner, will not need a co-signed application to opt in to KiwiSaver.

Distributions by co-operative companies

Sections DV 11 and CD 34 of the Income Tax Act 2007 enable a resident co-operative company to deduct a distribution paid to a member if it is in proportion to the value of trading stock transactions between the member and the co-operative. This enables co-operatives to deduct distributions paid on supply-backed shares (that is, shares that members hold in proportion to their trading stock transactions with the co-operative). The proposed amendments to the Income Tax Act 2007 would extend this treatment to enable certain co-operative companies to deduct for tax purposes a dividend paid on a non-transaction share held by a member. A non-transaction share is a share that gives a member the right to sell trading stock to the company but where the member has not exercised the right. The amendment would apply only when the number of non-transaction shares held by any member does not exceed 20% of the number of supply-backed shares.

A co-operative company electing to deduct distributions may also, by notifying the Registrar of Companies, be exempt from the 20 working day limitation in section 125(2) of the Companies Act 1993. The amendment would give the board of the co-operative greater flexibility to set a date for determining members' entitlements to receive distributions (the "record date"). The record date may be any date within the financial year or other period to which the dividend relates.

Cancellation of BETA debits from conduit-relieved dividends

Prior to the recent international tax changes, conduit tax relief could be used to relieve tax on income earned in foreign subsidiaries, to the extent that the New Zealand parent company was owned by non-residents. The introduction of an active income exemption for controlled foreign companies, and an exemption for most foreign dividends received by companies, has made conduit tax relief largely redundant and so it has been repealed. To make the repeal of conduit tax relief effective, it is necessary to cancel those BETA debits that arose from conduit-relieved dividends. Cancellation will not lead to any double taxation as conduit-relieved dividends would not have been taxed in the first place. Other BETA debits will still be available for use during the two-year transitional period that was announced by Ministers in February 2008.

Binding rulings

Binding rulings are intended to provide taxpayers with certainty in entering into business transactions in which the interpretation of tax law is a key element. A binding ruling therefore sets out how Inland Revenue will apply tax laws to a particular arrangement. Taxpayers are not required to follow the ruling. If the taxpayer chooses to follow the ruling, Inland Revenue must apply the tax laws as set out in the ruling.

New rules address two major issues that were the subject of an officials' issues paper entitled *The binding rulings system: legislative issues*.

In relation to questions of fact, the proposed amendments provide that the Commissioner cannot rule on the existence of facts but only on the application of tax laws based on the facts provided by the applicant. The legislation also sets out particular factual matters that cannot be ruled on—questions in relation to the taxpayer's intention, the value of anything and what constitutes commercially acceptable practice. To remove any inference that the Commissioner is unable to rule on tax avoidance (which would defeat the main purpose of the suggested change) the exclusion for commercially acceptable practice is limited to where that term is used in the tax legislation. In relation to matters before the courts, the proposed amendments limit the Commissioner's discretion to decline to rule on cases involving identical or substantially similar arrangements, facts or issues.

Gift duty exemptions

The Estate and Gift Duties Act 1968 (EGDA) contains a number of exemptions from gift duty for certain types of gifts. In particular, section 73 contains exemptions for gifts made to charities and certain specifically named bodies.

Over the past year, the Minister of Revenue and tax policy officials have received a number of requests for amendments to the EGDA to exempt certain gifts from gift duty.

The proposal therefore seeks to exempt the following gifts from gift duty:

- transfers of assets by, and gifts made to, local or central government;
- gifts made to donee organisations (organisations that are approved by Inland Revenue, which are listed at its website, or that are approved by Parliament and listed in Schedule 32 of the Income Tax Act 2007); and
- distributions of property made in accordance with a Court order under the Law Reform (Testamentary Promises) Act 1949 or the Family Protection Act 1955.

Non-resident rig operators

Non-residents operating offshore rigs or seismic vessels in New Zealand currently benefit from a temporary tax exemption on their profits. This exemption expires on 31 December 2009. It is proposed that this exemption be extended for a further 5 years, to 31 December 2014.

Adequacy statement

The principles of the Code of Good Regulatory Practice and the regulatory impact analysis requirements, including the consultation requirements, have been complied with in respect of each of the proposals described in this Regulatory Impact Statement. The Statement is considered to be adequate. The respective Regulatory Impact Statements were circulated with Cabinet papers for departmental consultation.

Status quo and problem

Trans-Tasman portability of retirement savings

The treatment of retirement savings during an individual's working life is an area where differences in domestic policy settings impact on the seamless nature of the trans-Tasman labour market. New Zealanders and Australians have an automatic right to move freely across the Tasman and are able to reside and work in either country. However, personal retirement savings accumulated in Australia cannot be transferred to New Zealand and cannot easily be accessed before retirement.

The ability to transfer savings is one factor individuals may take into account when considering employment opportunities on either side of the Tasman. All else being equal, the inability to take retirement savings across the Tasman may act as a barrier to an individual taking up employment in the other country.

The current inability of individuals to streamline and consolidate their personal retirement savings has led to some individuals paying multiple fees for the administration of their retirement savings accounts. This would apply to individuals who worked in Australia but have since relocated to New Zealand and established another retirement savings account. These costs undermine the effectiveness of policies aimed at improving retirement living standards.

The inability to consolidate accounts has also resulted in the proliferation of many small retirement savings accounts in Australia. The Australian Superannuation Minister has indicated that there is around A$13 billion in “lost” retirement savings accounts in Australia. Given the extent of labour movement between New Zealand and Australia, it is reasonable to expect that a sizeable amount of these funds could belong to individuals now living in New Zealand. The proliferation of these inactive accounts contributes to higher administrative costs, which potentially impact on the returns provided by private sector pension fund providers.

The introduction of KiwiSaver, a work-based retirement savings scheme, in July 2007 has presented an opportunity to allow for retirement savings portability and assist trans-Tasman labour market mobility.

KiwiSaver: enrolment of under 18 year olds

The KiwiSaver Act does not prescribe who can contract with a scheme provider on behalf of a child. It is at the discretion of a provider whether or not an application is accepted. This has led to disputes between parents and guardians, complaints to Inland Revenue and scheme providers, as well as complaints from children who have been enrolled without their consent. Children and their parents are able to contest an enrolment on the grounds that the contract was non-binding.

As the rapid growth in KiwiSaver membership begins to level off, a number of scheme providers are looking to increase their membership by encouraging the enrolment of under 18 year olds in KiwiSaver. As providers can decide whether to accept enrolments for under 18 year olds, there are instances where people other than parents or legal guardians have enrolled young people in KiwiSaver. People may enrol a child so the child can receive the $1,000 kick-start payment, without realising the full effects of the child’s enrolment into a scheme binding on them until they are 65.

Distributions by co-operative companies

Sections DV 11 and CD 34 of the Income Tax Act 2007 allow a resident co-operative company to deduct a distribution paid to a member if the distribution is in proportion to the sale and purchase of trading stock between the member and the co-operative. This enables co-operatives to deduct distributions on shares that members are required to hold to match the supply of trading stock to the co-operative (“supply-backed shares”).

It is not always clear at the beginning of a trading season what the level of trading stock transactions for the season will be, so members may end the trading period holding shares in excess of those required to match supply. Such excess shares are referred to in this statement as “non-transaction” shares.

Sections DV 11 and CD 34 do not apply to dividends paid on non-transaction shares, leaving the standard dividend provisions to apply. Having a different tax treatment for supply-backed and non-transaction shares does not conceptually make sense when these shares are of the same type in other respects. It would also create compliance costs for co-operatives, in particular when it is not clear at the time of payment of the dividend whether shares are supply-backed or non-transaction.

An amendment in relation to section 125 of the Companies Act 1993 is also desirable where distributions are payable on co-operative shares and the number of shares held by members varies periodically due to such things as the seasonal nature of transactions. Section 125 requires that shareholders' entitlements to receive dividends shall be determined on a date set by the board (the "record date") which must be a date within 20 working days of when the dividend is determined. If the timing for setting the dividend results in the record date being outside the period or season to which the dividend relates, members' entitlements to receive dividends may not correspond with their capital contributions over the relevant period or season. This may act as a disincentive to members contributing capital to the co-operative company.

Cancellation of BETA debits from conduit-relieved dividends

Prior to the recent international tax changes in the Taxation (International Taxation, Life Insurance, and Remedial Matters) Act 2009, controlled foreign company (CFC) income was taxed twice: first when the income was earned by the CFC and attributed back to its New Zealand shareholders; and secondly when the CFC paid a dividend to those shareholders. Branch equivalent tax accounts (BETA) are the mechanism for relieving the double taxation that could otherwise occur from having these two layers of tax.

As part of the international tax reforms, an exemption has been introduced for most types of foreign dividends received by companies. This removes the potential for double taxation, and makes it possible to phase out BETA accounts held by companies.

In February 2008, the Ministers of Finance and Revenue announced that, after the international tax changes took effect, companies would be able to carry forward and use any existing BETA debit balances for a further two years. This transitional period was intended to prevent double taxation in the rare cases where dividends have been paid significantly in advance of attributed income arising.

The existence of a small number of companies with very large BETA debit balances has recently become apparent. This is a particular issue for companies receiving conduit tax relief. In such cases, the excess BETA debits can potentially be used to offset tax on some other attributed foreign income, or even the attributed foreign income of other companies in the same group.

Under the old international tax rules, this was not too concerning, since conduit tax relief could have been used to relieve attributed foreign income in any case. But under the new international tax rules conduit tax relief is repealed, so it provides an opportunity for some companies to effectively prolong conduit tax relief for a further two years. At the upper limit, between $300m to $400m of income tax could potentially be relieved in the two-year interval between the repeal of conduit tax relief and the proposed cancellation of BETA debits. Although this sounds large, it should be noted that, under the conduit tax relief rules, there was no limit to the amount of foreign income that these companies could potentially relieve.

Binding rulings

Section 91E(4)(a) of the Tax Administration Act 1994 prohibits the Commissioner from ruling on questions of fact. An alternative interpretation was put forward that the Commissioner would be prohibited from making a private ruling on an arrangement when the description of how the law applies to the arrangement "expressly or implicitly requires particular facts to be found to exist before the description can be given". If correct, this interpretation could mean that the Commissioner would not be able to rule on matters concerning tax avoidance which could result in taxpayers being denied certainty in this important area. Such an interpretation may have implications for the validity of past rulings, as well as for the availability of future rulings, and create uncertainty and compliance costs for taxpayers in relation to current rulings applications.

Under section 91E(3)(b) of the Tax Administration Act 1994 the Commissioner "may decline to make a private ruling if the matter on which the ruling is sought is subject to an objection, challenge, or appeal, whether in relation to the applicant or to any other person". An interpretation was put forward suggesting a broad application is possible. This could mean that taxpayers would be uncertain as to whether the Commissioner would issue a ruling in relation to any number of matters, again including tax avoidance.

A broad discretion not to issue a ruling, as indicated by the alternative view of section 91E(3)(b) of the Tax Administration Act 1994, does not fit well in a tax system based on self-assessment as taxpayers may be uncertain about how the Commissioner will exercise the discretion and may feel unable to confidently enter into legitimate business arrangements.

Gift duty exemptions

The way the Estate and Gift Duties Act 1968 (the EGDA) is currently structured means that gift duty has a wide ambit, as a gift is caught by the legislation unless it is specifically exempted. Consequently, Ministers and officials receive frequent requests for legislative change to exempt certain gifts.

Transfers of assets by, and gifts made to, local and central government

The requests for exemptions for transfers of assets by, and gifts made to, local and central government, fall into the following 4 categories:

- *Transfers of assets by local authorities*—local authorities often transfer assets as part of local council restructurings, giving rise to gift duty implications. Restructuring transactions to deal with the actual or potential imposition of gift duty is resource intensive and inefficient for local authorities.
- *Gifts made to local authority trusts*—the general characteristics of local authority trusts are that the sole trustee is a local authority, and trust funds are held for charitable (or public) purposes, benefiting all or a significant portion of the public within the territory of the local authority. Gifts made to such trusts may give rise to gift duty, because of the legal and evidentiary uncertainty of such trusts registering with the Charities Commission.
- *Gifts made to local or central government*—a donor proposes to gift a number of parcels of land to both local and central government agencies, and wishes to ensure that such gifts are not subject to gift duty.
- *Gifts made to district health boards (DHBs)*—DHBs are Crown entities owned by the Crown. For income tax purposes, Crown entities are treated as public authorities and are therefore exempt from income tax. However, gifts to DHBs may be liable for gift duty. A donor wished to gift a dialysis machine to a DHB but was concerned about the potential gift duty implications.

Gifts made to donee organisations

Individuals, companies, and Māori authorities qualify for tax relief on gifts of money made for charitable, benevolent, philanthropic, or cultural purposes within New Zealand, or for certain purposes overseas. However, the exemption from gift duty applies only to gifts that are made to organisations registered with the Charities Commission. Consequently, donors may be entitled to a tax benefit for their gifts to donee organisations but then subject to gift duty. This outcome has been criticised for being inconsistent.

Distributions of property under Court order under Law Reform (Testamentary Promises) Act 1949 or Family Protection Act 1955

In 1993, estate duty was abolished for deaths occurring after 17 December 1992. Legislation effecting this abolition was passed under the Estate Duty Repeal Act 1999, which provided for the repeals of Parts 1, 2 and 3 of the EGDA.

Under repealed section 7(2) of the EGDA, it was clear that the distribution of any property in accordance with a Court order under the Law Reform (Testamentary Promises) Act 1949 or the Family Protection Act 1955 was exempt from gift duty. Since the repeal of that section, the gift duty treatment of such distributions has become unclear.

Non-resident rig operators

A temporary 5-year exemption from tax on the profits of non-resident operators of offshore exploration rigs and seismic vessels was introduced in 2004. The exemption runs from 30 June 2004 to 31 December 2009.

The exemption was introduced as part of a package of measures to encourage offshore exploration for gas. The tax exemption addressed problems caused by the way that New Zealand's double taxation agreements impacted on non-resident rig operators and was intended to remove any tax biases impeding the acceleration of offshore exploration for gas.

New Zealand firms are now drawing up their programmes of oil and gas exploration for 2010 and beyond and need certainty about the future tax treatment of rigs and seismic vessels.

Objectives

Trans-Tasman portability of retirement savings

The objective of retirement savings portability is to improve labour mobility between Australia and New Zealand by allowing individuals to transfer their retirement savings to their country of residence.

KiwiSaver: enrolment of under 18 year olds

The objective is to provide legislative clarity about who can enrol a child under 18 years old into KiwiSaver. The KiwiSaver Act 2006 does not prescribe who can contract with a scheme provider on behalf of a child. It is at the discretion of the provider whether or not an application is accepted. This has led to complaints from parents and guardians, as well as from children who have been enrolled without their consent. The proposed amendments will create rules governing the enrolment of under 18 year olds in KiwiSaver, which will reduce the incidence of complaints. If the proposed rules are not followed, Inland Revenue will be able to consider an enrolment invalid.

Distributions by co-operative companies

The objectives of the proposed amendments are to:

- tax dividends paid by co-operative companies in a coherent and, relative to other co-operatives and companies, neutral way, while minimising compliance costs;
- protect the interests of shareholders while minimising the compliance costs for the co-operative company.

Cancellation of BETA debits from conduit-relieved dividends

The proposed amendments aim to balance two objectives:

- To make the repeal of conduit tax relief effective, by removing the opportunity for companies to use large BETA debit balances to effectively prolong conduit tax relief.
- To allow BETA debits to continue to be used to prevent double taxation in cases where dividends have been paid (and taxed) significantly in advance of the underlying income being attributed (and taxed) under the CFC rules.

Binding rulings

The objective of the proposed amendments is to improve the binding rulings legislation and clarify key provisions to ensure that they apply in the manner that has been understood by Inland Revenue, taxpayers, and the tax profession since the binding rulings system was introduced. Certainty in relation to the outcome of tax laws is important for the unhindered progress of commerce and for the integrity of the tax system in a self-assessment environment.

Gift duty exemptions

The policy objective is to determine whether specific legislative exemptions from gift duty are justified for the requested gifts. In determining whether the exemptions are justified, the policy intention of gift duty (to protect against income tax avoidance, social assistance targeting, and defeating creditors) needs to be taken into account.

Non-resident rig operators

The objective is remove artificial biases to offshore oil and gas exploration, while ensuring the fiscal cost is acceptable and the integrity of the tax system is maintained.

Alternative options

Trans-Tasman portability of retirement savings

Status quo: The status quo would maintain the current restrictions on retirement savings portability. Under the status quo, an individual may transfer their KiwiSaver savings to Australia on permanent emigration, but Australian complying superannuation funds may not be transferred to New Zealand. As a result, the status quo is not preferred because it does not assist in improving labour mobility between New Zealand and Australia.

Retirement savings portability with no policy differentials applied: Under this option, retirement savings could be transferred between the KiwiSaver and Australian complying superannuation schemes without restriction. The savings would be entirely subject to the rules and policies of the host country. This option is not preferred because it does not allow the Australian and New Zealand Governments to preserve the intent behind each country's retirement savings policies.

KiwiSaver: enrolment of under 18 year olds

The main alternative to the preferred option is to allow any child under 18 years old to be signed up to KiwiSaver by their legal guardian, with or without the child's consent. This option would also provide clarity for the rules by limiting who can enrol a child to the child's legal guardians, and by ensuring that valid contracts entered into are binding on the child— that is, not subsequently contestable. However, this option does not recognise that as children grow older their intellectual capacity and maturity increases.

Distributions by co-operative companies

For the tax treatment of distributions, the three options are:

- To retain the status quo, which would mean treating dividends paid on supply-backed and non-transacting shares differently, deductible and non-deductible respectively.
- To treat dividends paid on both types of share as non-deductible.
- To treat dividends paid on both types of share as deductible (preferred option).

The first option is not preferred as that would mean dividends paid on the same class of shares would have different tax treatments in different circumstances (in some cases being deductible by the co-operative and having no imputation credits, and in other cases being non-deductible by the co-operative but carrying imputation credits). In principle, and to minimise compliance costs, all of the dividends should be treated in the same way.

The second option is not preferred as this would mean making fundamental changes to the taxation of co-operative distributions without the time for full analysis and consultation. A full-scale review of the appropriate treatment of dividends paid by co-operatives should be undertaken before making such a change. An interim measure is required because a co-operative is contemplating paying dividends on non-transacting shares in the near future.

The options in relation to the record date for co-operative dividends are to:

- provide that a special resolution of shareholders is required to set the record date;
- extend the time limit for setting the record date relative to the date when the dividend is determined, from 20 to 90 working days;
- provide that the board of a co-operative company may set a record date for determining shareholders' entitlements to receive dividends that may be any date within the financial year or other period to which the dividend relates (preferred option).

The first option is not preferred as the additional protection afforded by the requirement to obtain a special resolution is minimal. In addition, if the record date for dividends changes from time to time, it may be costly to require these changes to be approved by shareholders each time.

The second option is not preferred as it is arbitrary and could enable the record date to be set outside the period to which the dividend relates.

Cancellation of BETA debits from conduit-relieved dividends

An alternative approach would be to extinguish all BETA debits from the date that the new international tax rules take effect (i.e. from a company's first income year beginning after 1 July 2009). This would ensure that BETA debits could not be used to prolong conduit tax relief. However, to the extent that CFCs and branch equivalent FIFs not eligible for conduit relief had paid dividends under the old rules in advance of the underlying income being attributed under the new rules, this would lead to some double taxation. That would be problematic as a matter of principle, although few taxpayers are likely to be affected in practice.

Another approach considered was to limit the use of BETA debits so that they could only be used to relieve attributed foreign income from the same country as that in which the dividend that originally generated the BETA debit was paid (jurisdictional ring-fencing). This approach would prevent BETA debits earned from an investment in a high-tax jurisdiction from sheltering the income of a new investment in a low-tax jurisdiction. BETA debits could still be used to relieve the double taxation that can occur when the same investment income is taxed as a dividend and then as attributed foreign income. However, jurisdictional ring-fencing was considered to be less effective at addressing the fiscal risk than the preferred option, and would have involved higher compliance costs.

Binding rulings

An alternative option in relation to ruling on questions of fact was to give the Commissioner a general discretion not to rule in relation to questions of fact. This was not preferred as it would still create uncertainty as to whether the Commissioner can rule on tax avoidance matters.

In relation to ruling on matters that are before the courts, an alternative option would have been to base the exercise of the Commissioner's discretion on factors such as the need for consistency in relation to specific common issues, integrity of the tax system and compliance and administrative cost reduction. This was not preferred as it would provide less certainty for taxpayers.

Gift duty exemptions

An alternative option that was considered was to defer consideration of the current requests for exemptions from gift duty, and consider them as part of the wider review of gift duty that will be undertaken next year.

This option was not pursued, however, as the review of gift duty may take some time and including these gifts as dutiable gifts currently serves as a deterrent for donors making such gifts.

Non-resident rig operators

A number of options for the tax treatment of non-resident rig operators have been considered, ranging from doing away with the exemption altogether, to making it permanent. The preferred option best meets the policy objectives.

Preferred option

Trans-Tasman portability of retirement savings

Summary of preferred option

The preferred option is to allow for retirement savings portability between Australia and New Zealand, with some limitations regarding the access to transferred funds. The portability arrangements will apply to retirement savings held in a New Zealand KiwiSaver scheme and an Australian complying superannuation scheme.

There are several areas where the source country policies will continue to apply to transferred savings. These policy differences will be applied only to the savings initially transferred to either country. Any earnings on those savings in the host country will be subject to host country rules. To allow retirement savings to remain subject to some source country rules, transferred savings must be separately identifiable within an individual's retirement savings account.

The proposals to enhance portability will be voluntary for both retirement savings providers and members and there will be no enforced transfer of superannuation savings on emigration to either country.

The following policy differences will be applied through the following portability arrangements.

KiwiSaver funds transferred to Australia

KiwiSaver savings that are transferred to Australia will not be able to be accessed until the New Zealand age of eligibility for retirement (currently 65 years of age). The benefit of this condition is that it will avoid creating an incentive to move, or retire in Australia to access KiwiSaver funds at the lower Australian age of retirement, which is currently set at 55-60 years of age. It also ensures that individuals are treated equitably in terms of accessing their KiwiSaver savings, regardless of whether they reside in New Zealand or Australia. KiwiSaver savings may be transferred only to Australian complying superannuation schemes that are regulated by the Australian Prudential Regulation Authority (APRA). This would exclude the transfer of KiwiSaver funds to Australian self-managed funds, which are not currently regulated by APRA. Such a provision is required to extend the current KiwiSaver prohibition on self-managed funds in New Zealand.

Transferred KiwiSaver funds will be subject to all other Australian rules governing the Australian Superannuation Guarantee scheme. For example, Australia does not permit withdrawals for home purchases or transfers of savings to another country (other than New Zealand).

Australian savings transferred to New Zealand

Australia-sourced savings may not be used to assist with the purchase of a first home in New Zealand.

Australia-sourced savings held in New Zealand accounts will not be able to be transferred to any third country. This will preserve the current limitation on Australian residents taking their savings to other countries on permanent emigration.

Australia-sourced savings may be accessed at age 60 if a member is retired. This will ensure that an individual is not disadvantaged by moving to New Zealand from Australia.

All other New Zealand rules governing KiwiSaver will apply to retirement savings transferred to New Zealand, including hardship provisions.

Taxation and other issues

KiwiSaver member tax credits will not be recouped by New Zealand when funds are taken to Australia. Australia has also agreed not to apply any exit taxes to retirement savings taken out of Australia by non-residents before the age of retirement.

To further protect the value of savings, both countries have also agreed to exempt any transfer of savings from being taxed as dividends. Under current taxation arrangements some Australian retirement savings may be taxed on entry into New Zealand as they could be treated as a unit trust investment.

Cash withdrawals of KiwiSaver funds on emigration to Australia will no longer be permitted as a result of the portability arrangements. This will strengthen the primary policy intention of KiwiSaver—to encourage a long-term savings habit and asset accumulation by individuals who are not in a position to enjoy standards of living in retirement similar to those in pre-retirement.

Impacts

As far as possible, the portability arrangements will allow host country rules to be applied to transferred savings. The benefit of allowing host country rules to apply is that it reduces compliance costs for KiwiSaver providers who accept transferred funds as they are able to rely on their existing systems.

Consultation with industry has identified that the requirement for providers to separately identify transferred retirement savings is likely to require some system changes by providers. As a result providers who choose to accept these funds will face some additional costs. However, without the separate identification of transferred savings, portability could not be implemented as New Zealand and Australia could not apply the policy differences necessary to preserve the intent behind their respective retirement savings policies.

To minimise these costs, generally only the initial capital value of the transferred savings must be separately identified. Earnings on these funds will be subject to the host country rules. Further consultation will be undertaken with industry to ensure that compliance costs are minimised as far as possible.

The exemption from entry and exit taxes will ensure that an individual's retirement savings are not eroded as a result of making the transfer. Given that Australian retirement savings cannot currently enter New Zealand, this exemption will be fiscally neutral.

KiwiSaver: enrolment of under 18 year olds

The preferred option is to provide for different rules depending on the age of the child:

- Children under 16 years old may be enrolled only by their legal guardian(s); they may not enrol themselves in KiwiSaver.
- Children aged 16 to 17 with a legal guardian must co-sign with their guardian to enrol in KiwiSaver; they may not enrol themselves, nor can they be enrolled by their guardian without their consent.
- Children aged 16 to 17 without a legal guardian may opt in to KiwiSaver by contracting directly with a scheme provider. This means that such children, who are married, in a civil union or living with a de facto partner, will not need a co-signed application to opt in to KiwiSaver.

This approach is consistent with the definition of "guardianship" in the Care of Children Act 2004, which recognises that as children grow older their intellectual capacity and maturity increases.

Distributions by co-operative companies

For tax, the preferred option is to extend the existing deductible distribution treatment to dividends paid on non-transacting shares provided these shares represent no more than 20% of supply-backed shares for any one member. This is warranted on the basis that, at a 20% level, there is still a close relationship between shareholding and trading stock transactions. It also minimises compliance costs.

For determining shareholders' entitlements to receive dividends, the preferred option for setting a record date is that it may be any date within the financial year or other period to which the dividend relates. This date should not be able to be set retrospectively. The option would enable the board of a co-operative company to reward members that contribute capital to the company throughout the relevant period.

Cancellation of BETA debits from conduit-relieved dividends

The preferred solution is to cancel only those BETA debits that arose from conduit-relieved dividends, and allow other BETA debits to be retained and used during the two-year transitional period previously announced by Ministers. This would be almost as effective as immediately extinguishing all the BETA debits, as conduit-relieved dividends have been the primary contributor to the build-up of large debit balances. At the same time, it avoids the potential for double taxation, as conduit-relieved dividends were not taxed in the first place.

Benefits and costs

The main benefit of this option is that it would prevent a possible new specific fiscal risk—namely, the potential loss of revenue associated with a (limited) continuation of conduit tax relief for a further two years.

The main drawback of the option is that it would increase compliance costs for some companies, by requiring them to look back and identify past dividends that had been conduit-relieved.

Risks

There is a risk that the corrective legislation will not be enacted before companies begin to use BETA debits to relieve attributed foreign income under the new international tax rules. This could mean that some relief would be clawed-back retrospectively, and companies would have further tax to pay.

This risk is being managed by including the required changes in the first available tax bill. This bill should be enacted prior to companies attributing income under the new rules.

Stock of regulation

The preferred solution will require relatively minor changes to the Income Tax Act 2007—the insertion of provisions to cancel BETA debits from conduit-relieved dividends and prevent their use.

Binding rulings

In relation to questions of fact, the preferred option is that the primary rule be that the Commissioner cannot rule on the existence of facts but only on the application of tax laws based on the facts provided by the applicant.

This would be accompanied by a list of certain factual matters that cannot be ruled on such as questions in relation to the taxpayer's intention, the value of anything and what constitutes commercially acceptable practice. To remove any inference that the Commissioner is unable to rule on tax avoidance (which would defeat the main purpose of the suggested change) an exclusion for commercially acceptable practice would be limited to where that term is used in the tax legislation.

In relation to matters before the courts, the preferred option is to limit the Commissioner's discretion to decline a ruling to cases involving identical or substantially similar arrangements, facts or issues.

Gift duty exemptions

Exempting the requested gifts from gift duty is the preferred option. This is because granting the exemption for transfers of assets by, and gifts made to, local or central government would:

- Encourage donors to give property (monetary and non-monetary) to local or central government. Currently, donors making such gifts are subject to gift duty. In essence, therefore, the Crown is the recipient of both the gift and the duty.

- Ensure consistency with other exemptions contained in the EGDA. For example, of the 12 named organisations listed in section 73 of the EGDA, three are Crown entities (New Zealand Antarctic Institute, Te Papa, and the Historic Places Trust).
- Reduce compliance costs for donors wishing to make gifts to local or central government, as restructuring such gifts to ensure that they do not incur gift duty is currently resource intensive and inefficient.

Granting the exemption for gifts made to donee organisations would align the gift duty treatment with the policy for encouraging greater giving to charitable and philanthropic causes.

Given that the original policy intention of the EGDA was that distributions of property made in accordance with a court order under the Law Reform (Testamentary Promises) Act 1949 or the Family Protection Act 1955 be exempt from gift duty, granting the exemption will ensure that this intention is maintained.

Revenue implications

It is difficult to ascertain the cost of exempting transfers of assets by, and gifts made to, local or central government, because Inland Revenue does not have sufficient data. It is likely, however, that any cost would be insignificant, as gift duty currently acts as a deterrent in giving such gifts. This means that donors of such gifts would either not have given the gift, or restructured the transaction to avoid the imposition of gift duty.

The revenue cost of exempting gifts made to donee organisations from gift duty is estimated at $0.5 million per annum. This costing relates to donee organisations that are not registered charities. Registered charities already have a gift duty exemption. The costing assumes that, of the total donee organisations listed with Inland Revenue, 5% are not registered charities. This cost is on the upper bound of the cost.

Since distributions of property made in accordance with a court order under the Law Reform (Testamentary Promises) Act 1949 or the Family Protection Act 1955 have previously been treated as exempt from gift duty and the amendment is for clarification purposes, there would not be a revenue cost associated with this amendment.

Compliance costs

Approving the requests for exemptions from gift duty will result in compliance cost savings for taxpayers. The savings could be large for the exemption from gift duty for transfers of assets by local authorities. This is because local authorities currently restructure such transactions to avoid the imposition of gift duty, which is resource intensive and inefficient.

Furthermore, because of the exemptions, donors of such gifts would no longer need to file gift duty statements with Inland Revenue.

Administrative implications

There could be small administrative savings for Inland Revenue, as a result of exempting the gifts from gift duty.

Non-resident rig operators

The preferred option is to extend the temporary exemption by a further 5 years. This extension would run from 1 January 2010 to 31 December 2014.

Implementation and review

It is standard practice for Inland Revenue to issue a Tax Information Bulletin following enactment of new legislation. The Bulletin sets out the details of the new law, including examples of practical effects. There are a number of ways in which taxpayers and practitioners provide feedback on the impact of new law. Specific implementation and review aspects of some of the major initiatives follow.

Trans-Tasman portability of retirement savings

On 16 July 2009, the Minister of Finance and the Australian Treasurer signed an Arrangement on retirement savings portability. Industry groups will have a further opportunity to provide input into the portability arrangements as the legislation is developed.

The Arrangement notes that the Governments have agreed to carry out a periodic general review of the operation of the Arrangement and its relevant legislation, to assess the effectiveness of the arrangements in fostering and enhancing workforce mobility between Australia and New Zealand, and whether any changes to the Arrangement or related legislation are required to improve the operation or coverage of the Arrangement.

KiwiSaver: enrolment of under 18 year olds

Inland Revenue will develop a communications strategy to inform the public, scheme providers, employers, the media, and other interest parties of the changes to the KiwiSaver rules.

Compliance with the new KiwiSaver rules governing the enrolment of under 18 year olds and the provision of annual reports via hyperlink will be monitored by the Government Actuary as part of the normal KiwiSaver regulatory process.

Consultation

Trans-Tasman portability of retirement savings

The Treasury, the Ministry of Economic Development, Inland Revenue, and the Ministry of Foreign Affairs and Trade have been involved in developing the retirement savings portability arrangements. The Australian Treasury has also been involved to represent the Australian government in the development of the arrangements. Officials met with the Investment Savings and Insurance Association (ISI) and the Association of Superannuation Funds (ASFONZ) to confirm that the high level details of portability were workable and to discuss some of the details of how a transfer would be made.

The representatives reacted positively to the proposal and were comfortable with the general process suggested. It was noted that a provider who chose to accept transferred funds would need to make some changes to their systems so that the funds could be separately identified and the policy differences applied. However, the voluntary nature of the portability arrangements meant that they could choose not to do this if they did not want to accept the funds.

One group indicated a desire to extend the portability scheme to all retirement savings schemes, rather than just KiwiSaver funds. They also suggested that it would be desirable to allow KiwiSaver funds to be transferred to self-managed superannuation funds in Australia.

Extending retirement savings portability, particularly to KiwiSaver complying funds, is something that could be considered in the future. However, at this stage, the only channel through which funds can be transferred is through an Australian complying superannuation scheme and a KiwiSaver scheme. Any extension of the portability arrangements would also require agreement from the Australian Government as they would want to be satisfied that the fund in question operated under similar rules to the Australian compulsory superannuation scheme. Allowing KiwiSaver funds to be transferred into self-managed superannuation funds is not being considered at this point because KiwiSaver funds are not able to enter these types of funds in New Zealand.

The industry representatives also raised a number of points, including:

- what monitoring will be done to ensure providers are complying with the policy differences applied to Australia-sourced savings in New Zealand;
- ensuring that any subsequent transfers of Australia-sourced savings once in New Zealand are only made to KiwiSaver providers who offer the facility to accept these funds; and
- whether New Zealand financial advisors who advise individuals on transferring their retirement savings to Australia, need to comply with Australian legislation governing the conduct of financial advisers.

KiwiSaver: enrolment of under 18 year olds

Inland Revenue, the Ministry of Economic Development, the Treasury, the Ministry of Social Development, and the Housing New Zealand Corporation were consulted on these proposals.

KiwiSaver scheme providers and industry representatives support the need to provide clarity about the enrolment of under 18 year olds.

Distributions by co-operative companies

There has been no opportunity for general consultation with the private sector. There was consultation with several government departments—the Ministry of Economic Development, Ministry of Agriculture and Forestry, Ministry of Foreign Affairs and Trade, and Department of the Prime Minister and Cabinet. None of those consulted oppose the amendment.

Cancellation of BETA debits from conduit-relieved dividends

The proposed change to the BETA transitional arrangements relates to two earlier policy decisions—to repeal conduit tax relief, and to introduce a foreign dividend exemption for companies. Those policy changes were consulted on as part of the international tax review, with a series of discussion documents and issues papers being published during 2006 and 2007.

The Treasury has been consulted on this issue and agrees with the proposed change, described above as the preferred option.

External consultation on this issue has not been carried out. This is not unusual for proposals intended to close specific loopholes in tax legislation that potentially allow for aggressive tax planning. Typically, the priority is to resolve the problem before alerting taxpayers. In addition, in this case, the problem was only recently identified and bill deadlines did not allow time for external consultation. It was important to introduce corrective legislation as soon as possible.

Taxpayers will, of course, have an opportunity to make submissions on the proposed amendments during the select committee process.

Binding rulings

Eleven submissions were received on the issues paper entitled *The binding rulings system: legislative issues*, from

- New Zealand Law Society
- PricewaterhouseCoopers
- Ernst & Young Limited
- BellGully
- Grant Thornton
- Minter Ellison Rudd Watts
- Corporate Taxpayers Group
- New Zealand Institute of Chartered Accountants
- Zespri International Limited
- KPMG
- KensingtonSwan

Crown Law, Inland Revenue, and the Treasury have also been consulted. Inland Revenue and the Treasury agree with the recommendations.

Gift duty exemptions

The Treasury has been consulted on this proposal. Inland Revenue has also undertaken some consultation with the submitters who have made requests for exemptions from gift duty, particularly regarding the compliance cost impact of granting the exemption for transfers of assets by local authorities. Taxpayers will also have an opportunity to make submissions on the proposed amendments during the select committee process.

Non-resident rig operators

Ministry of Economic Development, Inland Revenue, and the Treasury have been consulted.