The GST treatment of immigration and other services

An officials' issues paper

June 2013

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CHAPTER 1

Introduction

1.1 New Zealand's goods and services tax (GST) system is based on the "destination principle". This principle requires supplies of goods and services to be taxed in the jurisdiction where the goods and services are consumed. Almost all countries with a GST or value added tax (VAT) system apply this principle.

1.2 Accordingly, the Goods and Services Tax Act 1985 (GST Act) requires services supplied to non-residents who are outside New Zealand at the time the services are performed to be zero-rated. Zero-rating of services essentially allows suppliers to claim input tax deductions in relation to the services provided and charge GST to the consumer at a rate of zero percent.

1.3 This rule ensures that GST does not form part of the costs to overseas consumers. Further, it ensures that services are not double taxed, once by the jurisdiction in which the services are supplied and taxed a second time by the jurisdiction where the services are consumed.

Problems

1.4 Two problems have been identified with the rule that zero-rates services if they are supplied to non-residents who are off-shore.

- The zero-rating rule requires the supplier to have knowledge of the whereabouts of the non-resident consumer during the period in which the services are supplied. However, this is not always practically possible, as the non-resident may visit New Zealand in the period on a matter that may or may not be related to the provision of services. In this situation the supplier may be unaware of the non-resident's presence in New Zealand and mistakenly zero-rate the service.

- The application of the residence test can result in a determination that services are zero-rated becoming incorrect. This can occur because the residence rule essentially backdates a person's residency status.

Suggested solutions

1.5 We suggest that services to non-residents remain zero-rated even if a non-resident visits New Zealand during the period of service, as long as that visit is not in direct connection with the services performed.

1.6 We also suggest that the retrospective application of the tax residency rules be switched off in relation to the application of the zero-rating rule.

1.7 The paper seeks readers' views on the suggested solutions, any wider implications of the solutions and how they might work in practice.

Draft interpretation statement

1.8 The two problems discussed in this paper were identified from submissions received in response to a draft Inland Revenue interpretation statement, *GST on immigration services* released in April 2012.[1]

1.9 The draft interpretation statement considered whether the supply of immigration services can be zero-rated under section 11A(1)(k) of the GST Act when a non-resident visits New Zealand over the period during which the services are performed.

1.10 Immigration services can include many different types of services. The Immigration Advisers Licensing Act 2007 provides a wide definition of immigration advice as:

> *... using, or purporting to use, knowledge of or experience in immigration to advise, direct, assist, or represent another person in regard to an immigration matter relating to New Zealand, whether directly or indirectly and whether or not for gain or reward.*[2]

1.11 The Act specifically excludes the provision of information that is publicly available, and other non-specific immigration advice (for more information see section 7, Immigration Advisers Licensing Act 2007). The Act requires that individuals who provide immigration advice must be licensed unless explicitly exempt under that Act.[3]

1.12 The scope of the draft interpretation statement was limited to visa application services provided to a non-resident individual. The statement concluded that immigration services may be zero-rated, provided the recipient of the supply is a non-resident and remains outside New Zealand at the time the services are performed. If the recipient comes to New Zealand over the period during which the services are performed, the entire supply of services must be standard-rated, unless it is possible to apportion the supply.

1.13 The issues raised in response to the draft interpretation statement and the solutions suggested in this paper have wider implications. Therefore, the problems and suggested solutions have been framed in general terms and are not specific to the immigration service industry. The following chapters explain the relevant zero-rating rule, the difficulties raised and the suggested solutions in detail.

Next steps

1.14 Submissions will be taken into account when officials report to the

[1] The interpretation statement *GST on immigration services* is available at http://taxpolicy.ird.govt.nz/sites/default/files/2013-ip-gst-treatment-immigration-is.pdf. Note this statement has expired and is cited as a reference only.
[2] Immigration Advisers Licensing Act 2007, section 7.
[3] Immigration Advisers Licensing Act 2007, section 6.

Government on recommended changes. Any resulting legislative changes are likely to be included in the next available tax bill.

How to make a submission

1.15 Submissions should be addressed to:

The GST treatment of immigration and other services
C/- Deputy Commissioner Policy and Strategy
Inland Revenue Department
P O Box 2198
Wellington 6140

1.16 Alternatively, submissions can be made by e-mailing policy.webmaster@ird.govt.nz with "The GST treatment of immigration and other services" in the subject line.

1.17 The closing date for submissions is 5 July 2013.

1.18 Submissions should include a brief summary of major points and recommendations. They should also indicate whether the authors are happy to be contacted by officials to discuss the points raised, if required.

1.19 Submissions may be the subject of a request under the Official Information Act 1982, which may result in their publication. The withholding of particular submissions on the grounds of privacy, or for any other reason will be determined in accordance with that Act. You should make it clear if you consider any part your submission should be withheld under the Official Information Act.

CHAPTER 2

The zero-rating rule

2.1 Section 11A of the GST Act specifically prescribes the various situations when services are zero-rated for GST purposes.

2.2 Section 11A(1)(k) specifies one of these situations. It requires services to be zero-rated if they are supplied to a non-resident who is off-shore. Four requirements must be satisfied before the service can be zero-rated:

- The recipient of the supply must be a non-resident at the time the services are performed.
- The recipient must be outside New Zealand at the time the services are performed.
- The services cannot be supplied in connection with any New Zealand land or moveable property situated in New Zealand.
- The services cannot be an acceptance of an obligation to refrain from carrying on a taxable activity, to the extent that the activity would have occurred within New Zealand.

2.3 The first two requirements are relevant for the analysis of matters discussed in this issues paper.

Exception for non-resident companies or un-incorporated bodies

2.4 Section 11A(3) of the GST Act provides an exception to the requirement that the recipient of the supply must be outside New Zealand at the time the services are performed. The exception applies only to non-resident companies or unincorporated bodies. It does not apply to natural persons (individuals).

2.5 The exception states that the recipient of the supply will be deemed outside New Zealand if the recipient's presence is minor or the presence is not effectively connected with the supply.[4]

When are services performed?

2.6 The zero-rating rule in section 11A(1)(k) of the GST Act requires that the recipient of the supply must be a non-resident who is outside New Zealand "at the time the services are performed". In the case of a supply that occurs over a period of time (such as immigration services) the time the services are performed is interpreted as the period during which the supplier provides the

[4] Section 11A(3) of the GST Act.

services. This can be considered to be the period between the time the services commence and the time the services are completed.[5]

2.7 There are two main policy reasons why the rule looks at the period of supply in determining the status of the recipient and therefore whether services are zero-rated or standard-rated.

2.8 First, the requirement is consistent with the destination principle. As stated previously, the principle requires that goods and services are taxed in the jurisdiction where they are consumed. A practical way of determining whether services are consumed in a particular jurisdiction is to look at the person's resident status and presence during the period the services are supplied. For example, if the recipient is a resident and present in New Zealand during the period of service, that recipient is considered to have consumed that service in New Zealand and the services will, therefore, be standard-rated.

2.9 Secondly, there would be clear avoidance opportunities if the status of the recipient was determined at one particular point of time – that is, at the time of invoicing or payment for services. For example, in order to avoid tax, the recipient could ensure he or she is out of New Zealand at the one point of time when the person's status was determined.

2.10 However, assessing the tax status of the transaction over the period that the service is being performed can be difficult in practice and lead to uncertainty over the price paid (or received) for the service. The effect of the rule is that it requires the supplier to have knowledge of the recipient's physical location and the recipient's residence status during the period of service. This can be particularly difficult if the service is provided over an extended period of time. These issues are discussed in the following chapters.

Apportionment of a supply

2.11 It is also worth noting that, if there is a single supply (no distinction between parts of the supply) there is no ability to apportion the supply between a portion that would be standard-rated, and a portion that would be zero-rated.[6] So if there is a single supply of services to a non-resident who is off-shore, the supply is required to be zero-rated if the recipient enters New Zealand during the period of service.

2.12 The courts have held that there is a general ability to apportion zero-rated parts of a supply under the GST Act where, on the facts, there is a true distinction between parts of a supply. However, this ability to apportion is restricted to circumstances when, as a matter of fact and degree, a sufficient distinction exists between the different parts of the transaction to make it reasonable to separate them.[7]

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[5] Inland Revenue draft interpretation statement *GST on immigration services*, pg 5.
[6] Section 11A(1)(k) of the GST Act contains no apportionment provisions.
[7] *Auckland Institute of Studies Ltd v CIR* (2002) 20 NZTC 17,685 (HC).

2.13 The draft interpretation statement concluded that it is unlikely the visa application services would be able to be apportioned, as generally all of the services are performed as part of one supply (the supply of services to facilitate obtaining a visa).[8] However, following external consultation it was considered that, in particular cases, there might be some scope for apportionment.

2.14 Section 9(3)(a) does, however, allow a supply of services to be treated as successive supplies. The section deems a supply to take place successively where there is an agreement for periodic payments. In this case, it would be necessary to determine the correct GST treatment for each successive supply.[9]

Example 1

Jane, a non-resident who is off-shore, receives immigration services from a New Zealand-based immigration consultant. Jane agrees to monthly payments over the four-month period of service. During the second month of service, Jane travels to New Zealand and receives direct advice from the consultant.

2.15 In example 1 the consultant is able to zero-rate the services supplied during the first, third, and fourth months the services were supplied, as Jane was off-shore during these times. However, the consultant is required to standard-rate the supply during the second month of service, as Jane was present in New Zealand during that time.

[8] Inland Revenue draft interpretation statement *GST on immigration services*, pg 10.
[9] Inland Revenue draft interpretation statement *GST on immigration services*, pg 12.

CHAPTER 3

Determining location

3.1 As we have stated, in order for services to be zero-rated the supplier must have knowledge of the location of the recipient at the time the services are performed. However, this may not always be possible such as in situations where the non-resident visits New Zealand during the relevant period of services on a matter unrelated to the services being provided.

Knowing whether the non-resident consumer is in New Zealand

3.2 This issue concerns the second requirement of section 11A(1)(k) of the GST Act:

> *The recipient must be outside New Zealand at the time services are performed.*

3.3 In certain situations the supplier may not be aware that the recipient is in New Zealand during the time the services are performed. This can often occur when services are performed over an extended period of time.

Example 2

Jim, a non-resident, applies for a visa to work and live in New Zealand. The visa application process takes six months to complete. During this period Jim visits New Zealand to view some property that he would like to purchase. The immigration consultant is unaware of Jim's visit to New Zealand, and therefore, zero-rates the immigration fees charged to Jim.

3.4 In example 2 the immigration consultant is inadvertently in breach of the GST Act as the immigration fees are zero-rated despite Jim's presence in New Zealand at the time the services were performed. This does not appear to be a fair or appropriate outcome as it is not reasonable to expect that the consultant would have knowledge of Jim's presence in New Zealand.

3.5 Although example 2 specifically relates to the immigration industry it is conceivable that this situation may arise for other suppliers that provide services to non-residents, especially when services are provided over a prolonged period of time.

3.6 It is also worth noting that if the consumer was a non-resident company or unincorporated body, the exemption under section 11A(3) could apply, as the presence in New Zealand is not effectively connected to the suppy.

Suggested solution

3.7 Officials suggest that services supplied to non-residents remain zero-rated even if a non-resident visits New Zealand, as long as the non-resident's presence in New Zealand is not in connection with the services performed.

3.8 This approach is aligned with the exemption for non-resident companies and unincorporated bodies under section 11A(3) of the GST Act. However, the requirement, under section 11A(3), that the non-resident consumer has a minor presence in New Zealand should not in our view apply to individuals. An individual who is in New Zealand for a purpose related to the services being provided can be regarded as consuming the service in New Zealand, compared with a representative of a large non-corporate whose presence may not be reflective of the overall presence of the corporate.

3.9 To the extent an alignment with section 11A(3) is proposed, it may be unclear whether the non-residents presence in New Zealand is in "connection" with the service. Therefore, officials suggest that the non-resident's presence in New Zealand would only qualify for the exemption if the presence was not in "direct connection" with the service.

Scenario

One of Jim's visa requirements is that he has a job offer from an accredited employer. Would a visit to New Zealand for a job interview qualify as a visit that is connection with the immigration services performed?

3.10 Officials consider that in the above scenario, and if Jim was acting independently (on his own accord without the involvement of the immigration consultant), Jim's visit would not be considered to be in direct connection with the services being performed. However, if the immigration consultant was involved in the interview process, the visit could be in direct connection with the services performed. Ultimately, whether or not the exemption will apply will be based on the facts of the particular case.

Australian approach

3.11 Similarly to New Zealand's current zero-rating rule, the Australian legislation makes no explicit exemption for a minor presence which is not in connection with the services provided.

3.12 The Australian legislation states that supplies are GST-free if the supply:

> *is made to a recipient who:*
>
> *(a) is not an Australian resident; and*
>
> *(b) is not in Australia when the thing supplied is done;*

> *other than a supply directly connected with goods situated in Australia when the thing supplied is done, or with real property situated in Australia.*[10]

3.13 However, in an Australian tax ruling "not in Australia" is interpreted more broadly:

> … "*not in Australia" should be interpreted in the context of the supply in question. The expression "not in Australia" requires in our view that the non-resident or other recipient is not in Australia in relation to the supply*.[11]

3.14 This suggested approach in this paper is broadly aligned with the Australian approach.

Further considerations

3.15 In addition to the suggested rule, we have considered whether a "reasonably foreseeable" test is required, similar to the test in section 11A(2)(a) of the GST Act. That is, if the tax treatment could be based on whether it was reasonably foreseeable at the time the services were performed that the non-resident was not present in New Zealand, and if present, the presence was not in connection with the services being supplied.

3.16 A "reasonably foreseeable" test could bring greater certainty when determining the tax treatment of supplies. However, officials are aware of the difficulty in applying a subjective test and it is expected that, with the suggestions we are making, in the majority of situations a test of this nature may not be necessary. Submissions on this point would be helpful.

Submission points

3.17 Officials would like to get a better understanding of whether this issue is a problem in practice, particularly outside the immigration service industry. If this is a problem in practice, is the suggested solution appropriate to resolve the problem. Would it be workable in practice, or likely to create unnecessary uncertainty in its application?

[10] *A New Tax System* (Goods and Services Tax) Act 1999, 38-190.
[11] *Goods and Services Tax Ruling 2004/7*, paragraph 184.

CHAPTER 4

Residency and GST

4.1 This chapter deals with the interaction between the Income Tax Act 2007 (ITA) residency rules and section 11A(1)(k) of the GST Act. An issue specifically arises when the ITA residence rules backdate a person's residence status to a time before services are performed, which can result in services being incorrectly zero-rated.

Application of the income tax residency rules

4.2 This issue concerns the first requirement of section 11A(1)(k) of the GST Act:

> *The recipient of the supply must be a non-resident at the time services are performed.*

4.3 For the purposes of section 11A(1)(k), whether or not a natural person is a resident for New Zealand tax purposes depends on one of two tests being satisfied:

- the 183-day test; or
- the permanent place of abode test. [12]

4.4 The satisfaction of either test results in a non-resident becoming a New Zealand tax resident. However, the 183-day test is the relevant test in regard to this issue, and is located in section YD 1(3) of the Income Tax Act 2007. The rule states that a person is a New Zealand tax resident if that person is personally present in New Zealand for more than 183 days in total in a 12-month period. Furthermore, section YD 1(4) states that in these circumstances, a person is treated as being a resident from the first of the 183 days.

4.5 The retrospective application of this rule can mean that although a non-resident may not qualify for New Zealand tax-resident status until after services have been performed, the person's actual residence status is backdated to the first day of their arrival in New Zealand. This could be before the services were performed. This would mean that a previously correctly zero-rated supply would now have to have been standard-rated as the consumer is considered to be resident for tax purposes for the period during which the services were performed.

[12] A "non-resident" is defined in the GST Act as "a person to the extent that the person is not resident in New Zealand". Consequently, the definition relies on the definition of "resident" in the GST Act, which in turn relies on the meaning of "resident" in the Income Tax Act 2007 under sections YD 1 and YD 2.

4.6 This situation is illustrated below:

Example 3:

1 January 2013	David lives in Canada and decides to visit New Zealand for three months (91 days).
1 April 2013	David returns to Canada and decides to migrate to New Zealand. He engages an immigration adviser to obtain a visa. David remains outside New Zealand for the entire time that the services are performed. The immigration service fees are zero-rated as they are provided to a non-resident who is located off- shore.
1 August 2013	David is granted a visa.
1 October 2013	David arrives in New Zealand to live on a permanent basis.
1 January 2014	David has been present in New Zealand for more than 183 days in aggregate in the last 12 months and is deemed to be a resident for tax purposes from 1 January 2013. This now means that the immigration adviser has incorrectly zero-rated their services to David.

4.7 In example 3, the GST treatment of the supply will need to be revisited. This does not appear to be an appropriate outcome given the fact that the service provider is unlikely to be aware upfront of whether or not the non-resident will become a resident after the services have been provided. This leads to unnecessary uncertainty for the supplier.

Suggested solution

4.8 Officials' preferred solution to this problem is that the retrospective application of the tax residence rules be switched off in relation to the application of section 11A(1)(k) of the GST Act. This would mean that the recipient's residence status would still be based on the 183-day rule, but the recipient's status as a New Zealand tax resident would apply on a prospective basis (from day 183 as opposed to day 1).

4.9 If the suggested solution is applied to example 3, for the purposes of section 11(A)(1)(k) of the GST Act, David would be deemed to be a resident from 1 January 2014. Consequently, the immigration consultant would no longer be required to revisit the zero-rated immigration fees.

Submission points

4.10 Officials would like to get a better understanding of whether this issue is a problem in practice, and if so, whether the suggested solution is appropriate to resolve the issue.