Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill

Commentary on the Bill

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OVERVIEW

People who migrate to New Zealand (or those who return to New Zealand after working overseas) frequently have contributed to superannuation schemes in their previous country of residence.

The current rules for taxing New Zealand residents on their foreign superannuation are complex and can be difficult for taxpayers to understand. In some cases, superannuation interests are subject to tax on accrual under the foreign investment fund (FIF) rules. In other cases, a person may be taxed on receipt depending on the legal structure of the foreign scheme (such as whether the scheme is structured as a company or a trust). The tax treatment differs according to which set of rules applies. As a result, it is not always clear that the rules result in a fair outcome, particularly for lump-sum amounts.

From 1 April 2014, a new cohesive set of rules will replace the current rules applying to interests in, and income from, foreign superannuation schemes.

The FIF rules will cease to apply to foreign superannuation interests.

Instead lump-sum amounts will be taxed on receipt under one of two new calculation methods: the schedule method or the formula method. The schedule method is the default method. It is designed to approximate the tax that would have been paid on accrual while the person was New Zealand-resident, in conjunction with an interest charge that recognises that the payment of tax has been deferred until receipt. The formula method taxes the person based on the actual gains while they were resident in New Zealand, again in conjunction with an interest charge that recognises that the payment of tax has been deferred until receipt.

The proposed new rules were signalled in the officials' issues paper, *Taxation of foreign superannuation*, released in July 2012. While essentially following the approach proposed in the issues paper, the rules proposed in the bill vary in some respects from those proposed in the issues paper. These variances are in response to submissions received and subsequent consultation with interested parties.

TAX TREATMENT OF FOREIGN SUPERANNUATION

(Clauses 6–9, 17, 18, 25, 40–43, 75, 103(9) –(11), 106, 115–117)

Summary of proposed amendment

The bill proposes new rules for taxing interests of New Zealand residents in foreign superannuation schemes. Under the proposed changes, interests will no longer be taxed on accrual under the foreign investment fund (FIF) rules or on distribution from a company or a trust. Instead, distributions will be taxed under a new set of rules specific to foreign superannuation.

Lump-sum amounts from foreign superannuation schemes will be partially or wholly taxed when received. The new rules will apply to cash withdrawals and to amounts transferred into New Zealand or Australian superannuation schemes. Transfers between foreign schemes will generally not be taxable. Withdrawals in the first four years after a person becomes resident will not be taxable.

After the four-year exemption period, a person’s tax liability on a withdrawal will generally be calculated using a new “schedule method”. Proposed new schedule 33 provides a particular fraction based on how long the person has been a New Zealand resident before making the withdrawal. This fraction will be applied to the withdrawal to determine the person’s taxable income. This method will approximate the tax that would otherwise have been paid on accrual while the person is resident in New Zealand.

An alternative method of calculating actual gains derived while the person is New Zealand-resident – the “formula method” – will also be available for amounts received from foreign “defined contribution schemes”. An interest factor will be applied to the value of the gains to compensate for the use-of-money (deferral) benefit.

The proposed new rules will mainly apply to people who contribute to a foreign superannuation scheme through an employer while working overseas. They will also cover non-employment-related schemes which fall within the tax definition of a “foreign superannuation scheme”. The proposed rules will not apply to periodic pensions or foreign social security, which will continue to be taxed as they are currently − that is, taxed on receipt at the person’s marginal tax rate. The proposed rules will not be expected to apply to withdrawals from Australian superannuation funds, which are generally exempt under the New Zealand-Australia double tax agreement.

Under the proposed changes, people who have transferred their superannuation savings from a foreign superannuation scheme to a KiwiSaver scheme will be able to withdraw funds from the transferred amount to pay the tax liability.

Application date

The amendments will apply from 1 April 2014.

A person may continue to apply the FIF rules to an interest in a foreign superannuation scheme if they returned FIF income or a loss in respect of that interest before the date this legislation was introduced.

As a concessionary measure, people who have made a lump sum withdrawal or transfer before 1 April 2014 will have the option to pay tax on only 15 percent of the lump-sum amount. People using this option will need to include 15 percent of the lump-sum amount as income in their 2013–14 or 2014–15 tax return. This option will satisfy the tax liability for past withdrawals in relation to which a person did not properly return income.

Background

An officials' issues paper released in July 2012[1] proposed to replace the current rules for taxing foreign superannuation with a new set of rules that would be fairer and simpler for taxpayers to understand and comply with. Further analysis of the rationale of this proposal may be found in the Regulatory Impact Statement to this bill, published on Inland Revenue's tax policy website, www.taxpolicy.ird.govt.nz.

The issues paper proposed that:

- foreign superannuation interests would be taxed on receipt rather than under the FIF rules;
- lump sums would be partially taxed based on the person's length of residence (previously called the "inclusion rate" method but under the changes proposed in the bill, this is referred to as the "schedule method"); and
- periodic pensions would continue to be taxed on receipt at a person's marginal tax rate, which is the current tax treatment.

While generally supportive of taxing foreign superannuation on receipt, submitters suggested a number of changes. The proposed changes in the bill take into account submitters' views.

In particular, an alternative method is being introduced to tax actual investment gains derived while the taxpayer is a New Zealand resident (the "formula method"). This will be available in respect of interests in foreign "defined contribution schemes" if the person has access to sufficient information.

The issues paper proposed that the new rules would apply to transfers from the 2011–12 tax year (generally from 1 April 2011). However, most submissions favoured a prospective application date. Accordingly, the new rules will generally apply from 1 April 2014. A concessionary measure allowing people to pay tax on 15 percent of

[1] *Taxation of foreign superannuation*, released on 24 July 2012.

their lump-sum transfer will be available, in addition to existing law, for transfers made before 1 April 2014.

In some cases, foreign superannuation is transferred to a locked-in New Zealand scheme. A person may be unable to access the transferred amount in order to pay the tax liability, which can result in cashflow difficulties. The issues paper invited comment on whether a mechanism for allowing tax to be paid directly from a New Zealand fund would be useful. As a practical solution, an amendment to the KiwiSaver rules will therefore permit withdrawals from KiwiSaver schemes to pay the tax liability.

Detailed analysis

New rules for interests in foreign superannuation schemes

The bill proposes new rules for all interests in foreign superannuation schemes from 1 April 2014. The new rules will apply to interests in a "foreign superannuation scheme" as defined in section YA 1 of the Income Tax Act 2007.

A new definition of "FIF superannuation interest" is included in section YA 1, which specifies the requirements by which a person may continue to use the FIF rules from 1 April 2014. The FIF rules will apply only to these interests. The qualifying criteria are discussed in more detail below.

Interests in foreign superannuation schemes which are not FIF superannuation interests will be excluded from the FIF rules through amendments to section EX 29 and a broad new FIF exemption in section EX 42B. Proposed new section EX 42B provides that interests in or rights to benefit from a foreign superannuation scheme will not be subject to the FIF rules for income years beginning on or after 1 April 2014.

Accordingly, sections CQ 5, DN 6, EX 29, EX 33 and EX 42 are being amended or repealed to remove references to the FIF rules that will no longer be required.

Proposed new section CD 36B clarifies that foreign superannuation withdrawals will not be taxed as dividends under the company tax rules. Similarly, amendments to sections HC 15 and HC 27 provide that foreign superannuation withdrawals are not subject to the trust tax rules.

Instead, all amounts from foreign superannuation schemes – whether in the form of lump sums or pensions − will be taxed on receipt.

Proposed new section CF 3 introduces new rules for taxing lump sums received from foreign superannuation schemes. Lump sums will be taxed either under the schedule approach or the formula approach.

As with other forms of income, it should be noted that the portion of the lump sum that is assessable income may impact a person's entitlements and obligations for that tax year, such as child support, Working for Families, and student loans.

When will lump-sum withdrawals and transfers be taxed?

A lump sum withdrawal will be taxable under the proposed new rules if it is a "foreign superannuation withdrawal" and if it is received during the person's "assessable period". The rules for calculating when a person's assessable period begins and ends are discussed below.

Proposed new section CF 3(1) defines a "foreign superannuation withdrawal" as an amount received from a foreign superannuation scheme that is not a pension. It includes:

- a cash withdrawal;
- a transfer from a foreign superannuation scheme into a New Zealand superannuation scheme;
- a transfer from a foreign superannuation scheme outside Australia into an Australian superannuation scheme; and
- a disposal of the superannuation interest to another person − for example, as part of a relationship property agreement or if the interest is sold to another person.

Example

James worked in the United Kingdom and has an interest in a UK scheme. He moves to New Zealand and transfers part of his interest into a KiwiSaver scheme under the UK's QROPS[2] legislation. The amount that is transferred will come within the definition of a foreign superannuation withdrawal and so James must calculate his tax liability on the transfer under the new rules.

When will lump sum withdrawals and transfers not be taxed?

Withdrawals and transfers from Australian superannuation schemes

Withdrawals from Australian schemes, and transfers from Australian schemes to New Zealand schemes, are generally not taxed under the Australia-New Zealand double tax agreement or under the forthcoming trans-Tasman superannuation portability agreement (which will take effect from 1 July 2013). This treatment will continue under the new rules.

[2] Qualifying recognised overseas pension scheme.

Transfers between two foreign schemes (rollover relief)

A transfer between two foreign superannuation schemes typically gives rise to a taxable event under current law, being a disposal of rights in the first scheme and an acquisition of rights in the new scheme.

Proposed new section CF 3(1) provides that a transfer from one foreign superannuation scheme to another foreign superannuation scheme will not be taxable. This may occur, for example, when a person disposes of their interest to purchase an annuity with a different provider, or if a person transfers from one foreign scheme to another foreign superannuation scheme in order to obtain better returns. Instead, the person will be taxed on the eventual withdrawal or payment (or transfer to an Australian or New Zealand scheme) based on the length of their New Zealand residence from when they initially acquired the interest (in the first scheme).

As transfers from Australian schemes are typically exempt, as noted above, transfers from a foreign scheme to an Australian scheme will be taxable as if the transfer was made to a New Zealand scheme.

Example

Sarah, a New Zealand resident, has an Individual Retirement Account in the United States. She wants to purchase an annuity with a different scheme provider. Under normal circumstances this would be taxable as it is a disposal and reacquisition. However, under the proposed new rules Sarah will get rollover relief so does not need to pay tax on the amount she withdraws to purchase the annuity. Any pension received while resident will be taxable under the current law.

Transfers upon death

Rollover relief will also be provided when a deceased person's interest in a foreign superannuation scheme is transferred directly to a New Zealand resident. The transfer will not be taxed. Instead, the recipient will be taxed on the eventual withdrawal or transfer (subject to the rollover relief discussed above), based on the duration of New Zealand residence of both the recipient and the deceased.

Example

Matthew moved to New Zealand in 2016 to be closer to his New Zealand-based daughter Jenny. Matthew died in 2023, seven years after migration. Matthew had an interest in a foreign superannuation fund which was acquired while non-resident. His foreign superannuation was transferred to Jenny under his will, and was not taxed at that time. Jenny withdraws the foreign superannuation in 2026, after her father's death. She is treated as having acquired the foreign superannuation interest in 2016, which is when Matthew first became resident after acquiring the interest.

No tax if lump sum is withdrawn during first four years of residence

Under the current rules, people who are transitional residents are generally not subject to tax on foreign income during the first four years of residence. The FIF rules do not apply and any withdrawals are not taxable.

Under the proposed new rules, new sections CF 3(2)(b), CW 28B and CF 3(3) provide for a four-year grace period (exemption period) during which certain people who do not meet the criteria for the transitional residents' exemption may also make a withdrawal or transfer with no New Zealand tax consequences. The exemption period will operate in a similar way to the transitional residents' exemption, to ensure consistency of treatment between all new migrants. A person may only receive the exemption period once.

The exemption period will apply for the 48-month period starting at the end of the month in which they become resident (and are not non-resident under a double tax agreement). It will apply for persons who acquired an interest in a foreign superannuation scheme while non-resident under either section YD 1 or an applicable double tax agreement. The exemption period will not be available for interests that were acquired while the person was resident in New Zealand.

Proposed new section CF 3(2)(a) confirms the current position where there is no tax on foreign superannuation withdrawals for transitional residents. The transitional residents' exemption in section CW 27 is also being retained in its current form.

Example

Amanda is deemed to have acquired a permanent place of abode in New Zealand on 16 June 2015. She is eligible for an exemption period which begins on the date she acquired her permanent place of abode. Her exemption period ends on 30 June 2019. Her assessable period begins on 1 July 2019.

Methods for taxing lump sums

Lump sums received will be taxable if they are received during the person's *assessable period*. How to calculate the assessable period is described below.

A lump sum will be partially taxed under one of the two following methods:

- the "schedule method" (the default method) in proposed new section CF 3(6)(a); or
- the "formula method" in new section CF 3(6)(b).

Proposed new section CW 28C provides that the part of the lump sum that is not treated as a gain under the schedule method or formula method is exempt income.

A person who satisfies the criteria to use the formula may choose to apply either that method or the schedule method in relation to withdrawals from a particular interest in a foreign superannuation scheme.

The criteria for using the formula method are listed in section CF 3(6)(b). The foreign superannuation scheme must be a defined contribution scheme for which a person has sufficient information about the value of the scheme and contributions made. A person must not have used the schedule method for a past withdrawal in respect of that particular interest, and must not have made a withdrawal or transfer before 1 April 2014.

Calculating the assessable period

As noted above, a person who receives a foreign superannuation withdrawal during their *assessable period* will be taxed under either the schedule or formula method.

If the person acquired the interest while they were non-resident, the assessable period will start when their exemption period ends.

If the person acquired the interest while they were resident, they are not eligible for an exemption period. Their assessable period will start when they acquire the interest.

The assessable period ends when a person becomes non-resident.

The tax liability arising under the schedule method will depend to a large extent on how long the person has been a New Zealand tax resident. This is based on the number of income years beginning in the person's assessable period. The interest factor in the formula method is also a function of years of residence. Sections CF 3(8)(c) and CF 3(15)(c) provide that a person's years of residence is calculated as the greater of 1 and the number of income years which begin in the assessable period before a person makes a withdrawal.

Example

Ben's exemption period ends on 30 September 2015. His assessable period begins on 1 October 2015. The first income year beginning in his assessable period starts on 1 April 2016. Ben leaves New Zealand and his last day as a New Zealand tax resident is 27 March 2030. His assessable period is from 1 October 2016 until 27 March 2030.

As noted above, section CF 3(1) provides that transfers between two foreign schemes will generally not be taxed. Instead, the amount will be taxed under the schedule or formula method either when it is finally withdrawn or when it is transferred to a New Zealand or Australian superannuation scheme. The schedule and formula methods are based on the duration of residence since the interest in the *first* scheme was acquired, so the assessable period will begin on the date the interest in the first scheme was acquired.

When an interest in a foreign superannuation scheme is transferred to another person, the transfer will be taxable to the transferor based on their years of residence, if the transferor is a New Zealand resident. The recipient's assessable period will begin when they first acquire the interest from the transferor, if they are a New Zealand resident. This will apply in situations such as a relationship split, where a relationship property agreement may transfer all or part of an interest in a foreign superannuation scheme from one party to the other.

For someone who loses residency and then becomes resident again, it is possible to have more than one assessable period. In this situation, the applicable assessable periods will be aggregated.

The assessable period will be determined for each specific foreign superannuation interest, based on the number of years of residence since the interest in *that* particular interest was acquired.

It is possible that a person might have different assessable periods for different interests. For example, a person migrates to New Zealand with an interest in a foreign superannuation scheme and they acquire an interest in another scheme while they are New Zealand-resident. The assessable period for the first interest will begin when their four-year exemption period ends and for the second interest it will begin when the second interest is acquired.

This will ensure that the new rules will still work as intended if an individual has interests in multiple schemes and transfers amounts at different points in time.

Schedule method

Proposed new sections CF 3(6)(a), CF 3(7), (8) and (16) provide for the schedule method. The schedule method is the default method for taxing foreign superannuation withdrawals.

The schedule method deems a certain amount of the lump-sum receipt to be investment gains, based on the person's years of residence. The approach uses fractions that represent the proportion of the lump-sum receipt to be included in assessable income. The schedule year fractions increase with years of residence. The remainder of the lump-sum receipt is not assessable.

The fractions in proposed schedule 33 are set at the rate necessary to put a person who leaves their foreign superannuation overseas in the same position as if they had instead transferred their superannuation to New Zealand and paid tax on investment gains as they accrued. Given the assumptions (including a 5% post-tax interest rate in the foreign scheme), a person should conceptually be indifferent between keeping their superannuation overseas and transferring it to New Zealand. Further discussion of the policy rationale behind the schedule method can be found in the annex to the issues paper. [3]

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[3] *Taxation of foreign superannuation*, released on 24 July 2012.

A person's assessable income will be calculated as follows:

Assessable income = (super withdrawal – contributions left) x schedule year fraction

The term "super withdrawal" is the amount of the transfer or withdrawal made by the person.

The appropriate "schedule year fraction" to use is identified by calculating the number of income years beginning in the assessable period, before the person receives the lump sum. In short, this is the number of income years which begin after the person is a New Zealand resident and after their four-year "exemption period" ends. The effect of counting a person's years of residence from the end of the exemption period is to treat them as being non-resident during the exemption period. Gains which accrue during those four years will not be clawed back and taxed on receipt.

Example

Lucy's assessable period begins on 1 August 2020. She withdraws a lump sum of \$50,000 on 27 January 2024. There are three income years beginning in Lucy's assessable period, so Lucy is required to use the schedule year fraction for year three. The corresponding schedule fraction is 14.06%, so her assessable income will be \$7,030 (being \$50,000 x 14.06%). Assuming Lucy's tax rate is 33%, she will be liable to pay \$2,319.90 of tax on her \$50,000 lump-sum withdrawal.

If the number of income years beginning in their assessable period is zero (that is, in the part-year in which their exemption period ended but before the start of the next income year), the person should use the schedule year fraction associated with year one.

Example

Karen's assessable period begins on 1 October 2020. She withdraws a lump sum of \$50,000 on 5 February 2021, which means that an income year has not yet started during her assessable period. Karen is required to use the schedule year fraction for year one because the withdrawal was made between 1 October 2020 and 31 March 2022. The corresponding schedule fraction is 4.76%, so her assessable income will be \$2,380 (being \$50,000 x 4.76%). Assuming Karen's tax rate is 33%, she will be liable to pay \$785.40 of tax on her \$50,000 lump-sum withdrawal.

Proposed new schedule 33 provides the full schedule of rates per year of residence as follows:

Schedule year	Schedule year fraction
1	4.76%
2	9.45%
3	14.06%
4	18.60%
5	23.07%
6	27.47%
7	31.80%
8	36.06%
9	40.26%
10	44.39%
11	48.45%
12	52.45%
13	56.39%
14	60.27%
15	64.08%
16	67.84%
17	71.53%
18	75.17%
19	78.75%
20	82.28%
21	85.74%
22	89.16%
23	92.58%
24	95.83%
25	99.08%
26+	100%

The "contributions left" item in the formula is effectively a deduction for contributions made for or on behalf of a person while the person is a New Zealand resident, if the contributions satisfy certain conditions. The schedule method may otherwise treat some of the New Zealand contributions as gains and would result in over-taxation.

Proposed new section CF 3(16) sets out these conditions:

- at the time the contribution is made, the person must be a New Zealand resident under section YD 1 and not non-resident under a double tax agreement;
- the contribution must be required under the rules of the foreign superannuation scheme (that is, voluntary contributions will not be eligible);

- the contribution has been subject to New Zealand tax, such as being paid out of after-tax income or subject to employer superannuation contribution tax or fringe benefit tax (for an employer contribution); and
- the contribution must not have previously been deducted under the schedule method.

The contributions that are able to be deducted are restricted in this manner because the schedule rates already include an implicit allowance for contributions. For example, for the year one schedule rate, 4.76% of the withdrawal is treated as taxable New Zealand-sourced gains and the remainder is treated as non-taxable amounts (that is, contributions as well as gains derived while non-resident).

A number of submitters on the issues paper argued that there should be no restrictions on the types of contributions that are deductible. This would not be appropriate, as it could lead to contributions being effectively deducted more than once − first, by being deducted as "contributions left" in the formula and, secondly, by then being allocated out using the schedule rates.

Formula method

The formula method is an alternative to the schedule method for people with a foreign defined contribution scheme if they have sufficient information. This method will tax actual investment gains derived while a person is a New Zealand resident (after the end of their exemption period). It was introduced following submissions on the issues paper.

Proposed new sections CF 3(6)(b), CF 3(9), (10), (11), (12), (13), (14), (15) and (16), and section YA 1 "foreign defined contribution scheme" provide for the formula method.

To use this approach, a person is required to obtain the market value of the foreign superannuation interest at the time the exemption period ends, as well as information about contributions made and other necessary information. Requirements relating to the quality of information will apply.

The formula in section CF 3(9) is:

$$\textit{Distributed gain} = (\textit{super withdrawal} \times \textit{calculated gains fraction}) - \textit{gains out}$$

"Super withdrawal" is the amount of the foreign superannuation withdrawal and "gains out" is the total amount of distributed gains previously calculated under this formula for previous withdrawals in the assessable period.

The "calculated gains fraction" is given by the formula in section CF 3(11):

$$\frac{\textit{Predistribution} + \textit{withdrawals} - \textit{transit} - \textit{contributions}}{\textit{predistribution}}$$

“Predistribution” is the value of the person’s interest in the scheme immediately before they made their foreign superannuation withdrawal. “Withdrawals” is the total amount of previous foreign superannuation withdrawals made in the assessable period. “Transit” is the opening value of the person’s interest in the scheme at the beginning of their assessable period. “Contributions” is the total amount of recognised contributions under section CF 3(16), as described above.

Interest will be charged on the amount of taxable New Zealand gains to account for the deferral benefit that the person obtains by not paying tax on accrual (similar to the use-of-money interest rules). The interest will be payable at the same rate as the average growth of the person’s superannuation interest over the number of years of residence. The interest component is contained in section CF 3(13) to (15).

Taxpayers will not be able to switch from the schedule method to the formula method.

Example

Thomas migrates to New Zealand with a foreign superannuation scheme worth NZ$100,000. Ten years after Thomas' assessable period begins, his scheme is worth $180,000 and he withdraws a lump-sum amount of $60,000. Five years after this, his scheme is worth $150,000 and he withdraws the full amount. Thomas has made no contributions to the scheme while he has been New Zealand-resident.

<u>First withdrawal</u>

The transit value is $100,000 and the predistribution value is $180,000. Since Thomas has made no contributions or taken any withdrawals, contributions and withdrawals are $0.

His "calculated gains fraction" under section CF 3(11) is:

$$\frac{\$180{,}000 + \$0 - \$100{,}000 - \$0}{\$180{,}000} = \frac{4}{9}$$

Thomas' "distributed gain" under section CF 3(9) is:

$$\left(\$60{,}000 \times \frac{4}{9}\right) - \$0 \;= \$26{,}667$$

The formula in section CF 3(13) is applied to this amount to calculate what Thomas should include as income in his IR 3. This formula requires calculating the "grow rate" which is given by section CF 3(14).

<u>Second withdrawal</u>

As before, the transit value is $100,000 but the predistribution value is now $150,000. Thomas' "calculated gains fraction" is calculated as follows:

$$\frac{\$150{,}000 + \$60{,}000 - \$100{,}000 - \$0}{\$150{,}0000} = \frac{11}{15}$$

Thomas' "distributed gain" under section CF 3(9) is:

$$\left(\$150{,}000 \times \frac{11}{15}\right) - 26{,}667 \;= \$83{,}333$$

Thomas is then required calculate his assessable income from this amount using the formula in section CF 3(13).

__Transfers to KiwiSaver schemes__

In some cases, foreign superannuation may be transferred into a locked-in superannuation scheme, such as KiwiSaver. This may lead to cashflow difficulties for the person as they cannot access any of the transferred amount to pay the resulting tax liability. To address this, new clause 14A will be inserted into schedule 1 of the KiwiSaver Act 2006. This will allow a person to withdraw an amount up to the value of the tax due from their KiwiSaver scheme.

If a taxpayer wishes to use this facility, they will be required to provide a statutory declaration to their KiwiSaver provider. The manager of the KiwiSaver scheme must be sufficiently satisfied that the requested amount does not exceed what a hypothetical tax liability could be for that person in relation to that interest. The money will be paid to the individual rather than directly to Inland Revenue, so the individual will be responsible for ensuring that their tax liability is paid.

Example

Hannah transfers her interest worth $100,000 in a UK scheme into a KiwiSaver scheme on 1 July 2014. She makes an application to the manager of her KiwiSaver scheme on 6 October 2015 to withdraw the amount of her tax liability arising from the transfer. She provides a signed statutory declaration and the documents required by the manager. The KiwiSaver manager approves the withdrawal and Hannah uses the funds to pay her tax liability.

__Transitional measures: FIF rules can continue to apply for certain interests (grandparenting)__

A new definition of a "FIF superannuation scheme" has been inserted in section YA 1 to enable the FIF rules to continue to apply to interests when the person has complied with the FIF rules by the introduction date of the new legislation.

These people will have the option to either continue to return income under the FIF rules (that is, they will be grandparented), or to apply the new rules instead.

If a person continues to apply the FIF rules, any withdrawals or transfers in relation to that foreign superannuation interest will not be taxed under the proposed new rules.

There are certain requirements that must be satisfied in order for a person to use the FIF rules in relation to a particular foreign superannuation interest. Some will be determined based on past behaviour. These criteria must be met each time a person seeks to apply the FIF rules (that is every income year from 1 April 2014):

- the person must have had an attributing interest in a FIF under section EX 29 for an income year up to and including the 2014 income year (the qualifying year);
- for the relevant income year, the FIF must have been a foreign superannuation scheme;

- the person must have calculated their FIF income or loss resulting from that attributing interest under one of the methods specified in section EX 44; and
- the FIF income or loss must have been included in a tax return filed with Inland Revenue by the date of introduction of this bill.

A person who does not meet these criteria by 1 April 2014 may not continue to use the FIF rules for the 2015 income year (commencing 1 April 2014) or subsequent years.

The effect of these criteria is straightforward. A person who complied with the FIF rules for a prior year, and filed that return before the introduction of this bill, may be grandparented under the FIF rules. If a person has two or more interests in foreign superannuation schemes, the criteria are assessed per interest (not just once for that person).

That person must then continue to return FIF income or losses in relation to that grandparented interest for all income years after 1 April 2014. If FIF income or loss is not returned in a year (in which the person still holds the interest), the interest will cease to be grandparented. The person must pay tax under either the schedule method or the formula method on any subsequent withdrawal.

A person whose foreign superannuation assets are valued at less than the $50,000 minimum threshold in section CQ 5(1)(d) may choose to apply the FIF rules in this manner, as long as the above criteria are satisfied.

Example

Aaron is a migrant to New Zealand and acquired a permanent place of abode in May 2006. He was a transitional resident until the end of May 2010. For the 2011 income year, Aaron complied with the FIF rules in relation to his foreign superannuation interest, and included the FIF income in his tax return before the filing date. He does not return FIF income in relation to this interest in the 2012 to 2014 income years because the interest qualified for a FIF exemption following a change in the foreign superannuation scheme's rules which made it locked-in. As at 1 April 2014, the criteria are still satisfied as Aaron correctly returned FIF income in the 2011 income year. Despite the exemption, Aaron will have to return FIF income in relation to his interest for the 2015 income year in order for it to remain grandparented.

Transition – low cost option for withdrawals from 1 January 2000 to 31 March 2014

Proposed new sections CZ 21B of the Income Tax Act 2007, CF 3 of the Income Tax Act 2004, and CC 4 of the Income Tax Act 1994 allow an optional method in addition to the current provisions for lump-sum transfers and withdrawals up to 31 March 2014, including past transfers that have not complied with the current law.

The alternative to using the current provisions is the option to pay tax on only 15 percent of the lump-sum amount. The remainder of the lump sum will not be assessable. This is a simple option which is intended to encourage compliance before the introduction of the new rules.

People who have complied with the existing law and paid the associated tax will not be able to reassess their position using the 15 percent option.

To use the option, a person will need to return 15 percent of the lump-sum amount in their 2013–14 or 2014–15 tax returns. Penalties and interest will not apply from the tax year in which the withdrawal or transfer was made. The 15 percent option will continue to be available in later years, but the legislation proposes that penalties and use-of-money interest will be calculated from the 2014–15 tax year. The proposed legislation will be changed to clarify that this will be done by amending the person's 2014–15 income tax return.

As with other forms of income, it should be noted that the portion of the lump sum that is assessable income may impact a person's entitlements and obligations for that tax year, such as child support, Working for Families, and student loans.

If the person does not use the option to pay tax on 15 percent of the amount, then they must apply the law as it was at the time that they made the withdrawal. The original due date for payment of tax would still apply if there is a positive amount of income under reassessment. This means that any relevant penalties and use-of-money interest will apply from the income year in which the transfer or withdrawal occurred.

MINERAL MINING

OVERVIEW

The bill proposes to repeal and replace the current rules that apply to mining companies that explore for, develop mines for or physically mine "specified minerals". There are 50 specified minerals, of which gold, silver and iron sands are the most commonly mined.

The current rules that apply to specified mineral mining are highly concessionary. The changes proposed in this bill are designed to more closely align the treatment of specified mineral miners with that of taxpayers more generally, while accommodating some of the more unique aspects of the mineral mining industry.

The proposed new rules were signalled in the officials' issues paper, *Taxation of specified mineral mining*, released in October 2012. The rules proposed in the bill vary in some respects from those proposed in the issues paper. These variances are in response to submissions received and subsequent consultation with interested parties.

The changes will apply from the beginning of the 2014–15 income year.

WHO THE RULES APPLY TO

(Clause 13)

Summary of proposed amendments

The tests of what types of activities and sources of income a person has to receive in order to be classified as a “mineral miner” are similar to those currently in place. However, the proposed new rules will apply to persons, not just companies.

Application date

The amendments will apply from the beginning of the 2014–15 income year.

Key features

The proposed rules will apply to all “mineral miners”. The definition of “mineral miner” in section CU 6 applies to all forms of legal entity. The current rules apply only to “mining companies”. Because the new rules are less concessionary, it is expected that miners will adopt different structures to carry out their operations. The new definition therefore applies to all persons:

- whose only or main source of income is from mining-related activities; or
- whose only or main activity is mining-related.

The relevant sources of income or activities are unchanged from the current legislation, as it is considered these capture the appropriate parties.

To ensure this consistency, the proposed rules also largely transpose the existing definitions of “mining operations, “associated mining operations” (proposed section CU 7) and the definition of what were “specified minerals”, but are now defined as “listed industrial minerals” (proposed section CU 8).

WHAT IS "INCOME" TO A MINERAL MINER?

(Clause 13)

Summary of proposed amendments

Under the proposed new rules, a mineral miner can derive income from four main sources:

1. amounts derived from their mining operations or associated mining operations;
2. amounts derived from the disposal of land;
3. consideration from disposing of a mineral mining asset; and
4. amounts recovered under a special claw-back rule that applies if deductions are taken when, in hindsight, those deductions should not have been taken immediately, but spread over the life of the mine.

Application date

The amendments will apply from the beginning of the 2014−15 income year.

Key features

Amounts from mineral mining operations (sections CU 1 and CU 7)

As mentioned previously in "Who the rules apply to", the definitions of "mining operations" and "associated mining operations" are consistent with the current legislation. "Mining operations" covers exploring for minerals, performing development work, extracting minerals and other work directly related to mining. It is important to note that work done on a "service for reward" basis for a mineral miner will not be covered because the person performing the service will not be a "mineral miner" and is therefore outside the ambit of these rules.

"Associated mining operations" covers activities carried on in association with mining operations and include accumulation, initial treatment and transport of minerals up to a saleable form or to a stage where they are ready to be used in a manufacturing operation.

Disposal of land (section CU 2)

Under the proposed rules, land will effectively become revenue account property of a mineral miner. This means the miner will be allowed a deduction for the relevant land in the year of disposal and the amounts derived from disposal will be treated as income – also in the year of disposal. This will give rise to either a net gain or loss on disposal that will be reflected as either income or a deduction.

Disposal of a mineral mining asset (section CU 3)

Consideration received from the disposal of a "mineral mining asset" will be treated as income to a mineral miner. "Mineral mining asset" is defined in section CU 9 as a mining or prospecting right, an exploration, prospecting or mining permit or a share or partial interest in any of these. It does not include land. "Mining or prospecting right" is broadly defined to effectively include any authority related to exploring, searching or mining for minerals and includes any interest in such authority.

It is important to note that proposed section CU 3 is over-ridden by proposed section CX 43, which relates to farm-out arrangements. A "farm-out arrangement" is defined in section YA 1 and is being modified so that it applies to a mineral mining context. At its most simplistic level, a farm-out arrangement is one where a person (the farm-in party) agrees to incur expenditure in doing work in a permit area and, in return, the existing permit holder (the farm-out party) agrees to surrender part of their interest in that permit.

Section CX 43 provides that farm-in expenditure under a farm-out arrangement is excluded income of the mineral miner that is the farm-out party. The intention behind the interaction between these sections is that a person who sells an interest in, a permit will be treated as having disposed of a mining asset and the proceeds will be treated as income. By contrast, if the "farm-in party" instead agrees to incur costs in relation to the permit area, the amount spent by that person will be treated as excluded income of the first party.

Proposed section CU 5 also clarifies that:

- a partner is treated as having the relevant share of assets owned by the partnership; and
- reference to a disposal of an asset includes the disposal of a part of an asset.

Claw-back rule (section CU 4)

The deductions available to a mineral miner under the proposed rules are discussed in more detail below. However, as a general rule, "exploration expenditure" will be deductible to a miner, whereas "development expenditure" must be capitalised and spread over the life of the mine created. This arguably creates incentives to a miner to prefer an "exploration expenditure" categorisation because of the immediate deduction available. It is also recognised that there will be expenditure incurred that, at the time, may be "exploration" or may be "development" – with its true categorisation only becoming apparent in hindsight.

To deal with these situations, a recovery or claw-back rule will apply to expenditure that is deducted as exploration expenditure, but which actually results in an asset that is used for commercial production. In order for the claw-back rule to apply, the following criteria must be met:

- the expenditure is treated as exploration expenditure;

- the mineral miner is allowed a deduction for it;
- the year is later than the 2013−14 income year;
- the expenditure results in an asset; and
- the miner uses that asset for or in relation to the commercial production of a mineral.

The amount of income is the amount of expenditure that produced the asset, but is capped to the amount of the deduction taken, and is allocated to the income year in which the relevant asset is used in commercial production.

Appropriated income

Under the current rules, a mining company can deduct amounts appropriated for future development or exploration expenditure. This ability to deduct for future expenditure is one of the more concessionary aspects of the current rules and is being repealed as part of these changes.

It is recognised that mining companies may have appropriated significant amounts under the appropriation rules. Therefore, the repeal of these rules could result in those companies having larger than expected income tax liabilities for the 2014−15 income year when the appropriated amounts are added back as income. To alleviate this, proposed section CZ 28 allows a mineral miner with an income tax liability as a result of this repeal to allocate the income equally over the 2014−15 and 2015−16 income years.

DEDUCTIONS FOR A MINERAL MINER

(Clause 27 and 35)

Summary of proposed amendments

The bill proposes that most expenditure of a mineral miner be divided into the following categories, dependent on the phase of the mine in question:

- mining prospecting expenditure – immediately deductible;
- mining exploration expenditure – immediately deductible, subject to the claw-back rule discussed above;
- mining development expenditure – deductible over the life of the mine created;
- mining rehabilitation expenditure – deductible in the year it is spent.

Other types of expenditure are:

- expenditure on land – deductible in the year the land is disposed of;
- expenditure on the acquisition of mineral mining assets – timing of deduction dependent on the stage of the operations; and
- all other expenditure – subject to general tax rules, including capital/revenue distinction when appropriate.

Application date

The amendments will apply from the beginning of the 2014−15 income year.

Key features

Under the proposed new rules, all of the main types of expenditure will be treated as mutually exclusive. This means that prospecting, exploration, development and rehabilitation expenditure will each have specific exclusions for any amounts that fall into one of the other categories. Equally, "residual expenditure" is excluded from all of the main classes of expenditure. To accommodate this, "residual expenditure" in section YA 1 will be extended to include appropriate types of mining expenditure.

Proposed section DU 9(2) also clarifies that no expenditure covered by the definitions of exploration, development or rehabilitation expenditure can be reclassified as prospecting expenditure. This is necessary because prospecting expenditure is immediately deductible and not subject to any claw-back rule.

As expenditure will generally relate to a "permit area", the definition of that term has been expanded to include mineral mining activities.

Mining prospecting expenditure (sections DU 1(1)(a) and DU 10)

A mineral miner will be allowed an immediate deduction for mining prospecting expenditure. This term is defined in proposed section DU 10 to mean expenditure incurred directly in relation to a prospecting right or "mining prospecting information", which is defined consistently with the corresponding term in existing legislation.

Specifically excluded from "mining prospecting expenditure" are the costs of land, plant, machinery, expenditure that falls into on the other main classes of expenditure and "residual expenditure". Plant and machinery acquired will be subject to the general capital/revenue distinction. To the extent they are capital and depreciable, they will be subject to the normal depreciation rules at the appropriate rate.

Mining exploration expenditure (sections DU 1(1)(b), DU 6 and DU 11)

"Mining exploration expenditure" will also be immediately deductible, except when the claw-back rule described previously applies. In that case, the exploration expenditure will be effectively reclassified as "mining development expenditure" and is subject to the spreading rule in proposed section DU 6. The spreading rule is explained in more detail below.

The definition of "mining exploration expenditure" is largely taken from existing legislation. However, it also specifically excludes land, plant and machinery (as well as the other classes of expenditure and residual expenditure).

Mining development expenditure (sections DU 6, DU 7, DU 8 and DU 12)

"Mining development expenditure" will be capitalised and deducted over the life of the mine. It is defined to mean expenditure:

- incurred in preparing a permit area of mining operations or associated mining operations; or
- on operations carried out on a permit area for deriving income, including mining, work directly related to mining and earthworks.

It is important to note that, in either case, the expenditure must relate to a permit area.

Proposed section DU 12(2) contains a number of specific inclusions, such as acquiring mining permits, obtaining resource consents, establishing mine infrastructure (including, plant, machinery, vehicles, production equipment and storage facilities) and costs of providing utility services to the permit area.

Specifically excluded from the definition is the cost of land and any expenditure incurred after commercial production has begun on property that has an estimated useful life independent of the mine. This is designed to capture ongoing expenditure of the mining operations, including plant and machinery purchased after commercial production has begun, which should be deducted according to the estimated useful life of that asset.

The rationale for these rules is in accordance with general tax principles: amounts spent on the creation of an asset should be capitalised and deducted over the course of that asset's useful life. So, for example, expenditure on earthworks undertaken to increase the production capacity of a mine should be spread over the life of the mine created. By contrast, expenditure on a vehicle that has not contributed to the creation of the mine asset (because it was purchased after the mine was operational) should be deducted over its own estimated useful life.

Spreading rule

Proposed sections DU 6 to 8 set out the spreading rule that applies to development expenditure.

The starting premise is that a deduction for the relevant expenditure is denied except in accordance with the spreading rule. Deductions are denied until the mineral miner starts to use the permit area to derive income. The formula for spreading is:

$$\text{rate x value}$$

"Value" is the adjusted tax value or the diminished value of the expenditure, as appropriate.

The relevant "rate" is the nearest rate to those set out in the schedule 12, column 1 (for the diminishing value rate) and column 2 (for the straight line rate). To arrive at the rate, it is necessary to perform the calculation in proposed section DU 8:

$$\frac{100\%}{\text{Assumed life}}$$

"Assumed life" is a self-assessed determination of the life of the mine. For a mineral miner that uses an amortisation period for the mine for accounting purposes, the assumed life cannot be less than the accounting amortisation period. If a mineral miner is not required to use an amortisation period for their accounts, they must reasonably estimate the period they expect the permit area to accommodate commercial production. The assumed life is capped at 25 years from the later of the date commercial production begins in the permit area or the date in which the expenditure is incurred.

As a mine develops, a miner will continually reassess the assumed life of that mine. It may be that an additional mineral deposit is discovered, which increases the assumed life, or that some factor results in that assumed life reducing. Because the estimated assumed life is not a static concept, proposed section DU 8(3) requires a miner to re-estimate this figure for each year. The figure arrived at applies from the start of the next income year.

Example

If a miner's initial estimate is that commercial production will last 8 years, and they elect to use the straight-line method, their rate will be:

$$\frac{100\%}{8}$$

=12.5 % (this corresponds with a rate in schedule 12, column 2)

This estimate is reassessed and confirmed every year until year 4, when an additional deposit is discovered, pushing out the assumed life for a further 6 years (so 14 years in total and 10 years from the current year). The new rate will be:

$$\frac{100\%}{10}$$

=10%

This new rate will apply from the start of year 5. At this stage it is anticipated that half of the original expenditure will have been deducted, with the half remaining being spread over the subsequent 10-year assumed life.

Proposed section DU 7 clarifies that the spreading calculations have to be performed in respect of particular expenditure over the spreading period. The spreading period starts from the later of the income year in which commercial production starts in a permit area or the income year in which the expenditure is incurred – and ends at the expiry of the assumed life of the mine.

Mining rehabilitation expenditure (sections DU 2 and DU 13)

Under the proposed rules mining rehabilitation expenditure will be deductible in the income year in which the amount of expenditure is actually paid (as opposed to "incurred"). To recognise the fact that this payment may occur after the conclusion of a miner's income-earning activity, a tax credit may be generated under proposed section LU 1 for the corresponding year (this tax credit is explained in more detail below).

"Mining rehabilitation expenditure" is defined to mean rehabilitation expenditure incurred on mining permit land carried out in order to comply with the miner's obligations under their permit or the Resource Management Act 1991. It covers amounts paid during or after the miner's operations have ceased, but excludes the cost of the land itself.

Land (section DU 3)

As mentioned above, consideration derived from the disposal of land will be treated as income of the miner. Proposed section DU 3 sets out the deductions available for land purchases. A miner will be allowed a deduction for land or interests in land that it acquires. However, the rule is limited to land that is part of the mineral miner's permit area, the site of mining operations or associated mining operations. Any expenditure for which the miner has a deduction before disposing of the land or interest in land will be excluded.

The deduction will be allowed in the year the land or interest in land is disposed of. This means that the timing of this deduction will match any income derived under proposed section CU 2 and so a net income amount or deduction will be available in that year, depending on whether the land is sold for a profit or loss. Although land generally does not decline in value, a miner may have paid a premium for the land based on its perceived mineral deposits. If those deposits are then removed, it is possible that the land will be sold for less than its purchase price.

Again, it is recognised that this disposal may be the final act of a miner's operations, so could occur in a period when no income-earning activity takes place. So, like rehabilitation expenditure, any loss attributable to land sales may be eligible for a tax credit under proposed section LU 1.

Mining assets and farm-out arrangements (sections DU 4 and DU 5)

The bill proposes that expenditure on the acquisition of a mineral mining asset will either be immediately deductible or deductible over the life of the relevant mine, depending on the timing. If the asset is acquired before the date a mining permit for the permit area to which the asset relates, then it will be deductible. This is because, if a mining permit has not been obtained, the area will still be in the prospecting/exploration stage. Once a mining permit has been obtained, the holder of that permit is intent on developing the area for commercial production. The purchaser is therefore buying a functioning asset, which should be depreciated over its useful life. The way this is achieved (through proposed section DU 4(2)), is to treat the purchase of a mining asset after the mining permit is granted as "development expenditure", so it will be spread over the life of the mine.

Proposed section DU 4(3) clarifies that "expenditure" for these purposes does not include the actual application costs for a mining right or permit.

As a result of sections CU 3 and DU 4, the purchaser of a mineral mining asset will be eligible for a deduction for that expenditure (either immediately or over time) and the person disposing of that asset will treat the consideration received as income.

On the other hand if a person, instead of acquiring the mineral mining asset outright, agrees to incur farm-in expenditure, proposed section DU 5 clarifies that this expenditure is to be treated as if it were the applicable class of mining expenditure. If, for example, the expenditure was classified as development expenditure, the farm-in party would be allowed a deduction for that amount over the life of the relevant mine. As the existing rights holder is not getting any money from the farm-out arrangement, the expenditure of the farm-in party is excluded income to the farm-out party (as discussed above in proposed section CX 43).

Other types of expenditure

Other types of expenditure not covered by the specific rules in subpart DU will be covered by the appropriate general rules set out in the Act. This includes the application of the capital/revenue distinction in determining whether expenditure is immediately deductible, deductible over time or not deductible.

TAX CREDITS FOR MINERAL MINERS

(Clause 88)

Summary of proposed amendments

A new subpart LU is proposed to allow mineral miners a refundable credit in circumstances when there is a tax loss due to a loss on disposal of land or because rehabilitation expenditure has been incurred. The value of this credit is limited to the income tax liability attributable to the relevant permit area.

Application date

The amendments will apply from the beginning of the 2014−15 income year.

Key features

It is likely that the natural life cycle of a mine will conclude with mining ceasing, the land being restored and then sold. This scenario may result in a mineral miner incurring rehabilitation expenditure or a loss from a land sale after the income-earning activities have ceased. This would see a miner having deductions and losses, but with no prospect of future income to offset those losses against.

To recognise this, proposed section LU 1 sets out when a tax credit is available to a mineral miner. The person must have either:

- incurred an amount of rehabilitation expenditure; or
- disposed of land for a loss –

and, after taking those amounts into account, have a tax loss for the year.

The credit is the tax rate multiplied by the "expenditure or loss" (section LU 1(2)). The amount of "expenditure or loss" will be capped at the lesser of:

- the total of the relevant losses; and
- the person's loss for the year (section LU 1(3)).

The total amount of the credit will also be limited to the historical income tax liability the miner has in relation to the permit area. This is to prevent credits that may exceed the tax paid from the mine in question (section LU 1(4)).

Proposed section LU 1(5) also clarifies that any loss giving rise to a credit does not form part of a tax loss component or net mining loss of the miner. This is to prevent a miner claiming a credit under subpart LU but also using the same loss to offset any future income.

Proposed section LU 1(6) sets out that the credit generated is refundable.

ANTI-AVOIDANCE RULES FOR MINERAL MINERS

(Clause 61)

Summary of proposed amendments

The current anti-avoidance rules in section GB 20 that apply to petroleum miners are being extended to also apply to mineral miners. The broadening of these rules is to reflect the similarities between the two industries, particularly in relation to the tax avoidance risks that they represent. It is considered preferable to have specific rules that apply so the industry has some clear guidance in this area.

Application date

The amendments will apply from the beginning of the 2014−15 income year.

CONSEQUENTIAL AMENDMENTS

(Clauses 10−12, 19−24, 28, 34, 37, 39, 56−60, 64 76−85 and 103(2), (3), (5) – (7), (12), (14), (15), (17) – (36), (40) –(43), (47−(51))

Although it is not intended to alter the current mineral mining rules in relation to loss ring-fencing, loss carry-forward and shareholder continuity, consequential amendments to Part I of the Act are necessary to delete provisions no longer relevant (such as those that relate to mining holding companies) and amend references to "mining company" so the rules apply, where relevant, to all entity types.

Other consequential amendments are also proposed to the following definitions in section YA 1:

- Asset
- Associated mining operations
- Commercial production
- Dispose
- Farm-out arrangement
- Holding company
- Income from mining (definition repealed)
- Initial treatment
- Listed industrial mineral (definition inserted)
- Mineral mining asset (definition inserted)
- Mining company (definition repealed)
- Mining development expenditure
- Mining exploration expenditure
- Mining holding company (definition repealed)
- Mining operations
- Mining or prospecting right
- Mining outgoing excess (definition repealed)
- Mining permit
- Mining permit area (definition repealed)
- Mining prospecting expenditure (definition inserted)
- Mining prospecting information
- Mining purposes (definition repealed)
- Mining rehabilitation expenditure (definition inserted)
- Mining share (definition repealed)
- Mining venture (definition repealed)
- Net mining loss
- Non-resident mining operator (definition repealed)
- Permit area
- Prescribed amount (definition repealed)
- Prescribed period (definition repealed)
- Prescribed proportion (definition repealed)
- Reinvestment profit (definition repealed)
- Resident mining operator (definition repealed)

- Residual expenditure
- Schedular income
- Specified mineral (definition repealed)

Application date

The amendments will apply from the beginning of the 2014−15 income year.

OTHER POLICY MATTERS

ANNUAL CONFIRMATION OF INCOME TAX RATES

(Clause 3)

Summary of proposed amendment

The bill sets the annual income tax rates that will apply for the 2013–14 tax year. The annual rates to be confirmed are the same that applied for the 2012–13 tax year.

Application date

The provision will apply for the 2013–14 tax year.

Key features

The annual income tax rates for the 2013–14 tax year will be set at the rates specified in schedule 1 of the Income Tax Act 2007.

WORKING FOR FAMILIES TAX CREDITS

(Clauses 63, 89−98 and 118)

Summary of proposed amendments

Amendments to the provisions for Working for Families (WFF) tax credits seek to clarify and improve the provisions to ensure they operate as intended. The proposed amendments are consistent with the policy behind previous amendments, including the broadening of the definition of family scheme income to prevent people structuring their income to inflate their entitlements.

Application date

The amendments will generally apply for the 2014−15 and later tax years, with some applying from the date of Royal assent.

Key features

A number of specific changes to the WFF tax credit provisions are proposed:

- Sections MD 1, 2 and 16 are being amended to ensure that the formula for calculating the family credit abatement produces the correct result in all cases, when it relates to a family that receives a parental tax credit in a lump sum for a child born within 56 days of the end of the tax year.
- Section MB 4 provides that income attributable to shares in a close company held by dependent children will be included in family scheme income. This addresses a situation where a person could reduce their income by allocating shares in a close company to their dependent children. It also clarifies how dividends from close companies are treated.
- Section MB 7 ensures that when calculating family scheme income the attribution of trust income takes into account only settlors who were alive in the income year.
- Sections MA 8 and MB 1 clarify that family scheme income is based on a person's net income and is further adjusted as provided by subpart MB.
- Section GB 44, the anti-avoidance provision, is being clarified to ensure that all arrangements that have a purpose of favourably affecting an entitlement to WWF tax credits are covered by the provision.
- Section MD 12 clarifies the days when a person is entitled to a parental tax credit by reference to the criteria in section MD 11.
- The reference to "fortnightly instalments" is being removed from section MD 13 and regulation 8 of the Health Entitlement Cards Regulations 1993, as instalments can be paid weekly as well as fortnightly.
- The list of defined terms in section MC 6 is being updated.

Background

WFF tax credits are provided to the principal caregiver of dependent children based, among other things, on their level of family scheme income for a tax year. WFF tax credits are abated when family scheme income exceeds $36,350 and are abated at the rate of 21.25 cents per dollar. The tax credits can be received as a lump sum at the end of the tax year or in weekly or fortnightly instalments throughout the year.

The WFF tax credits are:

- Family tax credit − for principal caregivers of dependent children.
- In-work tax credit − for principal caregivers of dependent children who are not receiving an income-tested benefit and who meet the full-time earner requirements.
- Parental tax credit − for principal caregivers of a newborn child who are not receiving a social assistance payment and not receiving paid parental leave.
- Minimum family tax credit − for principal caregivers of dependent children who meet the full-time earner requirement and do not receive income from certain sources such as an income-tested benefit.

The provisions have been amended a number of times over the last decade including as part of the rewrite of the Income Tax Act. The names of WFF tax credits and some criteria were amended in 2004. The parental tax credit abatement formula was introduced in 2007 (with effect from 1 April 2008). The definition of family scheme income was broadened as part of Budget 2010, with effect from 1 April 2011. This included a new provision for attributing the income of a trust and trust-owned companies to the settlors of a trust.

Detailed analysis

Calculation of parental tax credit and abatement

The parental tax credit is a payment covering the first eight weeks (56 days) after a child is born (the parental entitlement period). Section MD 11 indicates that a person is entitled to the parental tax credit if they meet the requirements in section MC 2, and for any day within the parental entitlement period they or their spouse are not in receipt of a social assistance payment. They must also not receive paid parental leave for that child. Section MD 12 calculates the amount of parental tax credit and is being amended to clarify that the number of days is based on the days a person meets the entitlement criteria in section MD 11.

The maximum amount a person is entitled to is then abated by family scheme income using the main abatement formula in section MD 13.

If a principal caregiver has a child born within the last 56 days of the tax year, and receives the parental tax credit as a lump sum in the tax year the child is born, there is an additional abatement calculation reflecting that part of the parental entitlement period falls in the next tax year. For example, for a child born on 1 March, the main abatement formula would calculate abatement for the month of March only but the parental tax credit is based on entitlement for the period 1 March to 25 April. The formula in section MD 16 is required to calculate abatement for the period 1 March to 25 April in this situation.

The formula in section MD 16 is being replaced to clarify how it operates in calculating an additional abatement (in the above example for the period 1 April to 25 April). It also improves how the formula works in very unusual circumstances. The formula calculates additional abatement for the parental tax credit based on the rate of abatement that applied on the last day of the last entitlement period in the tax year the child was born. If there was no entitlement period in the tax year the child was born, the rate of abatement is based on the first day of the first entitlement period in the following tax year. The result of the proposed formula in section MD 16 is that the same amount of abated parental tax credit is received regardless of when in the year a child is born.

Family scheme income of major shareholders in close companies

Section MB 4 is being replaced with an expanded formula and additional definitions. The current formula determines the amount that is included in family scheme income when a person is a major shareholder in a close company on the last day of the company's balance date for financial purposes. The amount is based on the proportion of the company's income for the accounting year that reflects the person's proportional holding of company shares, and reduced to reflect dividends paid.

A major shareholder is someone who owns or controls, directly or indirectly, at least 10 percent of the shares of a close company. While a major shareholder includes a person who controls, including indirectly, at least 10 percent of the shares, the formula in section MB 4 only refers to shares held by the person. When shares are held by a dependent child of a principal caregiver or their spouse, the current formula would attribute the relative share of the income of the company to the dependent child. Section MB 11 includes resident passive income derived by a dependent child in family scheme income, including dividends received from a close company, but not attributed income under section MB 4.

The replacement formula continues to apply only when a person is a major shareholder in a close company on the last day of the company's balance date. However, a person who is a major shareholder in a close company will be unable to reduce their attributed income under section MB 4 by transferring ownership of the shares to their dependent child, or dependent child of their spouse, while still retaining control of the shares.

The income attributed under section MB 4 will be the greater of zero or the amount given by the formula. This clarifies that the result under section MB 4 cannot be a negative amount (in situations when dividends exceed attributed income).

The formula allocates the amount of company income, less total dividends paid by the company, to shareholders based on their proportional holding. Dividends are deducted from the amount of company income as dividends received are already included in family scheme income through section MB 1 (net income of a person) or section MB 11 (resident passive income of a dependent child). The proportion of shares for a person is based on the number of shares held directly and the number of shares attributed to them. Attributed shares are shares held by a dependent child of the person or the person's spouse, and they are shared among the relevant number of major shareholders connected to the dependent child.

Family scheme income of settlors of trust

Section MB 7 attributes income where a person is a settlor of a trust. Under this section the income of the trust (and trust-owned companies) is allocated in equal portions to the settlors of the trust when calculating family scheme income. A settlor is a person who, at any time, transfers value to the trust or for the benefit of the trust. Settlors can include people who have gifted property to the trust and since died. The formula is amended so that the attribution of income takes into account only settlors who are alive during the income year. This includes people who were alive for only part of the income year, including the person for whom family scheme income is being calculated.

Arrangements involving tax credits for families

Section GB 44 currently refers to a person (a claimant) entering into an arrangement and the Commissioner's ability to reduce the claimant's tax credit. It is unclear from the wording whether the section would cover an arrangement entered into by a spouse of a principal caregiver, if the principal caregiver was not a party to the arrangement, yet benefited from an increased entitlement to WFF tax credits. For example, a spouse is a major shareholder in a close company and the principal caregiver is not, and the spouse enters into an arrangement with the company to reduce the amount of family scheme income attributed to them in that year. The amended drafting of the section is more closely aligned with the style of other anti-avoidance provisions.

Definition of family scheme income

Both the change in section MA 8 and the change in section MB 1(1) highlight that a person's entitlement to a WFF tax credit is based on a person's family scheme income. Furthermore, family scheme income is based on a person's net income (calculated under section BC 4) and adjusted as provided by subpart MB. This replaces the current wording in section MB 1(1) which referred to entitlement being based on "the net income (the family scheme income)". The current wording is unclear and the amendment is intended to make the provisions more accurate.

NOTIONAL INTEREST UNDER IFRS

(Clauses 38 and 55)

Summary of proposed amendment

In some situations International Financial Reporting Standards (IFRS) accounting rules require a special treatment for interest-free and reduced-interest loans. This can involve the recognition of a one-off adjustment to the value of the loan and notional payments (or receipts) of interest. These adjustments do not reflect actual payments made between parties, but rather are bookkeeping adjustments required for accounting purposes.

Proposed amendments to section EW 15D clarify that these bookkeeping adjustments do not have a tax effect. The amendment confirms that positive adjustments are not taxable and negative adjustments are not deductible.

The amendments will apply only to loans that begin with below market interest rates. The treatment of loans that subsequently pay below market interest (for example, because of movements in market interest rates) is unaffected. Loans that pay no explicit interest but involve increasing repayment amounts as a substitute for interest (for example, deep-discount bonds) are also unaffected.

Under the financial arrangement rules any deduction for notional expenses and any notional income returned will be reversed when a loan terminates. However, a loan may not terminate for some time. As such, proposed new section EZ 64 is a transitional provision that requires a taxpayer who has been claiming deductions for notional adjustments (or paying tax on them) to perform a change of spreading method adjustment in their 2014−15 income year. This proposed section brings forward any reversal.

Application date

The proposed changes will apply from the beginning of the 2013−14 income year.

OVER-CREDITING OF IMPUTATION CREDITS IN EXCESS OF FIF INCOME

(Clauses 15 and 86)

Summary of proposed amendment

Amendments are being made to address a mismatch arising under the tax rules in relation to imputed dividends paid by Australian companies under the trans-Tasman imputation rules. This mismatch arises because imputation credits are calculated on the basis of the dividend paid but income tax arises only on the foreign investment fund (FIF) income.

New section LE 8B limits the amount of the tax credit to the shareholder receiving the imputed dividend to the amount of imputation credits they would have if the imputation credits were calculated on the basis of the shareholder's FIF income from that company. The amendments apply only if the dividend received from the company exceeds the amount of FIF income.

Application date

The amendment applies for tax years commencing 1 April 2014.

Key features

New section LE 8B limits the amount of the tax credit to the shareholder receiving an imputed dividend from an Australian company to the amount of imputation credits they would have if the imputation credits were calculated on the basis of the resident's FIF income from that company. The section will apply only if the dividend amount exceeds the amount of FIF income.

In addition, a new section CV 18 is being added to ensure that the shareholder's tax liability is calculated correctly in relation to the FIF income and imputation credits by providing that a person's income includes the amount of imputation credits under new section LE 1(8B). In the absence of section CV 18, a shareholder subject to section LE 1(8B) would be under-taxed on their FIF income.

Background

The trans-Tasman imputation rules permit an Australian company to operate an imputation credit account (ICA). An Australian ICA company that has paid New Zealand tax can attach imputation credits to dividends paid to New Zealand shareholders. Wholly owned Australian and New Zealand companies can also form a trans-Tasman imputation group. New Zealand tax paid by a member of the group will generate imputation credits that can be distributed to a New Zealand shareholder. The amount of imputation credits that a particular shareholder receives is determined with reference to the actual dividend paid by the company. In the domestic context, this works as intended.

However, an issue arises when a New Zealand-resident shareholder receives a dividend with imputation credits attached that is paid from a closely held Australian company. The New Zealand resident's investment in that company will generally be an attributing interest under the FIF rules. Under the FIF rules, a New Zealand resident is taxed only on the deemed FIF income; the actual dividend is disregarded.

A mismatch therefore arises, with imputation credits being calculated on the actual dividend paid but income tax arising only on the FIF income. If the dividend is of greater value than the amount of FIF income, the shareholder will receive excess imputation credits, which they can use against the tax on their other income, such as salary and wage income. This is inconsistent with the policy intent. The amendment is intended to address this mismatch.

BAD DEBT DEDUCTIONS FOR HOLDERS OF DEBT – COMPLIANCE

(Clauses 26, 29)

Summary of proposed amendment

Two changes are being made to the bad debt deduction rules in the Income Tax Act 2007.

The first change is a measure to reduce compliance costs. It will make the law fairer for taxpayers by allowing them to take bad debt deductions in certain situations when they would ordinarily be entitled to them on the cessation of the arrangement, but for technical compliance issues.

The second change is a base maintenance measure and is discussed in the following item.

Application date

The compliance changes apply from the 2008–09 year, subject to a grandparenting provision so that taxpayers who relied on the current law will not be able to re-open previous years' tax assessments to take advantage of new provisions for prior years.

Background

One function of the bad debt write-off rules is to ensure that taxpayers are not taxed on amounts which may have been derived and included as assessable income, but are never actually received. If deductions for bad debts were not allowed, taxpayers would pay too much income tax because they would be assessed on income which substantively was not received.

There is a required process for taking bad debt deductions. Bad debts for amounts owing under a financial arrangement must be written off before the financial arrangement ends (for instance, by liquidation). This means that if a taxpayer fails to take a bad debt deduction before that time, a bad debt deduction cannot be taken later.

Currently, the tax rules require that where a debtor goes into liquidation or bankruptcy, the creditor (holder) can take a bad debt deduction only if the debt was written off as bad in the same income year, and before the liquidation or bankruptcy took place. This requirement can be unnecessarily onerous for certain creditors (for example, "mum and dad" investors in failed finance companies), as it means they would need up-to-date knowledge of the financial state of the debtor in order to take the bad debt deduction in time. In some situations, creditors are not informed of upcoming liquidations or bankruptcies so they would need to regularly check the companies register or public listings for updates on the financial status of debtors.

The same strict write-off criteria apply to creditors when the debtor company has entered into a composition[4] with them. In these cases, the creditor can take a bad debt deduction only if the debt was written off as bad in the same income year and before the composition took place. Again, the write-off requirement can be unnecessarily onerous for creditors because the timeframe to write off the debt can be short (the period between being informed of the financial difficulties of the debtor and the composition itself).

Creditors who fail to write off the bad debt in time will have a tax obligation in respect of accrual income they have never received, or remission income that was never written off. This result is unfair and leads to unnecessarily high compliance costs.

The proposed changes will allow creditors to take bad debt deductions where the debt has been remitted by law (for example, after the debtor is liquidated/bankrupted), or where a debtor company has entered into a composition with the creditors.

Key features

At present holders of debt can only take bad debt deductions when the debt has been correctly written off as bad. Under the proposed new rules, bad debt deductions will also be allowed if the debt has been remitted by law, or a debtor company has entered into composition with creditors in relation to the debt.

If a bad debt deduction is sought following a remission by law or after a debtor company has entered into composition with creditors, the deduction must be taken in the year that the base price adjustment is performed.

For clarification, the requirement that the debt be "bad" before any deduction can be taken is unchanged.

[4] A composition with creditors is a deed or agreement where the debtor is released from making all remaining payments (for example, when the creditor agrees to accept 70 cents for every dollar owed by the debtor).

BAD DEBT DEDUCTIONS FOR HOLDERS OF DEBT – BASE MAINTENANCE

(Clause 29)

Summary of proposed amendment

This is the second of two bad debt measures in this bill. This change will align the tax rules with the current policy settings for taking bad debt deductions by limiting bad debt deductions that can be taken by holders of debt to the true economic cost.

Application date

The base maintenance changes apply from the date of introduction of the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill. As part of these changes, there will also be a rule that will require taxpayers who have taken excess deductions (that is, deductions exceeding the cost of acquisition and any income returned) to return those amounts as income in the 2014–15 year. The changes are also subject to a "savings" provision for taxpayers who are currently in the tax disputes process in relation to any prior bad debt deduction for the debt.

Background

Under the current rules, a creditor in a financial arrangement who deals in or holds the same or similar financial arrangements can take bad debt deductions for amounts owing even where they have not suffered a cash loss.

The following example illustrates this issue.

> **Example**
>
> In year 1 A lends B $1,000, repayable at the end of year 5. In year 2 C buys the debt off A and only pays $200 to purchase the debt (because B was facing financial difficulties so was considered unlikely to repay the full debt). Assuming the terms of the financial arrangement were not varied, B now owes C $1,000 at the end of year 5. Under the current law if C's business includes dealing in or holding those financial arrangements, C could arguably take a bad debt deduction for the entire $1,000. This deduction could potentially be taken in the same year that C purchases the debt, even though the financial arrangement does not mature until year 5. If A was a holder or dealer of financial arrangements it will have taken a deduction of $800 for the loss on sale of the debt.

While the base price adjustment (a wash-up calculation that is performed when the financial arrangement comes to an end) will square up any excess deductions taken giving an income result where appropriate, the creditor (C in the example) is still able to benefit from a timing advantage (and potentially a permanent advantage).

This timing advantage arises because the bad debt deductions could be taken well before income from the base price adjustment is recognised. This result is not in line with the current policy settings for bad debt deductions, and it means taxpayers can take a deduction for an amount greater than the cash/economic loss incurred. The timing advantage also presents a risk to the integrity of the revenue base.

The proposed changes will align the tax rules with the current policy settings for taking bad debt deductions by limiting bad debt deductions to the true economic cost.

Key features

Both original and subsequent holders of debt who carry on a business of dealing in or holding the same or similar financial arrangements will be limited to taking bad debt deductions up to the true economic loss. This means original holders will be able to take bad debt deductions up to the amount lent, and subsequent holders will be able to take bad debt deductions up to the purchase price.

Deductions for amounts greater than the economic loss will be allowed if the amounts have previously been returned as income.

As an anti-avoidance measure, a holder of debt who deals in or holds the same or similar financial arrangements will only be able to take bad debt deductions for the true money at risk. This means that if the purchase of a debt was funded by a limited recourse arrangement, a bad debt deduction will only be allowed to the extent to which the limited recourse arrangement does not relate to the debt.

In certain circumstances taxpayers who have taken bad debt deductions of more than the economic loss before the date of introduction of the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill, will be required to return the excess deductions as income in the 2014−15 year.

CHARITIES WITH OVERSEAS CHARITABLE PURPOSES

(Clause 105)

Summary of proposed amendment

The bill adds three new charitable organisations to schedule 32 of the Income Tax Act 2007. Donors to the following charities will be eligible for tax benefits on their donations:

- Kailakuri Health Care Project – New Zealand Link
- Marama Global – Education
- Marama Global – Health

Application date

The amendments will apply from 1 April 2014.

Background

Donors to organisations listed in schedule 32 are entitled as individual taxpayers, to a tax credit of 33⅓% of the amount donated, up to the value of their taxable income. Companies and Māori authorities may claim a deduction for donations up to the level of their net income. Charities that apply funds towards purposes mostly outside New Zealand must be listed in schedule 32 of the Income Tax Act 2007 before donors become eligible for these tax benefits.

The three charitable organisations being added to schedule 32 are engaged in the following activities:

- The Kailakuri Health Care Project – New Zealand Link provides low-cost medical services in Bangladesh.
- Marama Global – Education provides school facilities and teaching resources in North Korea and Uganda.
- Marama Global – Health provides basic and emergency obstetric and maternity equipment, supplies and training in Somalia.

FINANCIAL REPORTING

(Clauses 109 to 111)

Summary of proposed amendments

As part of the rewrite of the Financial Reporting Act it is proposed that small and medium-sized companies that are not public issuers of securities, such as bonds or shares, should not have to prepare general purpose financial statements.

However, as part of this rewrite, the Government has agreed that companies should have to continue to prepare financial statements, albeit to a lower special purpose standard. Further, Inland Revenue, as the biggest user in New Zealand of financial reports, should proscribe minimum reporting requirements. This will help ensure consistency in the Department's requests.

Application date

The objective is for the new rules to apply for the tax year commencing 1 April 2014 or equivalent. However, the application date is activated by the effective date of the repeal of the present financial reporting requirements under the Financial Reporting Act.

Key features

Subsection 17(2), which currently requires companies to produce a form of financial statements, is being consequentially repealed.

New sections 21B and 21C will require companies to prepare financial statements, and will allow, by way of Order in Council, for the setting of requirements for:

- who shall prepare financial statements (other than companies who must prepare financial statements); and
- what the minimum requirements are for the financial statements for both companies and any other classes of taxpayers.

An explicit consultation requirement will be imposed before the Orders in Council can be approved.

Consequentially section 22, which deals with the keeping of business and other records is being amended.

While nothing has been finalised, the intention is that the financial statements will be simple and based on double entry and accrual concepts, using where possible tax-related figures. Certain notes are likely to be required, including a statement of accounting policies, disclosure of related-party transactions and where necessary, a book-to-tax reconciliation. All of this detail will be subject to full consultation later this year.

REMEDIAL MATTERS

REMEDIAL CHANGES TO THE TAXATION OF INSURANCE BUSINESS

(Clauses 2(6) and (13), 32, 33, 36, 44 to 54, 87, 100, 101 and 103(44) to (46) and (54))

Summary of proposed amendment

A number of technical remedial changes are proposed to the treatment of general and life insurance business conducted in New Zealand. They clarify various aspects of the taxation rules applicable to general and life insurers.

Application date

Various dates will apply. These are outlined in the section titled "Detailed analysis".

Key features

The changes:

- confirm entitlements under section DR 4 of the Income Tax Act 2007 that life insurers have in respect of claiming a deduction for the life-risk component of life insurance claims tied to reserves that form part of any acquired or transferred insurance business;
- establish, under sections DW 4 and EY 5, a method for calculating an opening balance for life and general insurance reserves when the business is transferred into New Zealand;
- alter the formula in sections EY 17 and EY 21 which allocates income between a life insurer's policyholder and shareholder tax base. (a number of consequential amendments result from the proposed change); and
- clarify the relationship between sections EY 15 and EY 19 when apportioning investment income from savings product policies between a life insurer's policyholder tax base and shareholder tax base.

The remaining amendments are technical or consequential in nature.

Background

The Taxation (International Taxation, Life Insurance, and Remedial Matters) Act 2009 made significant changes to the way the Income Tax Act 2007 applied to the life insurance business in New Zealand. Changes were also made to the rules affecting the deduction of insurance claims for general insurers.

The changes proposed in this bill are part of a programme to ensure that the changes to the taxation of life insurance and general insurance, enacted by the Taxation (International Taxation, Life Insurance, and Remedial Matters) Act 2009, work as intended. The changes therefore largely confirm or clarify existing policy settings.

Detailed analysis

Reserves – impact of the capital limitation on deduction of claims paid on transferred life insurance business (clause 33(2) and (3))

Section DR 4 of the Income Tax Act 2007 is being amended to ensure that expenditure for claims related to life-risk connected with the outstanding claims reserve is deductible. Concerns had been raised that the operation of case law in connection with business transfers could have the effect of preventing life insurers from claiming a deduction in connection with meeting an insurance claim for life-risk for life policies connected with a newly acquired block of life insurance business. The change applies from 1 July 2010 or earlier income years that include 1 July 2010.

Reserves – setting an opening balance for reserves when general and life insurance business is transferred from non-residents to New Zealand insurers (clauses 36 and 44)

Sections DW 4 and EY 5 of the Income Tax Act 2007 are being amended to set out the calculation of an opening balance for reserves for insurance business that is being transferred by a non-resident to a New Zealand-resident insurer. The proposed new rules will require the New Zealand-resident to base the opening value on the closing balance of the non-resident business on the assumption that the non-resident was in fact a New Zealand tax resident. The concern is that insurance business could be transferred from a jurisdiction that does not have a similar commercial or tax regulatory environment and entitlements or taxable income could be over or understated. The change applies from the date of the first financial quarter following the enactment of the bill; this date is most likely to be 1 January 2014.

Profit-participation policies – allocation of income between the policyholder tax base and the shareholder tax base (clauses 46, 49 to 54 and 103(44) to (46) and (54))

The formula in section EY 17 of the Income Tax Act 2007 is being amended by substituting the term "present value (net)" with the term "present value (actuarial net)". The purpose of the change is to ensure that the claim the shareholder base has on future income derived on investment income is correctly valued. A similar change is being made to section EY 21.

The term "present value (actuarial net)" is defined in section YA 1 to be an actuarially determined discount rate based on the expected market returns (actual and assumed), or the face value of the discount period is less than a year. The discount-rate used should be same as the one used by the life insurer for financial reporting purposes.

To accommodate the change, consequential changes are being made:

- The term "present value (gross)" is being replaced with "risk-free (gross)" in section EY 24.
- The term "present value (net)" is being replaced with "risk-free (net)" in sections EY 28, EY 29, EZ 56 and EZ 57.

These changes apply from 1 July 2010 and earlier income years that include 1 July 2010.

Policyholder base income – non participation policies (clause 45)

Section EY 15 is being amended to clarify its relationship with section EY 19. Section EY 15 defines the income that should be allocated to the policyholder base. Section EY 15(2) specifies that policyholder income is limited to the amount provided for in the formula set out in that section. Any excess income becomes shareholder base income under section EY 19. The change applies from 1 July 2010 or income years including 1 July 2010.

Other remedial changes

Clause	Clarification changes	Reason	Application date
32	*Life insurance outside New Zealand* The colon ":" is being replaced with an "and" in section DR 3.	Improve the logic and interaction of the source rule in section EY 48.	From enactment of the bill.
33(1)	*Deduction for reserves* Deductions under section DR 4 are being defined in the context of non-participation policies.	To improve the linkages between the rules for non-participation policies and the deduction rule in section DR 4.	From enactment of the bill.
47, 48	*Incorrect cross-references to reserves* Cross-references in sections EY 19(3) and EY 20(2) are being fixed. Both sections refer to sections EY 23 to EY 29. The reference is being changed to sections EY 23 to EY 27.	Improve the internal consistency of the Income Tax Act 2007.	From enactment of the bill.
87	*Policyholder credit account* Section LR 1 is being repealed.	The operation of section LR 1 is contingent on the effect of a number of memorandum accounts that were repealed when the new life insurance rules took effect. The section no longer has any effect and is being removed.	From the 2014 income year.
100, 101	*Timing of debit entries to the imputation credit account* Sections OB 47 and OP 44 are being amended to clarify the consequences when an imputation	Under current law the debit entry is required at the time of the breach or the end of the tax year 31 March. At worst, the law could require two debit entries for the same breach in	From 1 July 2010 or earlier income years including 1 July 2010.

	credit in the imputation credit account of a life insurer is lost because continuity of shareholding is not maintained. The amendment provides that no debit arises at the end of the year.	continuity.	

REMEDIAL AMENDMENT TO THE TIME BAR FOR AMENDMENT OF INCOME TAX ASSESSMENTS

(Clause 114)

Summary of proposed amendment

The Tax Administration Act 1994 is being amended to clarify that the time bar applies not only to the Commissioner amending an income tax assessment to increase the amount of tax payable, but also to the Commissioner reducing the amount of a net loss.

Application date

The amendment will apply for the 2002–03 and later income years.

Key features

The time bar in section 108 of the Tax Administration Act 1994 which applies to the Commissioner amending an assessment to increase the amount of tax payable, will be amended to ensure it also applies when the Commissioner reduces the amount of a net loss.

Background

Section 108(1) of the Tax Administration Act 1994 prevents the Commissioner amending an income tax assessment to increase the amount assessed if four years have passed since the end of the tax year in which the taxpayer provides their tax return, unless the return was fraudulent, wilfully misleading or failed to mention income of a particular nature or from a particular source.

Before the introduction of the income tax self-assessment regime in the 2002−03 income year, section 92(5) of the Tax Administration Act 1994 clarified that despite the words "so as to increase the amount assessed" in section 108(1), the time bar applied equally to prevent the Commissioner amending an assessment outside the time bar in order to reduce the amount of a net loss under a determination of loss.

Section 92(5) was repealed in its entirety as part of the introduction of the income tax self-assessment regime. A replacement provision was not enacted to confirm that a reduction in the amount of a net loss is to be treated as an increase in the amount assessed for the purposes of the time bar in section 108.

The amendment proposed in the bill corrects this oversight with effect from the application date for the repeal of section 92(5) so that the original policy intention is restored retrospectively.

REWRITE ADVISORY PANEL AMENDMENTS

The following amendments reflect the recommendations of the Rewrite Advisory Panel following its consideration of submissions on the rewritten Income Tax Acts. The Panel monitors the working of the 2007 Income Tax Act and reviews submissions on what may be unintended changes in the law as a result of its having been rewritten. The Panel recommends legislative action, when necessary, to correct any problems.

Application dates

Unless otherwise stated all the amendments will apply retrospectively, with effect from the beginning of the 2008–09 income year.

Minor maintenance items

The following amendments relate to minor maintenance items referred to the Rewrite Advisory Panel as minor maintenance items and retrospectively correct any of the following:

- ambiguities;
- compilation errors;
- cross-references;
- drafting consistency, including readers' aids – for example, the defined terms lists;
- grammar;
- punctuation;
- spelling;
- consequential amendments arising from substantive rewrite amendments; or
- the consistent use of terminology and definitions.

In the table below, amendments to the Income Tax Act 2004 apply from the beginning of the 2005–06 income year.

Application dates

Clause	Section	Act	Amendment
5	CB 36	2007 Act	Terminology corrected
14	CV 2(1)	2007 Act	Correction to cross-reference
31	DP 11	2007 Act	Terminology corrected
62	GB 32(2B)(a)(i)	2007 Act	Terminology corrected
65	HA 4(2)	2007 Act	Correction to cross-reference
68	HM 8	2007 Act	Defined terms list
69	HM 11	2007 Act	Defined terms list
70	HM 12	2007 Act	Defined terms list
71	HM 13	2007 Act	Defined terms list
72	HM 50(5)(a)	2007 Act	Correction to cross-reference
73	HM 55FB(1)(b)	2007 Act	Correction to cross-reference
74	HM 72(1)	2007 Act	Correction of punctuation
99, 103(13), (52)	OB 1, YA 1, ICA company	2007 Act	Clarifying definition of ICA company
102(2)	RD 5	2007 Act	Terminology corrected
103(8), (53)	YA 1, FDP rules	2007 Act	Terminology corrected
103(37), (38)	YA 1 NZIAS references	2007 Act	Terminology corrected
103(39)	YA 1 partnership share	2007 Act	Terminology corrected
104	Schedule 1, Part A, Clause 1	2007 Act	Correction of cross-reference
Schedule 2, amending Act	After subpart LP	2007 Act, 1 June 2009	Repeal redundant heading
Schedule 2, amending Act	After section OP 77	2007 Act	Repeal redundant heading
Schedule 2, amending Act	After section RC 35	2007 Act	Repeal redundant heading
Schedule 2, amending Act	Section RZ 5D	2007 Act	Defined terms list