Taxation (Annual Rates for 2015–16, Research and Development, and Remedial Matters) Bill

Commentary on the Bill

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OVERVIEW

The Government's Business Growth Agenda emphasises the importance of innovation to help grow New Zealand's economy. Innovation creates new sources of economic growth by delivering new products and generating improvements in the quality and cost of existing products. Encouraging business innovation is one of the seven key initiatives of the Government's Building Innovation workstream, which recognises that research and development is a key element in the innovation process.

High up-front costs associated with undertaking research and development mean that relative to other investment projects, the profit cycle for research and development projects tends to be much more heavily skewed towards early losses. This can pose a particularly significant barrier to undertaking research and development for innovative start-up companies. Larger firms generally have the ability to use those losses earlier, setting them off against existing streams of income.

Current tax provisions delay the ability of loss-making businesses to use their deductions as they are required to carry the losses forward. This provides an important integrity measure in the tax system to mitigate the creation of artificial losses. However, these current tax settings create a cashflow problem for certain companies in an on-going tax loss position.

This cashflow bias is particularly significant for companies undertaking research and development, and this can increase the cost of investing in research and development rather than in other assets.

Problems can be compounded for start-up companies undertaking research and development who are already likely to suffer from broader capital constraints.

Current tax settings can also penalise businesses that engage in research and development that ultimately turns out to be unsuccessful. This is because current tax provisions state that losses, in this case from unsuccessful research and development, can only be used going forward if there is a subsequent profitable business. The current rules therefore make the use of previous tax losses contingent upon successful innovation or future income earning by the same group of investors. The risk of incurring this potential additional sunk cost is likely to discourage investment in marginal research and development projects further.

The proposed changes focus on start-up companies engaging in intensive research and development, and are intended to reduce their exposure to market failures and tax distortions arising from the current tax treatment of losses. The timing that those companies can access their losses will be brought forward, provided they meet certain criteria. This will help to reduce the bias against investment in these firms from current tax settings.

PROPOSALS FOR THE "CASH OUT" OF RESEARCH AND DEVELOPMENT TAX LOSSES

Summary of proposed amendments

The bill proposes to allow loss-making research and development start-up companies to "cash out" their tax losses arising from research and development expenditure.

The measures are intended to be as simple as possible. That intention and the focus on start-ups means that the proposed changes are not aimed at taxpayers with complex or unusual tax arrangements.

Under the proposals, research and development start-up companies will be able to claim up to 28 percent (the current company tax rate) of their tax losses from research and development expenditure in any given year.

The main eligibility requirements are that the company must be a loss-making company resident in New Zealand, with a sufficient proportion of expenditure on research and development.

The amount of losses that can be cashed out will be capped at $500,000 for the 2015–16 year, increasing by $300,000 over the next five years to $2 million. The amount that can be cashed out in any year is the smallest of that cap, the company's net loss for the year, the company's total research and development expenditure for the year, and 1.5 times the company's labour costs for research and development for the year. Because the cash-out is administered through the tax system, it is delivered in the form of a tax credit.

Research and development expenditure as defined for the initiative will be more restricted than expenditure that is subject to the income tax deductibility provisions for research and development. Expenditure on certain activities and some types of expenditure are excluded.

A cashed-out loss can be thought of as an interest-free loan from the Government to be repaid from the taxpayer's future taxable income; it is intended to provide a temporary cash flow timing benefit. When businesses make a return on their research and development, they will be required to repay some or all of the amounts cashed out. New deductions will reinstate corresponding losses that will be available to offset future income. Triggers for the repayment of amounts cashed out include the sale of research and development assets, liquidation or migration of the company, or the sale of the company.

Application date

The amendments will apply to income years beginning on or after 1 April 2015.

Key features

Eligibility
(Clauses 192 and 213)

The proposed eligibility requirements, as set out in new sections MX 1 and MX 2 of the Income Tax Act 2007, are intended to target the initiative to start-up firms engaging in intensive research and development. The initiative is not intended to apply to highly structured research and development companies or those who are not meeting their tax obligations.

The applicant must be a company that is resident in New Zealand for the whole year and not be one treated, under a double tax agreement, as a resident of a foreign country or territory. A company incorporated part-way through the year will be eligible as long as it meets all the requirements for the part of the year that it is in existence.

A company that is owned by the Crown, or a special corporate entity as defined, or one that is publicly listed will not be eligible. The company must have a net loss for the relevant tax year, and meet the wage intensity criteria. It must have research and development expenditure, and intellectual property that results from the research and development must vest, at least partially, in the company. It must also have complied with all tax law obligations.

A company that is part of a group of companies that includes a foreign company or a company that is treated, under a double tax agreement, as a resident of a foreign country will not be eligible.

Similarly, if a company is part of a group of companies, the group must meet the requirement to have a net loss (in aggregate), meet the wage intensity requirement, and have complied with all tax law obligations. These features are important for the integrity of the initiative.

Look-through companies and qualifying companies are excluded.

Wage intensity criteria

In order to target the initiative to research and development start-ups, expenditure on labour is used as a proxy to gauge the intensity of research and development. Evidence indicates that loss-making research and development-intensive businesses, particularly smaller and younger businesses, tend to spend a greater proportion of their wage and salary costs on research and development than other businesses. The wage intensity criteria are set out in new section MX 3 and, to be eligible, the company must have a wage intensity calculation of 0.2 or more.

The intensity calculation is:

$$\frac{\text{total research and development labour expenditure}}{\text{total labour expenditure}}$$

Total research and development labour expenditure is defined as the total of:

- salary or wages paid to employees for carrying out research and development;
- amounts paid to shareholder-employees as income for carrying out research and development; and
- the costs of research and development carried out by a contractor multiplied by 0.66 (the multiplier is intended to reduce profit and non-wage cost components of the contract price).

Research and development labour expenditure does not include labour employed on activities that are excluded from eligibility.

Total labour expenditure is the total of:

- salary or wages paid to employees;
- amounts paid to shareholder-employees as income; and
- the costs of research and development carried out by a contractor multiplied by 0.66 (as in the numerator).

Amount of the cash-out
(Clauses 192 and 213)

Because the cash-out is administered through the tax system, it is delivered in the form of a tax credit. Similarly to other tax credits, the amount will be cashed out only for the relevant year. That means that it will not be possible to cash out a loss in a year subsequent to when the loss arose.

New section MX 4 sets out the amount of tax credit for a year. It is the smallest of:

- \$500,000 multiplied by the corporate tax rate;
- the company's net loss for the year multiplied by the corporate tax rate;
- the company's research and development expenditure for the tax year multiplied by the corporate tax rate; or
- the company's total research and development labour expenditure for the year, multiplied by 1.5 and also multiplied by the corporate tax rate.

It is proposed that the \$500,000 cap on eligible losses will be increased to \$2 million over five years (by increments of \$300,000 per year).

New section MX 5 proposes to extinguish tax losses that are cashed out.

Research and development expenditure
(Clauses 213, 217 and schedule 1)

The definition of "research and development" is similar to that which applies to provisions that govern deductibility of research and development expenditure in the income tax rules. Using the existing definition is simpler for taxpayers already familiar with it for accounting purposes. However, to ensure that the initiative stays targeted, qualifying expenditure is limited.

Expenditure on certain activities will be excluded because they generally take place in a post-development phase, are related to routine work or there is an indeterminate relationship between the activity and economic growth. Many of the activities are likely to take place when the company is less likely to be capital and cashflow-constrained.

Excluded activities
An activity performed outside of New Zealand.
Acquiring or disposing of land, and related activities, except if the land is used exclusively for housing research or development facilities.
Acquiring, disposing of, or transferring intangible property, core technology, intellectual property, or know-how, and related activities (for example: drafting sale and purchase agreements for patents).
Prospecting for, exploring for, or drilling for, minerals, petroleum, natural gas, or geothermal energy.
Research in social sciences, arts, or humanities.
Market research, market testing, market development, or sales promotion, including consumer surveys.
Quality control or routine testing of materials, products, devices, processes, or services.
Making cosmetic or stylistic changes to materials, products, devices, processes, or services.
Routine collection of information.
Commercial, legal, and administrative aspects of patenting, licensing, or other activities.
Activities involved in complying with statutory requirements or standards.
Management studies or efficiency surveys.
Reproduction of a commercial product or process by a physical examination of an existing system or from plans, blueprints, detailed specifications, or publicly available information.
Pre-production activities, such as a demonstration of commercial viability, tooling-up, and trial runs.

Similarly, some items of expenditure are excluded on the basis that their inclusion could create an economic distortion, inequity between taxpayers in a similar position or risk compromising the integrity of the initiative. A notable exclusion is for expenditure that is not deductible.

Excluded expenditure
Expenditure for goods and services to the extent to which they relate to an activity that is an excluded activity (see the table above).
Expenditure on goods and services used to provide a service of research or development to an external contractee, or used to further another person's research or development activities.
Expenditure that corresponds to a payment for which the person has made an election under section CX 47(4) (Government grants to business).
Expenditure for which no deduction is available for the income year.
Expenditure for or under a financial arrangement.
Expenditure for the acquisition or transfer of intangible property, core technology, intellectual property, or know-how.

Reinstatement of losses
(Clauses 99, 117, 192, 194, 195 and 213)

A cashed-out loss can be thought of as an interest-free loan from the Government to be repaid from the taxpayer's future taxable income; it is intended to provide a temporary cashflow timing benefit when the company is in tax loss.

If the company or the shareholders make an untaxed return on their investment before they have repaid the value of the cashed-out loss, this will lead to an outcome that is concessionary to the taxpayer. In addition to the untaxed receipt, they also retain the benefit of the remaining cashed-out losses that have not yet been repaid. This also creates a fiscal risk.

If the company is able to sell intellectual property or if the company is sold, it is highly likely the research and development company will no longer be constrained to the same degree by the market failures and cashflow constraints affecting small research and development-intensive start-up companies. In this situation, the original policy rationale will no longer apply, as the company will have funds available to pay back the value of the cashed-out loss. New section MX 6 sets out the rules required to recover the value of any remaining cashed-out loss to ensure the correct policy outcome.

It is proposed that the cashed out payments should be repaid (and corresponding losses reinstated) when:

- the company makes a return on their investment by disposing of or transferring research and development assets;
- the company migrates;
- if the company is liquidated;
- the company amalgamates with another company; or
- if more than 90 percent of the company has been sold since the company first cashed-out research and development tax losses.

It is proposed that the company will have deductions corresponding to the repayments in order to reinstate the losses. New section DV 26 and new subsection EJ 23(1)(ab) reinstate the loss and should allow the deduction to be carried forward in line with other deductions for expenditure on research and development.

In the case of the sale of research and development assets, the repayment amount (research and development repayment tax) will be capped at the market value of the consideration for the disposal or transfer multiplied by the tax rate. However, if both the sale of research and development assets and one of the other triggers occurs in the same year, all of the cashed out amounts will need to be repaid that year.

In all five cases the repayment amount will be reduced by income tax paid by the company from the time that losses were cashed out. The payment of income tax is a repayment of the cashed-out amount (because the company does not have the use of losses that have been extinguished to set off against that income). No further repayments will be required if the company has already derived sufficient taxable income to repay the balance of the cashed out amounts before one of these events occurs.

Example

R&D Bio is incorporated in May 2015. It cashes out losses of $150,000 and $300,000 for the 2015–16 and 2016–17 income years respectively. It receives tax credits of $42,000 and $84,000. It carries forward other losses of $50,000. In the 2017–18 year the company enters a manufacturing phase selling trading stock to earn net income of $150,000. It has taxable income of $100,000 and pays income tax of $28,000. In the 2018–19 income year it sells know-how for $250,000 and also has taxable income of $80,000. That year R&D Bio has to pay research and development repayment tax of $70,000 ($250,000 * 0.28) as well as income tax of $22,400. In the 2019–20 income year R&D Bio has taxable income of $150,000 and pays income tax of $42,000. Unless R&D Bio cashes out further losses, no further repayments will be required from that time. Repayments and income tax payments made since the 2017–18 income year ($28,000+$70,000+$22,400+$42,000=$162,400) exceed the tax credits paid for the 2015–16 and 2016–17 income years ($42,000+$84,000=$126,000).

Imputation

No credit balance will arise in an imputation credit account of a company that has cashed out a loss until that company has repaid the cashed-out amounts. This is to maintain neutrality with taxpayers who are not able to cash out losses. The rules are set out in new section OB 47B

Example

In the example above, R&D Bio will not have a credit balance in its imputation credit account for either the 2017–18 year, nor for the 2018–19 income year. It will have a credit balance of $36,400 for income tax paid for the 2019–20 income year (income tax of $42,000 - loss cash-out balance of $5,600).

Effect on deductions

It is proposed that a deduction mechanism is used to reinstate the losses. Those deductions will be available to be allocated to a future income year.

Administration
(Clauses 180, 181, 187, 230 and 238)

Companies will need to apply to cash out their tax losses. Applications will need to be made at the same time companies file the corresponding income tax return. The income tax return and the application will need to be in electronic form. Electronic filing will also be required when a company pays research and development repayment tax.

Like other tax credits, cashed out amounts may be offset against tax payable by the company.

The rules governing the administration of the initiative are set out in sections LA 7, LB 4B and MA 1 of the Income Tax Act 2007, and new sections 70C and 97C of the Tax Administration Act 1994.

Consequential amendments
(Clauses 88 and 267)

Consequential amendments are being made in section DF (1BA) of the Income Tax Act 2007 and to the GST Order in Council 1992.

Black hole expenditure

OVERVIEW

These proposed amendments will give effect to changes to the income tax treatment of certain items of "black hole" expenditure that were announced as part of Budget 2014. "Black hole" expenditure is business expenditure that is not immediately deductible for income tax purposes, and also does not form part of the cost of a depreciable asset for income tax purposes which means it cannot be deducted over time as depreciation.

The amendments are primarily targeted at black hole research and development (R&D) expenditure. Under current tax law, taxpayers are allowed immediate income tax deductions for R&D expenditure incurred up until the point that an intangible asset is recognised under the accounting rules. Any further development expenditure incurred generally must be capitalised.

The problem is that development expenditure incurred subsequent to the recognition of an intangible asset for accounting purposes is potentially never able to be deducted for income tax purposes. This may discourage businesses from undertaking R&D that they would have undertaken in the absence of taxation.

The amendments aim to reduce the cases where tax rules may be discouraging investments that would be undertaken in the absence of taxation, by allowing capitalised expenditure to be deducted or depreciated, as appropriate.

On 7 November 2013, a Government discussion document, *Black hole R&D expenditure*, was released, which outlined initial proposals to allow tax deductions for black hole R&D expenditure. The proposals were part of the Government's "encouraging business innovation" initiative under its Business Growth Agenda "Building Innovation" workstream.

Submissions were generally supportive of the intent of the proposals to relieve black hole R&D expenditure. However, many of the submitters wanted the scope of the proposals widened to provide tax deductibility for both successful and unsuccessful capitalised development expenditure towards intangible assets that are not depreciable for tax purposes. In response to these submissions, the scope of the proposals was widened to also provide tax deductibility for these expenditures. Additionally, a number of submitters identified other categories of expenditure that fit within the policy framework in the discussion document (namely, expenditure relating to registered designs and the copyright in an artistic work that has been applied industrially) and the proposals were extended to cover them.

RESEARCH AND DEVELOPMENT EXPENDITURE ON DERECOGNISED NON-DEPRECIABLE ASSETS

(Clause 85)

Summary of proposed amendment

For taxpayers that have developed intangible assets that are not depreciable for tax purposes, an amendment to section DB 34 of the Income Tax Act 2007 will allow a one-off income tax deduction for capitalised development expenditure (incurred on or after 7 November 2013) upon the intangible asset to which it relates being derecognised for accounting purposes.

Application date

The amendment will apply from the beginning of the 2015–16 income year.

Key features

Section DB 34 will allow a taxpayer who has developed an intangible asset (recognised for accounting purposes) that is not depreciable for tax purposes an income tax deduction for capitalised development expenditure they have incurred on the asset. The proposed amendment only applies for expenditure incurred on or after 7 November 2013, the date the discussion document was released.

The deduction will be allowed upon the intangible asset being derecognised (that is, written off) for accounting purposes (other than due to its disposal). The deduction will be allowed irrespective of whether the asset was useful for a period or the R&D was unsuccessful.

The deduction will be allowed in the income year in which the relevant intangible asset is derecognised for accounting purposes.

Background

Taxpayers are currently allowed immediate tax deductions under section DB 34 of the Income Tax Act 2007 for R&D expenditure incurred up until the point that an intangible asset is recognised under the accounting rules. Any further development expenditure incurred must be capitalised. In the event that the R&D project does not create an asset that is depreciable for tax purposes, any development expenditure incurred post-recognition of an intangible asset for accounting purposes is generally non-deductible for tax purposes. This may discourage businesses from undertaking R&D investments that would have been undertaken in the absence of taxation.

It would be inappropriate, from an economic perspective, to allow tax deductibility for expenditure towards creating an asset that would not have been likely to have a finite life if successful. Not allowing a deduction for losses in this situation is the counterpart of not taxing capital gains.

It is recognised, however, that technology tends to move at a relatively fast pace and it is likely that R&D-generated assets will have finite useful lives, even if those lives are not able to be estimated with a reasonable degree of certainty at the time of the asset's creation.

While capitalised expenditure on successful R&D can lead to an asset that is worth more for a period than the amount of capitalised expenditure, resulting in an untaxed gain, not allowing any deduction for capitalised expenditure on an asset that can only have a finite useful life appears harsh.

Allowing a one-off tax deduction for capitalised R&D expenditure that relates to an intangible asset that is non-depreciable for tax purposes upon the intangible asset being derecognised for accounting purposes (other than due to its disposal) appears the most appropriate solution. This would mean that a deduction would be available irrespective of whether the asset was useful for a period or the R&D investment was completely unsuccessful. Restricting deductions to when an asset has been derecognised for accounting purposes restricts deductions to cases when it is clear that the expenditure is of no on-going value.

Expenditure incurred on or after the date of the 7 November 2013 release of the Government discussion document, *Black hole R&D expenditure*, should be eligible for deductibility under the proposed new provision. This was signalled as the Government's preferred option in the discussion document. This was done to ensure that the discussion document's release did not prompt businesses to defer their R&D expenditure in anticipation of new tax rules coming into effect. Allowing additional historical R&D expenditure to be eligible for deductibility would significantly increase the fiscal cost, but provide only limited additional benefit in reducing the bias that those who have incurred sunk costs have towards selling the resulting asset over continuing to hold it.

The proposed change will reduce distortions against investment in R&D caused by the current tax rules.

CLAW-BACK FOR DERECOGNISED NON-DEPRECIABLE ASSETS

(Clause 73)

Summary of proposed amendment

Proposed new section CG 7C of the Income Tax Act 2007 will claw back, as income, deductions that have been taken for capitalised development expenditure on derecognised non-depreciable intangible assets, in the event that the intangible asset is sold or becomes useful again.

Application date

The amendment will apply from the beginning of the 2015–16 income year.

Key features

New section CG 7C is a claw-back provision, which will apply to a taxpayer if:

- they have been allowed a deduction under section DB 34 because proposed new section DB 34(3) applies (that is, a deduction for capitalised development expenditure on a non-depreciable intangible asset that has been derecognised for accounting purposes); and
- the previously derecognised intangible asset:
  - is disposed of for consideration that is not income under another provision of the Income Tax Act 2007; or
  - is used or available for use.

In the case of a disposal for consideration, the amount that will be clawed back as income will be the lesser of the consideration derived for the disposal and the amount of the deduction previously taken.

In the case of the asset being used or becoming available for use, the entire amount of the deduction previously taken will be clawed back as income. For the purposes of the depreciation rules, the taxpayer will be treated as never having had the deduction. Therefore, if the taxpayer eventually acquires an item of depreciable intangible property to which the expenditure relates, they will be able to depreciate the expenditure.

Any income arising under proposed new section CG 7C will arise in the income year in which the previously derecognised intangible asset is disposed of for consideration, or is used or available for use, as the case may be.

Background

There is risk that, after a taxpayer has taken a deduction for capitalised development expenditure on a derecognised non-depreciable intangible asset, the intangible asset may be sold or become useful.

In the case of a sale, the taxpayer has conceptually derived income. Therefore, a claw-back provision is necessary to preserve a neutral tax treatment by ensuring that a taxpayer does not receive a deduction that is larger than the loss they have suffered.

If a taxpayer was able to receive an early deduction for expenditure that has created what turns out to be a useful asset, they would receive a significant advantage. Therefore, a claw-back provision is appropriate, as it would reduce this advantage and ensure greater economic neutrality and consistency with the treatment of expenditure that has created an asset that has always been regarded as successful.

Without a claw-back provision, there would be a risk of taxpayers manipulating the system. A claw-back provision is therefore an important integrity measure.

DEPRECIABLE COSTS OF CERTAIN DEPRECIABLE INTANGIBLE ASSETS

(Clauses 105, 106, 109 and 110)

Summary of proposed amendment

Proposed new section EE 18B of the Income Tax Act 2007 will enable taxpayers who have created an asset that is depreciable for tax purposes to include capitalised expenditure that relates to the asset as part of the depreciable costs of the asset.

Application dates

The amendment allowing capitalised expenditure relating to an existing item of depreciable intangible property (other than a patent, patent application, or plant variety rights) to be included as part of the item's depreciable costs will apply from the beginning of the 2011–12 income year.

The amendment allowing capitalised expenditure relating to a patent, patent application, plant variety rights or the new additions to schedule 14 of the Income Tax Act 2007 proposed in this bill to be included as part of the item's depreciable costs will apply from the beginning of the 2015–16 income year.

Key features

New section EE 18B specifies that the "cost" to a person of an item of depreciable intangible property for depreciation purposes includes expenditure they have incurred on an underlying item of intangible property, if that item gives rise to the item of depreciable intangible property.

In the case of patents, patent applications, plant variety rights, and the new additions to schedule 14 proposed, the person must have incurred the expenditure on or after 7 November 2013, for the expenditure to be included in the depreciable cost of the item of depreciable intangible property.

Consequential amendments are proposed to sections EE 33 and EE 34, which set out how to calculate the annual rate of depreciation for fixed-life intangible property and patents, respectively.

Background

Capitalised expenditure may be rendered non-depreciable, even if a taxpayer is successful in creating an intangible asset that is depreciable for tax purposes (that is, an asset listed in schedule 14 of the Income Tax Act 2007). As explained below, this may occur because, although the expenditure has given rise to an asset that is depreciable for tax purposes, the depreciable costs of the asset have been interpreted to exclude some types of expenditure.

An interpretation statement issued by the Commissioner of Inland Revenue takes the view that the depreciable patent costs (for a taxpayer who has lodged a patent application with a complete specification or had a patent for an invention granted) are limited to the administrative and legal fees incurred in the patent process.[1] According to the Commissioner's view of the law, capitalised development expenditure relating to the invention that is the subject of the patent (or patent application) is potentially neither deductible nor depreciable for tax purposes.

In reaching this view, the Commissioner considered the policy intent as to the meaning of "patent" in the depreciation provisions, and concluded that:[2]

> [T]here is no evidence that the meaning of "patent" was intended to be changed to mean "the patent and the invention" under the current depreciation legislation. Had this been the intention, it would be expected that such change would have been explicitly made. As this is not the case, it is the Commissioner's view that, in the depreciation rules, the patent costs means the costs of acquiring the patent and not expenditure incurred in devising an invention.

Although the Commissioner's interpretation statement is confined to patents, it is likely that the depreciable costs of plant variety rights would be interpreted in the same way, given that they are both types of intellectual property rights obtained by registration following an R&D process.

A similar interpretative issue exists in the case of "the copyright in software", with some doubt having been expressed about whether taxpayers who have developed software for use in their own business are able, under current law, to depreciate all of the capitalised development costs.

However, unlike in the case of patents and plant variety rights, there is a clear statement in a 1993 policy statement indicating that the policy intent was that capitalised expenditure incurred in the development of software by a business for its own use should be depreciable. In outlining the tax treatment of expenditure incurred on in-house software development, the statement says that "when the development is completed capitalised costs will be deductible under the depreciation regime".[3] It is understood that taxpayers who have developed software for use in their own business, based on the 1993 policy statement, have been depreciating all of the capitalised development costs.

Where expenditure is in economic substance related to the creation of an asset with a finite useful life that can be estimated in advance with a reasonable degree of certainty, the appropriate tax treatment is to allow the expenditure to be depreciated over that life.

The policy framework adopted for resolving issues with the depreciability of capitalised expenditure relating to intangible assets that are depreciable for tax purposes is to:

- make the changes apply from the beginning of the 2015–16 income year, with capitalised expenditure incurred on or after the date of the release of the Government discussion document, *Black hole R&D expenditure*, (that is, 7 November 2013) to be eligible for depreciation in the case of patents, patent applications, plant variety rights and the proposed new additions to schedule 14 of the Income Tax Act 2007; and
- make the changes retrospective to the statutory time-bar, for intangible assets, when the policy intent was that the expenditure should be depreciable.

[1] Interpretation statement "Income tax treatment of New Zealand patents", *Tax Information Bulletin* Vol 18, No 7 (August 2006), p 51.
[2] *Ibid*, p 44.
[3] Appendix to *Tax Information Bulletin* Vol 4, No 10 (May 1993).

NEW DEPRECIABLE INTANGIBLE ASSETS

(Clauses 72, 87, 104, 107, 111 to 116, 213(2), (9), (10) and (12), and 216)

Summary of proposed amendment

Proposed amendments to the Income Tax Act 2007 will make depreciable registered designs, applications for the registration of a design, and copyright in an artistic work that has been applied industrially. Several associated amendments are proposed as a consequence.

Application date

These amendments will apply from the beginning of the 2015–16 income year.

Key features

The proposed amendment to schedule 14 of the Income Tax Act 2007 will make the following intangible assets depreciable:

- a design registration;
- a design registration application; and
- copyright in an artistic work that has been applied industrially (as defined in section 75 of the Copyright Act 1994).

Including definitions of "design registration" and "design registration application" in section YA 1 make it clear that a registration of a design in New Zealand under the Designs Act 1953 and a registration of a design in other jurisdictions, under similar laws and associated applications, are eligible for depreciation.

Section EE 16 defines the cost of these new depreciable intangible assets for the purpose of calculating the annual amount of depreciation allowed. Expenditure incurred before 7 November 2013 is ineligible for depreciation. Section EE 19 reiterates this, making it clear that costs incurred before 7 November 2013 for these new depreciable intangible assets cannot be added to the asset's adjusted tax value and depreciated.

New section EE 34B sets out how to calculate the annual rate of depreciation for a design registration.

Section EE 67 provides that the legal life of a design registration or application for depreciation purposes commences from when the application was first lodged. Section EE 67 also provides that the legal life of the copyright in an artistic work to which section 75 of the Copyright Act 1994 applies is the length of time, from when the artistic work was applied industrially, that protection against infringement of that copyright is available under that Act.

Section DB 37 will allow a taxpayer a deduction for capital expenditure they have incurred for the purpose of applying for the grant of a design registration if they did not obtain the design registration because the application was not lodged or was withdrawn, or because the grant was refused. The deduction will be allocated to the income year in which the taxpayer decides not to lodge the application, withdraws the application or is refused the grant of design registration.

Section CG 7B ensures that this existing claw-back provision will claw back, as income, deductions that have been taken for aborted or unsuccessful applications for the grant of design registration, if the taxpayer subsequently sells or uses the abandoned application property.

Other minor consequential amendments proposed to sections EE 44, EE 57, EE 60 and EE 61 ensure that the depreciation rules operate appropriately in relation to the new depreciable intangible assets.

Background

An intangible asset can only be depreciated for income tax purposes if it is listed in schedule 14 of the Income Tax Act 2007. For an item of property to be listed in schedule 14, it must be intangible and have a finite useful life that can be estimated with a reasonable degree of certainty on the date of its creation or acquisition.

A design registered in New Zealand under the Designs Act 1953 has a legal life of 15 years (assuming all rights of renewal are exercised). Designs registered in other jurisdictions are also likely to have finite legal lives. It is therefore appropriate to make registered designs depreciable by adding them to schedule 14.

The 15-year legal life of a registered design generally begins on the date on which the first application is made, rather than the date the registration is granted. Therefore, it is also appropriate to make applications for the registration of a design depreciable, by adding them to schedule 14. This will ensure that depreciation is available during the time that registration is pending.

Section 75 of the Copyright Act 1994 contains a special exception from copyright protection for an artistic work that has been applied industrially. The effect of this exception is that, once an owner of copyright in an artistic work (or a licensee) has applied the artistic work industrially (as defined in the section), within New Zealand or overseas, their copyright protection will only last for a further 16 years (for product designs and casting moulds) or 25 years (for works of craftsmanship). This time limit makes the copyright in an artistic work that has been applied industrially appropriate for inclusion in schedule 14.

These proposed additions to schedule 14 follow feedback from submissions received on the Government discussion document, *Black hole R&D expenditure*, released on 7 November 2013. To ensure consistency with the proposed amendments on the deductibility of capitalised R&D expenditure, only capitalised expenditure on registered designs (and applications) and copyright in an artistic work that has been applied industrially incurred on or after 7 November 2013 will be eligible for depreciation.

As it is proposed to make registered designs depreciable, it is also appropriate to allow an immediate tax deduction for expenditure incurred for the purpose of applying for registration of a design if registration is not obtained. This will parallel the tax treatment of expenditure incurred for the purpose of applying for a patent when a patent is not obtained.

An existing claw-back provision applies to deductions taken for aborted or unsuccessful applications for the grant of a resource consent, a patent or plant variety rights, if the taxpayer subsequently sells or uses the abandoned application property. Applying this provision to deductions taken for aborted or unsuccessful design registration applications is appropriate to ensure consistency with existing policy settings.

Other policy matters

GST AND BODIES CORPORATE

(Clauses 249, 250, 251, 253 and 254)

Summary of proposed amendments

The amendments clarify that services provided by bodies corporate are supplies for consideration for goods and services tax (GST) purposes and give bodies corporate the option to register for GST. Rules to protect the tax base from any adverse consequences of allowing this choice are included in the proposed amendments.

Application dates

The proposed amendments apply from the date of the bill's introduction, with the exception of the definition of body corporate, as well as proposed sections 5(8A) and 51(1B), which have an application date of 1 October 1986 (the date the Goods and Services Tax Act 1985 came into effect).

Key features

Under the proposed rules, section 2 defines a "body corporate" as having the same meaning as under the Unit Titles Act 2010 but excludes a body corporate of a retirement village registered under the Retirement Villages Act 2003. "Common property" is also defined in section 2 and has the same meaning as in the Unit Titles Act 2010.

Proposed section 5(8A) clarifies that levies and other amounts paid by a body corporate's members to the body corporate are treated as being consideration received for services supplied by the body corporate to its members. Despite this, proposed section 51(1B) excludes the value of the body corporate supplies to members, from the body corporate's total value of supplies, when determining whether the body corporate is required to register under section 51(1). This means that if a body corporate only makes supplies to its members, it will not be required to register, even if the value of the levies or other amounts exceeds the $60,000 registration threshold.

However, if a body corporate is required to register because supplies to third parties exceed the registration threshold, or the body corporate decides to voluntarily register, it will be required to return output tax on the full value of both its body corporate and third-party supplies.

Proposed section 51(5B) provides that a body corporate that makes an application to voluntarily register after the introduction of the bill, must be registered with effect from a date after the registration application date.

If a body corporate decides to register, or is required to do so, proposed section 5(8AB) treats any funds held by the corporate at the date of registration as a supply of services for consideration in the course or furtherance of its taxable activity. The supply of services is treated as performed on the day of registration.

Bodies corporate that were registered before the date of introduction, but decided to cancel their registration post-introduction, are only able to deregister from the date they applied to cancel their registration (proposed section 52(8)). A proposed addition to section 10(7A) ensures that any common property held by the body corporate at the time of deregistration is valued at zero. This will mean the body corporate is not required to return output tax on those assets held at the time its registration ceases.

Proposed section 52(9) provides that a body corporate that registers for GST after the date of introduction cannot deregister for a period of four years.

Background

A body corporate is a legal entity created under the Unit Titles Act 2010 when multiple owners have unit title properties in an apartment building or similar complex. The body corporate comprises all of the property owners and provides a way for the owners to act together in relation to their common and shared interests. Bodies corporate are responsible for managing, maintaining, repairing and organising insurance for the building and common property areas, and for making and enforcing the body corporate operational rules.

Bodies corporate are a product of unit owners undertaking joint actions for their mutual benefit. Funds of the body corporate are held in expectation that they will all be spent. This means that from a GST perspective, bodies corporate should be largely GST-neutral.

Currently, most of New Zealand's approximately 13,800 bodies corporate are not registered for GST, and Inland Revenue's historic position was not to allow bodies corporate to register. A High Court decision in *Taupo Ika Nui Body Corporate v CIR* (1997) 18 NZTC 13,147, appeared to support this position by suggesting that many bodies corporate would not be required to register for GST because they did not make supplies to unit owners for consideration.

More recently, Inland Revenue was asked to revisit the question of whether bodies corporate should be able to register for GST. To answer this question, Inland Revenue undertook a legal analysis and came to a different view which was that a body corporate could be considered to make supplies to its owners and therefore carry on a taxable activity. A consequence of this view is that, if a body corporate makes supplies that exceed the $60,000 threshold, it would be required to register for GST.

Given the historic position, the new interpretation could adversely affect thousands of property owners, as it would require a large number of bodies corporate to register for GST.

The proposed amendments clarify that services provided by bodies corporate are supplies for consideration for GST purposes and give bodies corporate the option to be registered. This ensures that bodies corporate that are not currently registered will not have to do so unless they would be required to do so because of the level of their supplies to non-members or third parties. It also gives certainty to bodies corporate already registered for GST as these bodies corporate will be able to remain registered.

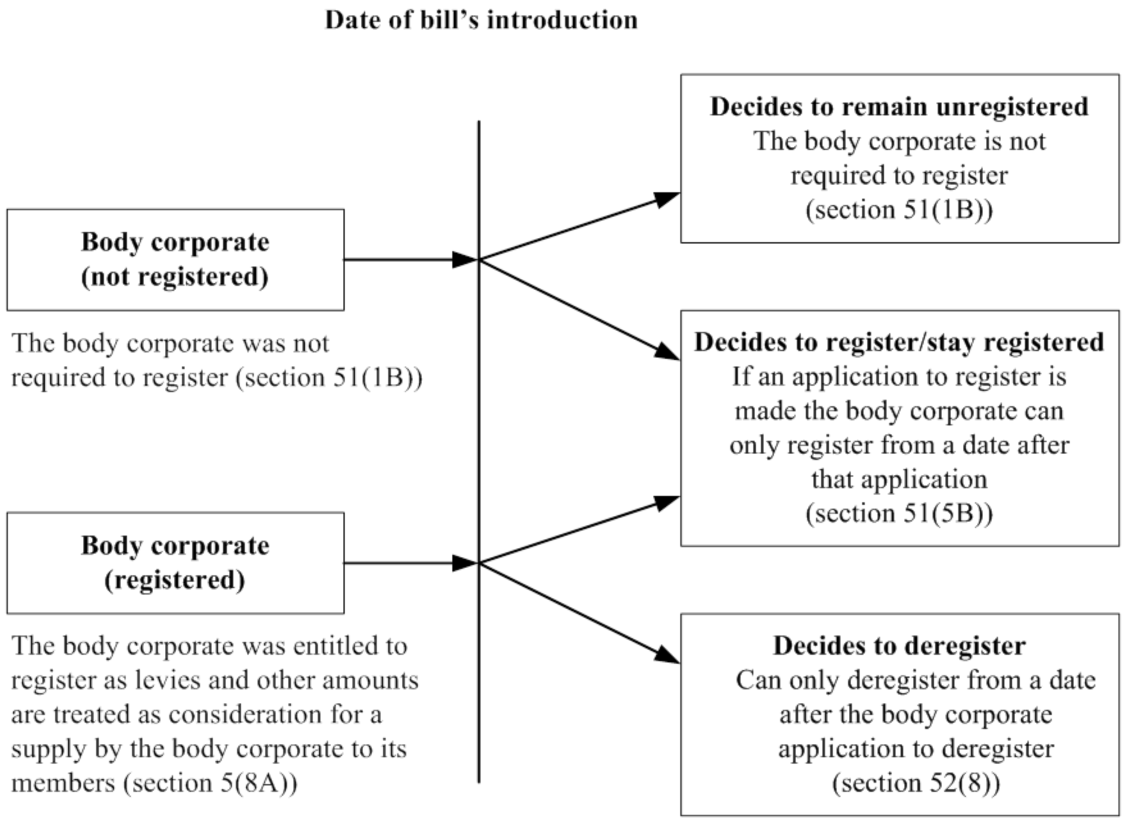
The approach proposed in this bill replaces that set out in the Government discussion document, *GST treatment of bodies corporate,* released on 6 June 2014.

Detailed analysis

Proposed section 5(8A) clarifies that body corporate levies are consideration for a supply by the body corporate to its members. This rule has an application date of 1 October 1986 (the date that GST took effect). This is to ensure that bodies corporate that registered before the date of the bill's introduction have that position confirmed by legislation.

Proposed section 51(1B) excludes the value of supplies to members, from the body corporate's total value of supplies, when determining whether the body corporate is required to register under section 51(1). This should give the majority of bodies corporate the option of registering for GST, unless their supplies to third parties exceed $60,000, in which case they will be required to be registered.

The effect of the proposed rules is summarised in the following diagram:



Retirement villages registered under the Retirement Villages Act 2003 are excluded from the new rules (see new definition of "body corporate"). This is because the nature of supplies that retirement villages provide can be distinguished from supplies made by a typical body corporate. This is recognised by the Unit Titles Act 2010, as significant parts of the Act do not apply to retirement villages.

The bill also proposes rules to protect the tax base from any adverse consequences that could arise as a result of allowing bodies corporate the option to register. This is achieved by imposing an output tax liability on any funds held by the body corporate at the time of registration if a body corporate decides to register after the bill's introduction date (new section 5(8AB)). This prevents a body corporate from obtaining a tax advantage by accumulating untaxed funds while it is not registered and then registering to claim input tax deductions when it spends the funds. The amendment, which will apply on the date of the bill's introduction, ensures bodies corporate remain GST-neutral.

A body corporate's "funds" include all cash and non-cash investments held by the body corporate. The new rule is intended to ensure a body corporate cannot restructure its cash reserves to avoid the application of output tax upon registration. "Funds" will include a body corporate's operating account, long-term maintenance fund, contingency fund and any capital improvement fund (see definition of "fund" under the Unit Titles Act 2010). Any financial investments held by the body corporate are also included (see section 130 of the Unit Titles Act 2010).

Proposed section 51(5B) requires that a body corporate that makes an application to voluntarily register after the introduction of the bill must be registered with effect from a date after the registration application date. This prevents bodies corporate from backdating their registration. Registration backdated prior to the introduction of the bill would have the effect of avoiding the output tax liability imposed under proposed section 5(8AB), discussed above. Conversely, bodies corporate that were registered prior to the date of introduction, but decide to deregister post-introduction, are only able to deregister from the date they applied to cancel their registration (see section 52(8)). This prevents bodies corporate from backdating their registration cancellation to a time that is most advantageous to them.

A body corporate seeking to deregister will not be refunded any GST paid on its funds held at the time of deregistration. This is consistent with the treatment of other registered taxpayers leaving the GST system. There is also likely to be a point on the "save and spend" cycle of a body corporate's activities when its accumulated funds are very low and it can exit the GST base with limited financial impact.

A four-year lock-in rule is proposed to prevent bodies corporate from continually changing their registration status (new section 52(9)). It applies when a body corporate registers after the date of introduction and then later applies to cancel its registration. The cancellation can only take effect on, or after the later of:

- the date on which the body corporate applies to cancel its registration, or
- the day that is four years after the day of registration.

Under the proposed rules, body corporate supplies to third parties still count towards the $60,000 registration threshold. These supplies are treated like any other supply for GST purposes and consequently, if a body corporate's supplies to third parties exceed the $60,000 registration threshold, it will be required to register. This will mean the body corporate will be required to return output tax on any funds on hand at the time of registration. This is considered preferable to treating supplies to third parties as separate from body corporate supplies, with only third-party supplies making up the body corporate's taxable activity. A segregated approach would require the body corporate to apportion its input tax deductions depending upon which supplies they relate to. This could impose significant compliance costs on bodies corporate.

As the exclusion in proposed section 51(1B) only applies for the purposes of section 51(1), once registered a body corporate must return output tax on the value of all the supplies it makes (both body corporate supplies and third-party supplies) in the usual way.

ANNUAL SETTING OF INCOME TAX RATES

(Clause 65)

Summary of proposed amendment

The bill sets the annual income tax rates that will apply for the 2015–16 tax year. The annual rates to be set are the same that applied for the 2014–15 tax year.

Application date

The provision will apply for the 2015–16 tax year.

Key features

The annual income tax rates for the 2015–16 tax year will be set at the rates specified in schedule 1 of the Income Tax Act 2007.

CHILD SUPPORT

(Clauses 3 to 64)

Summary of proposed amendments

The amendments seek to simplify the administration of the Child Support Scheme established by the Child Support Act 1991. There are also changes which seek to ensure that the policy objectives in the Child Support Amendment Act 2013 are achieved by correcting minor errors, clarifying wording and making additional consequential amendments to simplify the Child Support Scheme.

Application date

With some exceptions, the amendments come into force on the day after the date the bill receives Royal assent. However, the following clauses come into force on 1 April 2015:

- clauses 4, 49(1) and (2), and 50(2) to (7) (Interpretation, Application, Transitional and Savings Provisions);
- clause 15 (Living Allowance);
- clauses 23 and 28(2) (Penalties for underestimation of taxable income).

Clauses 31(2), 40(3) and (4), and 41(2) come into force on 1 April 2016.

Clauses 52, 56 and 57 come into force on the date on which the bill receives Royal assent.

Key features

The bill proposes that some of the child support reforms per the Child Support Amendment Act 2013 be repealed or amended. The changes to the reforms focus principally on the options for making payments or the method of recognising special circumstances for assessment purposes, and also focus on reducing debt.

The bill also proposes remedial changes to the Child Support Act 1991 and the Child Support Amendment Act 2013. The following remedial changes are intended to provide a simpler and improved Child Support Scheme, with positive or no impact on families:

- The definition of "social security benefit" (and "beneficiary") will be changed to exclude sole parents who are full-time students and who claim a Jobseeker Support payment on the grounds of student hardship between academic years. For child support purposes, they will be treated in the same manner as full-time students receiving a student allowance (clause 4(3) and (4)).
- Removing the ability in some situations for only one parent to end an assessment, particularly when it is based on estimated income. Removing the ability to unilaterally "opt out" will provide greater certainty about assessments and a reduced number of situations when retrospective assessments and debts occur (clauses 10, 11, 24(3), 28(1) and (47)).

- Changing the requirements regarding notices of assessment and entitlement to cope with unusual situations when the required amount differs from the usual assessment – for example, departures to a formula assessment (clauses 25 and 26);
- Allowing the Commissioner of Inland Revenue to make determinations that differ from what is applied for under the original departure application if the result of the determination is correct and fair, without the need for a cross-application or re-application to be made (clause 31(3));
- Allowing a parent to object to an amended assessment even when their final liability or entitlement has not changed, but a component within it has changed (clause 29(1) and (2));
- Currently, if a receiving carer receives an Unsupported Child Benefit for one child they are unable to end a child support assessment for any other children they care for, even when they are not receiving a benefit in respect of those other children. The ability to end an assessment would be widened to apply with respect to the children for whom the carer is not receiving a benefit, allowing them to set up voluntary arrangements (clause 11).

The proposed remedial changes to clarify the legislation, correct errors or make the Scheme easier to understand include:

- updating references to "welfare benefits" to reflect the new names and eligibility criteria following the welfare reform and ensure the child support living allowance is connected to the correct new benefit (clause 15);
- clarifying who can appeal a decision by the Commissioner to disallow an objection to an assessment (that is, the original objector can appeal rather than any person) (clause 29(3));
- having consistent use of the defined term "annual rate of child support" in the Act (clauses 12 and 36);
- clarifying how the split of the minimum amount of child support works when the liable parent has a formula assessment and voluntary agreement in place (clause 12);
- ensuring the estimation of taxable income sections still work when an overseas parent lives in a country where tax is not payable on income (clause 16);
- clarifying who the parties are in an application to be declared a step-parent (clause 37);
- making clear the time periods and income limits being referred to in the new administrative review ground on income earned to cover re-establishment costs (clauses 40 and 41);
- clarifying who can elect to end a Commissioner-initiated administrative review (clauses 32 to 35);
- clarifying the parties in various appeals such as an appeal to a decision establishing the proportions of shared care (clauses 38 and 39);
- restoring an earlier provision that allows information to be communicated to other agencies by the Commissioner in relation to threats made by the liable parent against the receiving carer. This used to apply to a spousal maintenance relationship but was inadvertently narrowed to just child support assessment relationships (clause 48).

Background

The Child Support Act 1991 sets out the requirements for individuals to apply for, be assessed on, and make and receive child support payments. It contains procedures for changes to assessments, determinations of liabilities, objections and appeal procedures via the Family Court regarding child support assessments. There are also provisions dealing with debt collection, penalties and debt write-offs of child support.

The Child Support Amendment Act 2013 implemented major reform of the Child Support Act to bring in a new, more detailed formula assessment which takes into consideration the costs of raising children and also the incomes of both parents. It also:

- changes the way a liable parent and a receiving carer is determined;
- recognises a greater number of people involved in the care of a child;
- provides greater options for the payment of child support;
- encourages payment of child support obligations; and
- provides greater flexibility for the Commissioner of Inland Revenue to manage child support debt.

The intention of the changes is to improve fairness of the Child Support Scheme by taking into account a wider range of individual circumstances and to reflect changes in family structure and involvement in bringing up children since the Child Support Scheme was first introduced.

The amendments in Part 1 of the Child Support Amendment Act were to come into force on 1 April 2014 and Part 2 of that Act was to come into force on 1 April 2015. Those dates were delayed by one year under provisions contained in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Amendment Act 2014. This was to allow Inland Revenue additional time to implement the changes to the quality standard required.

Remedial changes were also made under the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014.

The bill proposes that some of the child support reforms per the Child Support Amendment Act, the Child Support Act and the Taxation Amendment Acts be repealed or amended. The changes to the reforms do not affect the new framework of how child support is determined and who is responsible for paying child support – they concern the administration of the scheme – principally the options for making payments or the method of recognising special circumstances for assessment purposes.

Under proposals in the bill, the following aspects of the reforms will no longer proceed and be repealed in the Child Support Amendment Act:

- compulsory deductions of child support from employment income, and the associated grounds for an exception such as privacy or cultural reasons (a new provision for voluntary deductions will achieve similar outcomes) (clause 54);
- the new definition of “adjusted taxable income”, which includes income adjustments to taxable income, such as income in trusts and companies (an existing administrative ground can be used instead) (clauses 13, 14 and 17 to 22);

- a penalty for receiving carers who are parents and who underestimate their income for the year (existing provisions can achieve some similar outcomes) (clause 23);
- the ability to offset current payments against past debts where the liable parent and receiving carer swap roles (a new administrative review ground will be used instead) (clause 58);
- the discretion to recognise other payments, such as payment of school fees qualifying as child support payments when they directly benefit the child (as existing provisions can achieve similar outcomes) (clause 54).

CHARITIES WITH OVERSEAS PURPOSES

(Clause 218)

Summary of proposed amendment

The bill proposes adding 10 new charitable organisations to schedule 32 of the Income Tax Act 2007. Donors to the following charities will then be eligible for tax benefits on their donations:

- Adullam Humanitarian Aid Trust
- Bicycles for Humanity, Auckland
- Face Nepal Charitable Trust Board New Zealand
- Hagar Humanitarian Aid Trust
- Himalayan Trust
- International Needs Humanitarian Aid Trust
- Mercy Ships New Zealand
- Orphans Aid International Charitable Trust
- ShelterBox New Zealand Charitable Trust
- So They Can

In addition, Aotearoa Development Cooperative is to be renamed as ADC Incorporated following an organisation restructure by the charity.

Application date

The amendments will apply on 1 April 2015.

The renaming of Aotearoa Development Cooperative to ADC Incorporated will have effect from 20 June 2014. Reference to Aotearoa Development Cooperative will be removed from schedule 32 on and after 1 April 2015.

Background

Donors to organisations listed in schedule 32 are entitled as individual taxpayers, to a tax credit of 33⅓% of the monetary 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 that are mostly outside New Zealand must fulfil a number of requirements and be listed in schedule 32 of the Income Tax Act 2007 before donors become eligible for these tax benefits.

The 10 charitable organisations proposed to be added to schedule 32 in this bill are engaged in the following activities:

- Adullam Humanitarian Aid Trust: Formerly known as Barnabas Aid for Syria, the Trust was established in 2012 to provide aid and relieve the suffering, poverty and distress for communities caught up in natural disasters, civil strife, human rights abuses, war, oppression and violence. The Trust is currently active in Syria and is using a network of Christian churches to deliver aid to dislocated communities affected by the Syrian civil war. Aid is not restricted to church members. All individuals in need are equally eligible to receive aid when they are part of the same community that is suffering the distress which the Trust is seeking to relieve.
- Bicycles for Humanity, Auckland: This Trust is the Auckland chapter of the global Bicycles for Humanity network which provides second-hand bicycles, spare parts, and tools and accessories to impoverished communities in developing countries. Established in 2013, the Trust is working towards making its first shipment of second-hand bicycles to Namibia with the assistance of the Bicycle Empowerment Network. Following this, the trustees will consider a similar shipment to a South Pacific nation.
- Face Nepal Charitable Trust Board New Zealand: Since 2010, Face Nepal's objective is to provide economic and educational resources directed at the alleviation of poverty in Nepal. Its activities largely focus on arranging and co-ordinating volunteer work to support projects identified by the Nepali community.
- Hagar Humanitarian Aid Trust: The Hagar Humanitarian Aid Trust, formerly operating as Hagar New Zealand Charitable Trust was set up in 2009 to assist with the recovery and empowerment of women and children who are victims of human rights abuses, particularly human trafficking, sexual exploitation and gender-based violence. The Trust is active in supporting missions in Afghanistan, Cambodia, Viet Nam and Myanmar.
- Himalayan Trust: Established in 2008, the objective of the Trust is to provide medical and public health facilities and supplies, assistance in or towards quality education and improved facilities for Himalayan people. The Trust's work focuses on education, health and environmental protection. In various guises, the Trust has been operating since 1966 and was previously known as The Himalayan Trust Board (1974) and before that The Sherpa Trust Board (1966).
- International Needs Humanitarian Aid Trust: The Trust works in support of poor communities in over 33 countries in the developing world, including Pacific Island nations. It specifically funds projects directed at community development, vocational education, micro-credit, child-focused programmes and disaster relief. The Trust was formed in 2008 as an associated Trust to International Needs New Zealand (INNZ), which has been operating since 1972, specifically to be the operating arm of INNZ to carry out humanitarian work as described.
- Mercy Ships New Zealand: Through the use of hospital ships, Mercy Ships is involved in the provision of medical services and surgery in West Africa. It also provides medical training to build technical medical capacity in the host country. Mercy Ships New Zealand was set up in 2003 to support the work of Mercy Ships International which was founded in 1978.

- Orphans Aid International Charitable Trust: Established in 2004, the Trust was set up to provide social, medical and housing assistance to Romania's orphans. It also now actively supports projects in India directed at relieving child poverty, including education, and providing opportunities for women to develop work skills and run microbusinesses. They have recently become active in Uganda in projects aimed at preventing child abandonment and poverty.
- ShelterBox New Zealand Charitable Trust: The Trust was set up in New Zealand in 2013 and is part of a global network of 18 affiliates directed at providing those stricken by disaster with a relief package for basic shelter and on-going self-sufficiency. Most recently, the New Zealand Trust was involved in funding shelter boxes and delivery of relief in the Philippines following the devastating typhoon of October 2013.
- So They Can: The organisation is predominantly active in Kenya, and supports a number of projects directed at relieving child poverty and providing opportunities for women to develop work skills and run their own businesses. Funds are raised through a child sponsorship programme, grants from corporate and private foundations, and fundraising events. The Trust formerly operated under the name Breathe Foundation (2010).

Aotearoa Development Cooperative was added to the list of donee organisations in schedule 32 on 1 April 2013. It works with poor communities in Burma. In 2014 the charity restructured and became an incorporated society from 20 June 2014. The proposed change preserves the charity's donee status for the 2014 and later income years.

CALCULATION OF FRINGE BENEFITS FROM EMPLOYMENT-RELATED LOANS

(Clause 203)

Summary of proposed amendment

The amendment will allow employers who are part of the same group of companies as a person in the business of lending money to the public, the option of using the market interest rate method to calculate the fringe benefit arising from an employment-related loan.

Application date

The amendment will come into force on the date of enactment.

Key features

Currently only persons who are in the business of lending money to the public can use the market interest rate method to determine the fringe benefit arising from an employment-related loan. That method requires the employer to assess what the market interest rate would be on a comparable loan to an unrelated third-party borrower.

The proposed amendment will allow an employer who is a member of the same group of companies as a person who is in the business of lending money to the public, to use this method of valuing an employment-related loan.

The proposed amendment includes transitional rules to waive the normal change of method notification period so that an affected employer can apply the market interest rate method soon after enactment. If the election notice is provided before 1 April 2016, the market interest rate method can be applied from the quarter following notification. For a part-year period, the employer may treat this period as a whole income year for the purposes of satisfying the requirement that the method is applied for at least two income years. To qualify the employer must be paying fringe benefit tax (FBT) on a quarterly basis.

Background

When a person receives a loan from their employer at less than market interest, a fringe benefit arises, as the employee benefits from the reduced interest expense. This fringe benefit is subject to FBT.

To limit compliance costs, most employers must calculate the fringe benefit arising from the loan by comparing the interest accruing under the loan with the interest that would accrue if the loan was at the prescribed interest rate, which is set by regulation. The prescribed rate is set with reference to the Reserve Bank's survey of published floating first mortgage interest rates.

Since 2006, an employer in the business of lending money to the public has had the additional option of valuing the fringe benefit by comparing the rate of interest under the loan with the rate of interest that they charge on a comparable loan made to an unrelated borrower.

This additional option was provided because persons who lend money to the public were expected to have systems in place to easily monitor movements in market rates of interest, and could therefore apply the market interest rate method without difficulty.

The option for valuing the fringe benefit was not extended to other employers, as the compliance costs associated with the option would not make it worthwhile.

An issue has since emerged where employers whose employees receive discounted loans under an arrangement with a lender within the same group of companies cannot apply the market interest rate method to value the benefit when the employer itself is not lending to the public. These employers are required to value the benefit using the prescribed interest rate, which may lead to their having a slightly higher FBT liability because it does not factor in market discounts that may be available.

As it is anticipated that the employer will be able to obtain information on market interest rates from the lender, these employers too should be able to apply the market interest rate method without difficulty. Accordingly, the proposed amendment to give these employers the option of applying the market interest rate method should not have any compliance cost implications.

CFC remedials

FAIR DIVIDEND RATE METHODS

(Clauses 137, 138 and 139)

Summary of proposed amendment

The bill proposes changes so that taxpayers can change between fair dividend rate (FDR) methods in calculating income from offshore investments no more than once every four years for each foreign investment fund (FIF) interest.

Application date

The amendment will apply from the 1 April 2016 tax year.

Key features

Proposed section EX 51B of the Income Tax Act 2007 sets out when a person, other than a unit valuing trust, can use the FDR periodic method, and when they must use the FDR annual method. The proposed section allows a change in method no more than once every four years on a per fund basis.

Proposed section EX 53 sets out when a unit valuing trust or other persons who choose to do so can use the FDR periodic method. The proposed section allows a change in method no more than once every four years on a per fund basis.

Background

Under the FDR method of calculating their taxable income from offshore investments, taxpayers are considered to have income from their FIF interests equal to 5 percent of the opening value of each investment. This is referred to as the "usual method" of calculation. Most taxpayers use this method but they also have the option to use a more complex FDR method known as the "unit-valuing funds" method. Taxpayers must use the same FDR method for all of their FIF interests.

This second method was introduced for certain investment funds, for whom the calculation method is mandatory. It was also extended to all taxpayers who were willing to incur the additional compliance costs of basing the FDR calculation on the value of the investment on each day of the year – that is, they must make 365 calculations rather than just one.

The unit-valuing method provides a more accurate result as it takes into account changes in value throughout the year.

If a FIF loses value over the course of a year, the unit-valuing method will calculate a lower amount of income than the usual method because the latter method will base the entire year's income on the (higher) opening value. Conversely, if the FIF gains value over the year, the unit-valuing method will result in more taxable income than the usual method.

As the choice of method is made retrospectively – that is, after the taxpayer has observed if the FIF has gained or lost value, they are able to pick the method which produces the least income. This was not an intended feature of the rules as it was expected that taxpayers would choose one or the other method and use that consistently. The change proposed in this bill is intended to restore the original policy intention.

PREPAID EXPENDITURE

(Clause 126)

Summary of proposed amendment

The bill proposes amending the controlled foreign company (CFC) rules so that they mirror the effect of the prepayment rules in section EA 3 of the Income Tax Act 2007 and prevent taxpayers from claiming an immediate deduction for an amount that should be spread over several years.

Application date

The amendment will apply from the 1 April 2016 tax year.

Key features

Section EX 20C(13)(a)(iii) corrects an anomaly in the rules which allowed immediate deductions for amounts that should be spread over several years. This is achieved through direct reference to the adjustments provided in sections CH 2 and DB 50.

Background

The tax rules allow taxpayers to claim deductions for expenses incurred in generating taxable income. If a taxpayer incurs an expense in one year for something that will last more than one year, adjustments are made so that the deductions are spread over the relevant years. These rules, known as the prepayment rules, are separate from the depreciation rules but serve similar purposes.

Currently, the CFC rules do not include such adjustments and taxpayers can make a full claim in the year payment was made for expenses that may relate to goods or services that will be used over many years. This is an omission.

PART-YEAR EXEMPTIONS FOR AUSTRALIAN FIFS

(Clause 134)

Summary of proposed amendment

The bill proposes to limit the test for the Australian FIF exemption so that it only applies to the period of the year that the taxpayer holds an interest in the FIF.

Application date

The amendment will apply to income years starting on or after 1 July 2011.

Background

Taxpayers with a 10 percent or more interest in a FIF that is resident in Australia generally qualify for the Australian FIF exemption and do not have to declare income from that investment. One of the criteria for the exemption is that the taxpayer must have a 10 percent or more income interest in the FIF at all times in the income year.

Income interests are calculated by averaging out the taxpayer's interests in the FIF across the income year. This means that a taxpayer who has a 40 percent income interest in a FIF for six months of the year and a 20 percent income interest in the FIF for the remaining six months will be considered to have a 30 percent income interest in the FIF for the whole year.

This averaging out is done across the whole income year irrespective of whether the taxpayer had an interest in the FIF at all times or not. Therefore, if a taxpayer acquires a 15 percent holding halfway through a year, their income interest is calculated as a 7.5 percent income interest for the year.

In that scenario the taxpayer would not qualify for the Australia exemption in the year they acquired the interest in the FIF. In the next year they would qualify, if they continued to hold the interest and, if they dispose of the interest halfway through the following year, they would again fail to qualify for the Australian exemption as their FIF income interest would be less than 10 percent.

This is not the correct outcome as the taxpayer has held the same interest in the FIF across the three years, but is not taxed consistently. The proposed amendment is intended to correct this anomaly.

ANTI-AVOIDANCE RULE FOR THE TEST GROUPING CONCESSION

(Clause 165)

Summary of proposed amendment

The bill introduces an anti-avoidance rule to prevent taxpayers from using the test grouping rules, which were introduced as a compliance concession, to gain an unintended tax advantage.

Application date

The amendment will come into force on 1 April 2016.

Key features

Proposed section GB 15BA will provide that the Commissioner may treat an election to include or not to include a particular CFC in a test group as reversed if the person has entered into an arrangement to reduce the amount of net attributable CFC income or increased the amount of net attributable CFC losses.

Background

The CFC rules allow taxpayers to consolidate same-jurisdiction CFCs into a test group when applying the active income exemption test. This means that operational CFCs, who earn active income, can shelter the passive income of holding CFCs. While some criteria have to be met (for example, each CFC must have a taxed CFC connection with the same jurisdiction) the taxpayer otherwise has complete discretion over whether they include a CFC in a test group.

The rules were introduced to allow taxpayers to take full advantage of the active income exemption, irrespective of their business structures.

Because taxpayers have discretion in applying the test group rules it is possible for them to arrange matters so that they pay no tax when they have income but still accumulate losses when they do not.

This means that when there is an operating (active) CFC and a holding (passive) CFC the taxpayer can choose to group the CFCs when the holding CFC has passive income but not when it makes a loss. When grouped, the active income of the operating CFC will grant the group the active income exemption. When not grouped, the loss of the passive CFC will be carried forward to be used against any future attributable income within that jurisdiction. In this way taxpayers may be able to accumulate losses without having to pay tax on their income.

TEST GROUPS FOR GROUPS OF COMPANIES ACQUIRED OR DISPOSED OF DURING THE YEAR

(Clauses 128 and 129)

Summary of proposed amendment

The bill proposes to allow taxpayers who acquire or dispose of groups of foreign companies during the year to access the test grouping concession in that year, for those companies.

Application date

The amendment will apply for income years starting on or after 1 July 2009.

Key features

Proposed sections EX 21D and EX 21E are being amended so that taxpayers using either the default or accounting standard tests can form test groups comprising newly acquired or disposed CFCs.

Background

Taxpayers have the option of grouping multiple CFCs together into a test group and working out the ratio of active to passive income based on the consolidated accounts when applying the active business test. The CFCs must be resident in the same country and the taxpayer must hold an income interest of more than 50 percent in each CFC. The latter rule prevents a single CFC from being used by more than one taxpayer.

This rule produces counter-intuitive results when a taxpayer acquired or disposed of a group of foreign companies part-way through a year.

For example, NZ Co A sells a group of two Australian companies to NZ Co B on 1 October. As neither NZ Co A or NZ Co B will have more than a 50 percent interest in the Australian companies, as the interests are calculated by taking an average holding over the whole income year, they will be unable to access the test group concessions. This may mean that the passive income earned by one of the Australian companies will now have to be attributed back to both New Zealand taxpayers as it will no longer be sheltered by the active income of the other company.

In this scenario the intent of the more than 50 percent interest income requirement is to prevent NZ Co B from grouping the newly acquired companies with the existing CFCs that it already owns. There is no need for the rules to also prevent the two Australian companies from being grouped together by the New Zealand taxpayers for the periods that they hold the interests.

ATTRIBUTION OF INCOME FOR PERSONAL SERVICES

(Clause 166)

Summary of proposed amendment

The bill proposes to allow taxpayers to choose between the standard attribution of personal services rules or the CFC rules if they provide personal services through a foreign company.

Application date

The amendment will come into force on the date of enactment.

Key features

Proposed section GB 27 is being amended to exclude from the exemption from attribution, income from personal services derived through a CFC, if the amount is less than $5,000. This means that a person who derives income from personal services through a CFC has to attribute that income irrespective of the amount.

Proposed section GB 27 is also amended so that the exemption from attribution under section GB 27 only applies in relation to income derived from a CFC if the person has filed a tax return attributing income to the person under the CFC rules.

Background

The attribution rule for income from personal services applies when a taxpayer has interposed an entity (commonly a company) between themselves and the person they are providing services to. For example, Dr Paul could provide medical services to his patients but incorporate a company to be the contractual provider of those services. The company would then employ Dr Paul, who would see the patients and carry out the services. The attribution rule looks through the interposed entity and in certain circumstances attributes the income earned by the company for services provided by the taxpayer, back to the taxpayer.

These rules are duplicated and have the same effect under the CFC rules. Income earned by a taxpayer providing services through a foreign company is considered passive income and is attributed back to the taxpayer.

While the tax effect of the two sets of rules is the same, taxpayers who fall under the CFC personal services attribution rules face a more complex undertaking as they must comply with both the personal services attribution rules and the CFC rules.

This additional compliance burden is not felt by taxpayers who derive both personal services income and other forms of passive income from their CFC interests. These taxpayers would have to comply with the CFC rules regardless of how their personal services income was calculated due to the other passive income. However, taxpayers who only derive personal services income from their CFC interests face additional costs compared with taxpayers who fall under the standard rules. The proposed new rule corrects this.

ATTRIBUTABLE FIF INCOME METHOD FOR INDIRECTLY HELD INVESTMENTS

(Clause 136)

Summary of proposed amendment

This bill proposes to align the tax rules for taxpayers who hold FIF interests indirectly with those applying to taxpayers who directly hold FIF interests. The amendments are intended to ensure that income does not arise from a FIF interest if the taxpayer does not hold an interest in the FIF during that FIF's relevant accounting period.

Application date

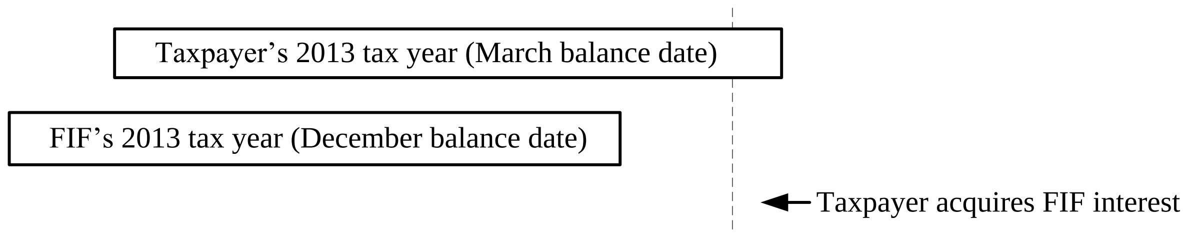
The amendment applies to income years starting on or after 1 July 2011.

Background

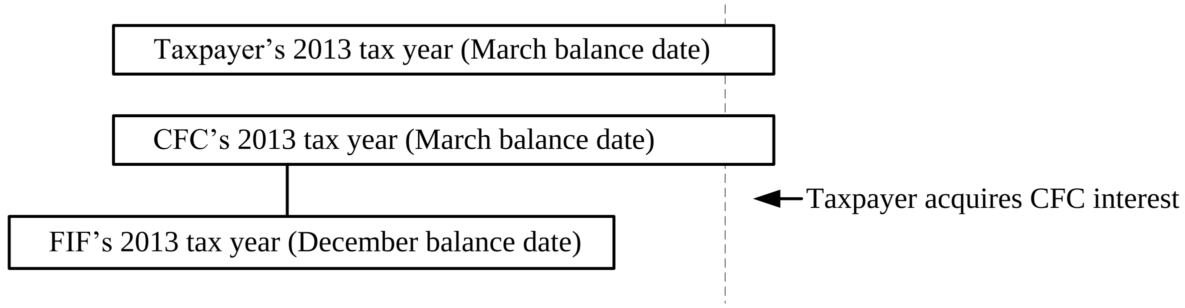
Taxpayers who hold a 10 percent or more interest in a FIF have the option of using the attributable FIF income method to calculate their FIF income. This method provides a more accurate result but at a higher compliance cost and largely mirrors the CFC rules.

Under the attributable FIF income method a taxpayer who acquires an interest in a FIF after the end of that FIF's income year will not have attributable income. For example, a taxpayer with a 31 March balance date acquires an interest in FIF Co on 1 March 2013. FIF Co's balance date is 31 December.

The taxpayer will not have to include any income from FIF Co's 2013 tax year (1 January 2012 to 31 December 2012) as they did not acquire the FIF interest until after the end of that year.



If, instead of directly acquiring the FIF, the taxpayer acquires a CFC that holds the same FIF investment, the treatment is different even if the taxpayer is using the attributable FIF income method for that interest.



In this scenario, the taxpayer is attributed income from the FIF for the 2013 tax year even though they did not hold an interest in the FIF during the FIF’s 2013 income year.

MINOR TECHNICAL REMEDIALS

The following changes are proposed to correct or update terminology used in the CFC rules to make them easier for readers to understand.

Section	**Change proposed**
Section CD 18(3)(a)	Refers to income tax paid “in the country”. Expands to “in the country or territory” in line with changes made to section LJ 3 in the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014.
Section CQ 2(2)	Renames section title “Special rule: Taxable distributions under the attributable FIF income method”. Current title uses out-of-date terminology.
Section CQ 5(3)	Clarifies that income from a FIF held by a non-attributing active CFC can be attributed by inserting “or a non-attributing acting CFC under section EX 21B (Non-attributing active CFCs)” at the end of the subsection.
Section CQ 5(1)(c)(xiv)	Deletes the word “non-resident’s” to match section DN 6(1)(c)((xiv).
Section DN 6(1)(c)(iv)	Replaces the word “regime” with “rules” to match section CQ 5(1)(c)(iv).
Section DN 6(3)	Clarifies that losses from a FIF held by a non-attributing active CFC can be attributed by inserting “or a non-attributing acting CFC under section EX 21B (Non-attributing active CFCs)” at the end of the subsection.
Section EX 58(6)	Clarifies that the section, which applies to CFCs that hold interests in FIFs, applies to both non-attributing active CFCs and non-attributing Australian CFCs by inserting “or a non-attributing active CFC under section EX 21B (Non-attributing active CFCs)” at the end of the subsection.
Section EX 24(3) + (4)	Replaces references to “branch equivalent income or loss” with “CFC attributable income or loss” to reflect current terminology.
Section EX 31(2)(c)(ii)	Clarifies how the rules apply when a taxpayer acquires separate share packages on different days by amending the subsection to read along the lines of “At the earliest date in the income year when the person acquires shares in the company, if the person does not own shares in the company at the beginning of the income year”.
Section EX 44(1)	Clarifies that this provision applies on an interest-by-interest basis rather than to all interests.
Section EX 62(2)(a)	Repeals section containing transitional rules relating to the 2011 FIF rule changes. These rules are no longer needed.
Section EX 62(6)	Removes references to “branch equivalent method” as this method is no longer available.
Section YA 1	Introduces a definition of an “indirect attributing interest” to clarify the changes made to section EX 58 in the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014.

Working for Families

OVERVIEW

Four remedial amendments to the Working for Families (WFF) scheme are proposed. Two amendments correct drafting oversights that occurred when the definition of "family scheme income", used to calculate WFF recipients' entitlements was broadened on 1 April 2011, while the remaining two amendments aim to reduce compliance costs for recipients of the scheme.

MAIN INCOME EQUALISATION SCHEME

(Clause 188)

Summary of proposed amendment

The proposed amendment to section MB 1(5D) will ensure that when a WFF recipient draws on funds deposited by associated entities into their main income equalisation account it does not reduce their WFF tax credit entitlement.

Application date

The amendment will apply from the beginning of the 2011–12 tax year.

Key features

The proposed amendment will extend section MB 1(5D) so that it includes "the person" and all their associated entities listed in section MB 9(b) to (d).

Background

The definition of "family scheme income" was broadened on 1 April 2011 in order to improve the fairness and integrity of the WFF system. As a result section MB 9 was created to ensure deposits made by persons and their associated companies and trusts into the main income equalisation scheme are included as family scheme income. Its inclusion prevents people from making deposits to the scheme to artificially reduce their income and therefore increase their WFF entitlements.

However, section MB 1(5D), which prevents these main income equalisation scheme deposits from being included in a person's family scheme income again when they draw on their funds, only refers to "a person". It does not list the person's associated entities. Therefore, arguably when people draw on income equalisation funds deposited into their account by an associated entity, the funds could be included in their family scheme income a second time. This does not align with the policy intention as it overstates the income available to a person over a set period.

SCHOLARSHIPS AND BURSARIES

(Clause 189)

Summary of proposed amendment

The proposed amendment to section MB 13(2) clarifies that educational bursaries are not included as income for WFF purposes.

Application date

The amendment will apply from the beginning of the 2011–12 tax year.

Key features

The proposed amendment to section MB 13(2)(f) in the Income Tax Act 2007 will extend the list of payments excluded from the definition of "family scheme income" from "an educational scholarship" to " an educational scholarship or educational bursary". This will ensure that bursaries are treated the same as scholarships for WFF purposes so receiving a bursary will not reduce WFF recipient entitlements.

Background

A number of payments that are treated as exempt from income tax are also not intended to affect Inland Revenue social policy entitlements. Two of these payments are scholarships and bursaries for attendance at educational institutions. Although these payments are similar, the current wording of the exemption of scholarships and bursaries from income tax in section CW 36 suggests they are different.

On 1 April 2011, "scholarship" but not "bursary" was added to the list of payments in section MB 13 that are excluded from "family scheme income" which is used to calculate WFF recipient entitlements. It was intended that scholarships and bursaries would be treated as being excluded from family scheme income.

FAMILY ASSISTANCE CREDIT DETAILS NOT NEEDED

(Clause 227)

Summary of proposed amendment

The proposed amendment to section 41(4)(a) of the Tax Administration Act 1994 will remove the requirement for taxpayers to provide Inland Revenue with details of every family assistance credit paid to them as this is unnecessary.

Application date

The amendment will come into force on the date of enactment.

Key features

The proposed amendment repeals section 41(4)(a) of the Tax Administration Act 1994.

Background

Section 41(4)(a) of the Tax Administration Act 1994 requires WFF recipients to furnish details to Inland Revenue of each family assistance credit paid to them in the tax year. However, Inland Revenue does not request or require this information from recipients.

FAMILY SCHEME INCOME STATEMENTS

(Clause 232)

Summary of proposed amendment

The proposed amendment to section 80KV of the Tax Administration Act 1994 will enable WFF recipients and their spouse, civil union partner or de facto partner to submit separate family scheme income declaration forms.

Application date

The amendment will come into force on the date of enactment.

Key features

The proposed amendment will change subsections (1) and (2) and add subsections (3) and (4) of section 80KV in the Tax Administration Act 1994 to ensure people who have been given a notice of entitlement (NOE) from the Commissioner are not always required to provide in their statement of family scheme income for the tax year, the income of their spouse, civil union partner or de facto partner.

Instead, it will also enable the person's spouse, civil union partner or de facto partner to submit a separate family scheme income form to confirm or correct the information contained in the NOE.

Background

Inland Revenue sends out NOEs in order to confirm a person's social policy entitlements and obligations. Section 80KV(2) of the Tax Administration Act 1994 then requires the person to give the Commissioner a statement that confirms or adds to the information in the NOE, including the family scheme income of their spouse, civil union partner or de facto partner. This requirement generally works for most households. However, for some (especially those with child support arrangements), it can be difficult to identify each spouse's portion of family scheme income. In these situations it would be better for each person to submit their income separately.

Other remedial matters

REPEAL OF SIMPLIFYING FILING REQUIREMENTS FOR INDIVIDUALS LEGISLATION

(Clauses 225(4) and (8), 240 and 243)

Summary of proposed amendment

Amendments are being made to the Tax Administration Act 1994 to repeal legislation aimed at simplifying filing requirements for individuals. The legislation was enacted in November 2012 but is not due to take effect until the 2016–17 income year. Implementing the filing simplification legislation is no longer a sound investment given Inland Revenue's Business Transformation (BT) programme as the expected benefits from the earlier simplification legislation will be better delivered as part of the BT programme.

Application date

The amendments will apply from the beginning of the 2016–17 tax year.

Key features

Several amendments are being made to section 33AA of the Tax Administration Act 1994 to ensure that after 1 April 2016:

- Individuals who are not required to file a tax return but choose to do so anyway can continue to file tax returns for each of the four tax years immediately preceding the tax year in which the individual decides to file a tax return. The result will be that individuals will continue to have the ability to choose the years in which they file a tax return.
- Recipients of Working for Families (WFF) tax credits (and their partners) must continue to file a tax return or receive a personal tax summary but only if they receive their WFF entitlements from Inland Revenue.

Consequential amendments are also being made to section 120B, which relates to use-of-money interest, and to section 139B, which relates to late payment penalty of the Tax Administration Act 1994.

Background

Filing simplification for individual taxpayers legislation was enacted in November 2012 as part of the Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill introduced in September 2011 and is due to take effect from the 2016–17 income year. This legislation contained the following two initiatives:

- *4 + 1 square-up*: Individuals who are not required to file a tax return, but who choose to do so anyway, will be required to file tax returns for the previous four years in addition to the year in which they have chosen to file; and

- *WFF delinking:* The link between the receipt of WFF tax credits and the requirement to file an annual income tax return was removed.

The policy underlying that legislation was set three years ago. At that time, the Government was concerned about the inherent tension between individuals who are not required to file a tax return and those who are. Individuals who are required to file a tax return may have a tax debt in one year and receive a refund in another year. For individuals who are not required to file, however, there is no incentive to file a tax return in order to square-up in years of tax debt, but they can easily claim any available refunds. The practice of filing tax returns in those years in which an individual is due a refund is referred to as "cherry picking". This practice has also resulted in a situation where large amounts of revenue are being paid out in refunds, without a reciprocal obligation to pay any tax debt.

The simplified filing legislation addressed concerns of fairness by removing the ability for people to "cherry pick" and removing the requirement for others to file tax returns. These initiatives were seen as a "back-end" solution (that is, stopping people from cherry picking the years in which they file a tax return) to a "front-end" problem of inaccurate PAYE deductions during the year, leading to the need to square-up and file a tax return at the end of the year.

At the time the filing simplification legislation was enacted in 2012, Inland Revenue's Business Transformation programme was in its very early stages. Inland Revenue's current BT thinking is for more streamlined processes with salary and wage earners' information being provided by third parties such as employers and banks to Inland Revenue, and Inland Revenue undertaking the necessary calculations. This should lead to a more accurate PAYE structure, which means fewer people in a refund or tax-debt position at the end of the year. The problem of "cherry picking" would become redundant.

Inland Revenue's review of the implementation of the filing simplification legislation has concluded that the legislation is no longer a sound investment, given Inland Revenue's BT programme. Inland Revenue considers that on current plan the BT programme will deliver the benefits (that is, more accurate PAYE) that are expected from the simplification initiatives from the 2019–20 year, and in a more coherent way that aligns with the vision of a proactive and efficient tax system.

In response to the findings of the Inland Revenue review, the Government agreed to repeal the filing simplification legislation.

EXTENDING THE GRACE-PERIOD OF THE TAX ON NET ASSETS FOR DEREGISTERED CHARITIES

(Clause 264)

Summary of proposed amendment

Section 129(2) of the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 is being amended to defer the application of the new tax on net assets for deregistered charities who provide housing as their main or primary purpose. This deferral is needed to provide more time for officials to finalise the eligibility requirements for the new tax exemption for community housing entities and for Charities Services to complete its review of the charitable status of community housing providers.

Application date

The amendment will apply beginning on 14 April 2014.

Key features

The amendment ensures that new section HR 12 of the Income Tax Act 2007, which imposes a tax on the net assets of deregistered charities, does not apply to entities that provide housing as their main or primary purpose and who have been deregistered by Charities Services before 1 April 2017.

Background

The Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 introduced a new set of tax rules for entities removed from the Charities Register (or deregistered). These rules are now in effect.

One of these rules (new section HR 12 of the Income Tax Act 2007), imposes obligations in relation to accumulated income and assets of a deregistered charity. In the year after the entity is deregistered, it can choose to either:

- distribute or apply the income and assets:
  - for charitable purposes; or
  - in accordance with the entity's rules (as contained in the Charities Register).
- become liable to pay tax on the value of its net assets.

This rule has split application dates. It applied from 14 April 2014 to any entity which requested to be removed from the Charities Register. It is due to apply beginning on 1 April 2015 to any other entity which is removed from the Charities Register.

The split application dates were introduced to deal with the possibility that some community housing providers might be deregistered. Charities Services undertook to review all registered charities which provided housing as their main or primary purpose following the Queenstown Lakes Community Housing Trust High Court decision. The grace-period for the net assets tax was set at 1 April 2015 to allow time for entities to be deregistered without being affected by the new obligations in relation to accumulated income and assets. It was also expected that by 1 April 2015 it would be clear how these deregistered charities were to be treated for tax purposes under the new tax exemption for community housing entities.

However, delays in finalising the tax exemption for community housing entities have meant it has not been possible for Charities Services to advance its review. Consequently, the Government has agreed to extend the grace-period for the tax on net assets for deregistered charities who provide housing as their main or primary purpose from 1 April 2015 to 1 April 2017.

MEANING OF "CHARITABLE OR OTHER PUBLIC BENEFIT GIFT"

(Clauses 183(1), (2), (3) and (6))

Summary of proposed amendment

Section LD 3 of the Income Tax Act 2007 is being amended to clarify that for a subscription to be treated as a "charitable or other public benefit gift", it must, in addition to not conferring any rights arising from its membership:

- be an amount of $5 or more; and
- be paid to an entity that is not carried on for the private pecuniary profit of an individual, and whose funds are wholly or mainly applied to charitable, benevolent, philanthropic or cultural purpose within New Zealand; or
- be an organisation listed in schedule 32.

Application date

The amendment will apply from 1 April 2008, when the Income Tax Act 2007 came into force.

Background

Currently, income tax relief is provided to individuals, companies and Māori authorities for gifts of money to a charitable or other public benefit entity ("a charitable or other public benefit gift").

Under section LD 3 of the Income Tax Act 2007, there are two categories of "charitable or other public benefit gift":

- a gift of $5 or more paid to a society, institution, association, organisation, trust or fund (an entity) that is not carried on for the private pecuniary profit of an individual, and whose funds are wholly or mainly applied to charitable, benevolent, philanthropic or cultural purpose within New Zealand, or an organisation listed in schedule 32 of the Income Tax Act 2007 (generally an overseas donee organisation); and
- a subscription paid to an entity, only if the subscription does not confer any rights arising from its membership.

Based on current wording, the legislation does not require a subscription paid to an entity to be:

- an amount of $5 or more; and
- the entity to be one that is not carried on for the private pecuniary profit of an individual wholly or mainly to charitable, benevolent, philanthropic or cultural purpose within New Zealand, or listed in schedule 32.

This is contrary to the original policy intent. The corresponding provision in the Income Tax Act 2004 clearly set out these requirements for subscription paid to be treated as a “charitable or other public benefit gift”.

It would appear that this is a drafting oversight which arose as part of the rewrite of the Income Tax Act 2004.

The implication is that in the absence of the proposed amendment, individuals would be able to claim tax relief for subscriptions paid to a non-charitable or public benefit entity, provided the subscription did not confer any rights arising from membership.

TAX STATUS OF TERTIARY EDUCATION INSTITUTE SUBSIDIARIES

(Clauses 76, 183(4), (5) and (6), and 213(67) and (75))

Summary of proposed amendment

The bill proposes that the income tax exemption for a Tertiary Education Institute (TEI) be widened to include income earned by a business, such as a subsidiary, for the benefit of the TEI.

Application date

The proposed amendment applies beginning on 1 July 2008.

Key features

The amendment extends the scope of section CW 55BA, relating to income derived by a TEI, to include TEI subsidiaries. This would mean that income from a business carried on for the benefit of a TEI is also exempt.

This restores the position that existed for TEI subsidiaries before enactment of section CW 55BA in the Income Tax Act 2007 which explicitly provided TEIs with an income tax exemption.

Background

TEIs and subsidiaries that applied their income for the purposes of the TEI were generally income tax-exempt as charities until 1 July 2008, when a requirement was introduced for charities to be registered with the Charities Commission[4] in order to be tax-exempt. Because the TEIs would have been subject to multiple reporting and monitoring requirements, a specific exemption was enacted for them, but this did not cover their subsidiaries.

The amendment will restore the position that existed for TEI subsidiaries before the Charities Commission registration requirement. This means subsidiaries that were tax-exempt before 1 July 2008 will retain this position.

[4] Now Charities Services – Department of Internal Affairs.

DEFINITION OF "REMUNERATION" IN VALUATION RULE FOR ACCOMMODATION PROVIDED TO MINISTERS BY RELIGIOUS ORGANISATIONS

(Clause 70)

Summary of proposed amendment

The proposed amendment clarifies the valuation rule for accommodation to ministers provided by religious organisations under section CE 1E of the Income Tax Act 2007.

Application date

The amendment will apply beginning on 1 April 2015.

Background

Section CE 1E of the Income Tax Act 2007 (inserted by section 15 of the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014) contains a specific valuation rule for accommodation provided to ministers of religion. The rule provides that the taxable value of the accommodation is 10 percent of the minister's "remuneration". This rule is a codification of a longstanding administrative practice.

Historically, the administrative practice involved valuing the accommodation for taxation purposes at 10 percent of the stipend provided to the minister. In codifying this rule it was agreed that the legislation should cover not only stipends but also equivalent remuneration to reflect changes to the way religious bodies have remunerated their ministers over the years. Some churches, for example, now pay their ministers market-related salaries. Accordingly, the valuation formula in the Income Tax Act uses the term "remuneration". A technical question has arisen over whether the term "remuneration" could be interpreted to include the value of the accommodation being provided to the minister. This outcome is not within the policy intent as it is inconsistent with previous administrative practice.

To avoid doubt, the proposed amendment makes it clear that the value of accommodation is not included in the minister's "remuneration" for the purpose of calculating the taxable value of the accommodation in accordance with section CE 1E.

COMMENCEMENT DATE FOR ACCOMMODATION PROVISIONS APPLYING TO MINISTERS OF RELIGION

(Clause 81)

Summary of proposed amendment

The proposed amendment ensures that the new accommodation provisions introduced in the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 that relate to accommodation provided by religious organisations to their ministers of religion will apply from 1 July 2013, as originally intended.

Application date

The amendment will apply on 1 July 2013 to 31 March 2015.

Background

The accommodation provisions relating to ministers of religion were reorganised in response to submissions made to the Finance and Expenditure Committee. During that reorganisation, the commencement date of the relevant provisions was inadvertently changed from 1 July 2013 to 1 April 2015. To rectify this error, a transitional provision is now proposed, that will cover the intervening period.

The transitional provision essentially replicates the requirements of section CE 1E which applies on 1 April 2015. Section CE 1E sets out the 10 percent of “remuneration” formula for determining the taxable value of accommodation provided to ministers of religion. The only difference in the transitional provision is that its formula does not include the “excess rental” as that adjustment was only intended to come into force on 1 April 2015. The “excess rental” is the difference between the market value of the accommodation provided and the market value of accommodation that is reasonably commensurate with the duties of the minister and the location in which he or she performs those duties.

FOREIGN SUPERANNUATION

(Clauses 71, 75, 96, 133, 145, 213, 256 and 260)

Summary of proposed amendments

A number of remedial changes are proposed to the tax treatment of foreign superannuation interests held by New Zealand residents in the Income Tax Act 2007. They clarify various aspects of the rules applying to foreign superannuation interests and ensure that the new rules operate as intended.

Application date

All but one of the proposed remedial amendments will apply on and from 1 April 2014, which aligns with the start date of the new rules.

The other proposed change relating to the $50,000 foreign investment fund (FIF) minimum threshold when a person has a FIF superannuation interest will apply beginning on 1 April 2015.

Key features

The proposed changes:

- ensure that the foreign superannuation rules (rather than the FIF rules) apply to interests acquired while a person was a New Zealand tax resident under domestic law, but not resident in New Zealand under a double tax agreement (DTA);
- reintroduce the exclusion from the FIF rules for interests in registered Australian superannuation schemes acquired while a person was a New Zealand resident;
- ensure that the schedule method in the foreign superannuation rules applies to lump-sum withdrawals and transfers from a foreign superannuation interest if a taxpayer has less than $50,000 of FIF interests;
- ensure that a person who transfers their interest from one foreign superannuation scheme to another foreign superannuation scheme continues to be subject to the foreign superannuation rules rather than the FIF rules; and
- resolve historic non-compliance with the FIF rules for persons who return pension income in their income tax return.

Background

The tax rules applying to foreign superannuation interests held by New Zealand residents were substantially reformed in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Act 2014.

The previous rules for interests in foreign superannuation schemes were complex and it was not always clear that they produced an appropriate result. In some cases, the interest was subject to the FIF rules and tax was required to be paid on accrual. When the FIF rules did not apply, tax generally needed to be paid under other tax rules when a distribution was received (such as the rules for pensions, or other tax rules such as the rules for distributions from trusts or companies).

From 1 April 2014, under the new rules, interests in most foreign superannuation schemes are taxed only on receipt. Pensions received from a foreign superannuation scheme continue to be taxed in full. For lump-sum withdrawals (and transfers to New Zealand and Australian superannuation schemes), generally a proportion of the amount is taxed depending on how long the person has been resident in New Zealand.

The FIF rules no longer apply to interests in foreign superannuation schemes unless the interest is grandparented or the interest is acquired while the person is a New Zealand tax resident.

A concessionary rule to help individuals meet their historic tax obligations was also introduced as part of the reforms. If a person made a lump-sum withdrawal or transfer between 1 January 2000 and 31 March 2014 and did not comply with their tax obligations at the time, they have the option to pay tax on 15 percent of the withdrawn or transferred amount. Otherwise, they remain liable under the rules that applied to their scheme at the time of withdrawal or transfer (either the FIF rules or other tax rules that may apply to their interest).

The changes proposed in the current bill ensure that the new rules for taxing foreign superannuation interests work as intended. The changes therefore largely confirm or clarify existing policy settings.

Detailed analysis

Interests in foreign superannuation schemes acquired while not resident in New Zealand under a double tax agreement

Under the new rules for taxing interests in foreign superannuation schemes, the FIF rules continue to apply if a person acquires their interest while they are New Zealand-resident. This is to ensure that the FIF rules that apply to foreign portfolio investments held by New Zealand residents are not undermined.

In certain circumstances, a New Zealander who goes overseas to work for several years (for example, on their OE) could still remain a New Zealand tax resident. Currently, a person in this situation with a foreign superannuation interest which was first acquired during this period is deemed to have a FIF superannuation interest and is required to account for tax under the FIF rules.

This result is not appropriate if the person is also tax resident in another country and “tiebreaks” to that other country under a double tax agreement (generally, if the person’s affairs are more closely linked to the other country) at the time that they first acquired the foreign superannuation interest. Amendments are being proposed to the definition of FIF superannuation interest to exclude from the FIF rules interests in foreign superannuation schemes acquired while the person is not resident in New Zealand under a double tax agreement (treaty non-resident). When a foreign superannuation interest is acquired in such circumstances, it is proposed that the interest is taxable on receipt – in particular, using the rules in section CF 3 for foreign superannuation withdrawals and the ordinary rules for pensions. This is provided for in proposed new section CF 3(1)(a).

Under the proposed change, an interest in a foreign superannuation scheme acquired while the scheme holder is treaty non-resident would *not* have an exemption period set out in section CF 3(5) and (6). Instead, the assessable period as set out in section CF 3(8) would begin when the person is treated as New Zealand-resident under all double tax agreements for the first time while owning the interest in the scheme. This is achieved by new section CF 3(8)(ab).

A consequential amendment is also being made to the rules providing for rollover relief in the case of a transfer following death or a relationship split. Where an interest in a foreign superannuation scheme passes to a person's spouse under a relationship agreement following death or relationship split, both the transferor and transferee would need to be resident under all double tax agreements for rollover relief to be provided. This is a consequential amendment to maintain revenue integrity.

The proposed change would apply beginning on 1 April 2014, which is when section CF 3 came into force.

Example

Mary is a New Zealand tax resident but has been working in Germany for the past few years. For the purposes of the Germany-New Zealand double tax agreement, Mary is considered to be a resident of Germany. While working in Germany, she contributes to a German pension scheme. Mary moves back to New Zealand and from 14 October 2014 is considered to be resident in New Zealand for the purposes of the Germany-New Zealand double tax agreement.

Mary does not have a FIF superannuation interest as she was non-resident under the Germany-New Zealand double tax agreement when she acquired the rights in her pension scheme. Under section CF 3, Mary's assessable period for her interest in the German pension scheme begins on 14 October 2014.

Application of the $50,000 FIF threshold to FIF superannuation interests

Under the new rules for taxing interests in foreign superannuation schemes, the FIF rules continue to apply if a person acquires their interest while they are New Zealand-resident. This is to ensure that the FIF rules that apply to foreign portfolio investments held by New Zealand residents are not undermined.

However, there is a minimum threshold under the FIF rules for certain taxpayers who have only relatively small foreign portfolio investments. The minimum threshold is intended to reduce compliance costs for these taxpayers.

Under the FIF rules, a person has no FIF income or loss if the total cost of their interests in FIFs is less than $50,000. This is provided for in sections CQ 5(1)(d)(i) and DN 6(1)(d)(i). When a person falls within the scope of this FIF threshold and they have not opted to pay tax under the FIF rules, tax is paid on receipt of any distributions from their FIFs under other tax rules that may apply to their interest (such as the rules for distributions from trusts or companies).

A problem can therefore arise for an individual who is below this $50,000 FIF threshold and owns a foreign superannuation interest they acquired while they were a New Zealand tax resident, as neither the new rules for foreign superannuation interests nor the FIF rules will apply to them. In this situation, they would need to consider other tax rules that may apply to distributions from their interest, such as the rules for distributions from companies or trusts. That is to say, some of the complication of the previous rules remains. This is not consistent with the intent of the new rules for taxing foreign superannuation interests, which was to provide a relatively simple set of rules for taxpayers to follow.

The proposed change addresses this concern by ensuring that the schedule method in the foreign superannuation rules (rather than other tax rules such as the rules for distributions from companies) applies to lump-sum withdrawals (and transfers to New Zealand or Australian superannuation schemes) made from a foreign superannuation interest that was acquired while a taxpayer was a New Zealand resident, where the taxpayer has less than $50,000 of FIF interests.

It will require those with no FIF income or loss due to the operation of sections CQ 5(1)(d) and DN 6(1)(d) to account for tax on any lump-sum withdrawals and transfers received from their foreign superannuation interest using the schedule method, as set out in section CF 3(10), (11) and (19).

This proposed change introduces the concept of a "low-value FIF superannuation interest" in section CF 3(1)(b) which determines when section CF 3 applies.

Note that proposed new section CF 3(1)(b) refers to sections CQ 5(1)(d) and DN 6(1)(d) in their entirety, which means that the proposed change would only apply if the person has not opted out of the FIF minimum threshold and into the FIF rules through sections CQ 5(1)(d)(ii), (iii), and DN 6(1)(d)(ii) and (iii).

A person with a low-value FIF superannuation interest would not be eligible for an exemption period set out in section CF 3(5) and (6). An amendment to section CF 3(5) provides clarity that this is the case.

The assessable period for a low-value FIF superannuation interest begins when the person first acquired the rights in the scheme. This is achieved by the proposed new wording of section CF 3(8) and new section CF 3(8)(ac).

In addition, they would not be permitted to use the formula method set out in section CF 3(12) – (19) to calculate their taxable income arising from a foreign superannuation withdrawal. New section CF 3(9)(b)(ib) reflects this.

The proposed change applies from 1 April 2015 to ensure that taxpayers who have taken action on the basis of the current legislation are not disadvantaged.

Example

George is a New Zealand tax resident. He travels to the United Kingdom for one year for his OE. While working in the United Kingdom he contributes to a pension scheme. During that time he remains a New Zealand tax resident and does not "tiebreak" to the United Kingdom under the New Zealand-United Kingdom double tax agreement. At face value, George has a FIF superannuation interest. However, George has no other foreign investments and the interest in his pension scheme is worth $5,000. Under sections CQ 5(1)(d) and DN 6(1)(d), George has no FIF income or loss and so is not required to account for tax on his foreign superannuation interest under the FIF rules.

George transfers his pension scheme to a New Zealand superannuation scheme and calculates his tax liability on the transfer using the schedule method as set out in section CF 3.

Previous FIF exemption for Australian regulated superannuation savings: section EX 33

Previously, section EX 33 provided an exemption from the FIF rules for Australian regulated superannuation savings. This was repealed in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Act 2014. Consequential references to section EX 33 in sections CQ 5(1)(c)(iii) and DN 6(1)(c)(iii) were also repealed by that Act.

This was not intended. It is therefore proposed that sections EX 33, CQ 5(1)(c)(iii), and DN 6(1)(c)(iii) be reinstated, effective from the date the of the repeal, 1 April 2014.

There is also a proposed amendment to the definition of "FIF superannuation interest" to ensure that a FIF superannuation interest does not include an Australian superannuation interest referred to in section EX 33.

Example

Natalie is a New Zealand tax resident but works in Australia. She contributes to a regulated superannuation fund while working in Australia. Under section EX 33, Natalie's interest in an Australian regulated superannuation fund is not an attributing interest in a FIF.

Transfers between foreign superannuation schemes

Under the rules in section CF 3, a transfer from one foreign superannuation scheme to another (non-Australian) foreign superannuation scheme is not taxable income. This is achieved through omission in section CF 3(2) which lists the types of foreign superannuation withdrawals that are considered to be income.

Rollover relief is provided until a person receives a foreign superannuation withdrawal that is income, but the assessable period takes into account the number of years the person held the original interest while they were New Zealand-resident.

When a transfer from one foreign superannuation scheme to another occurs, a problem arises because the interest in the new scheme is not adequately carved out of the FIF rules. This is due to a missing reference to section CF 3(21)(b) in the definition of "FIF superannuation interest".

The bill proposes that the definition of "FIF superannuation interest" be amended to include a reference to section CF 3(21)(b). The proposed change would apply from 1 April 2014.

Periodic pensions and historic FIF non-compliance

When the FIF rules ceased to apply from 1 April 2014, any historic non-compliance under the FIF rules is overridden if the person uses the formula or schedule method for lump-sum withdrawals and transfers made on or after 1 April 2014, if the person's assessable period began before 1 April 2014. The rule is provided for in section CF 3(22) to ensure that the person is not double taxed.

However, section CF 3(22) only applies when a person receives foreign superannuation withdrawals. If there is historic FIF non-compliance, but the person does not receive any foreign superannuation withdrawals and only receives a pension, there is no corresponding provision to override the FIF non-compliance.

This problem applies to people who mistakenly included their pension income in their tax return before 1 April 2014 when they should have complied with the FIF rules, as well as those who will start to receive a pension after 1 April 2014.

To resolve this problem, the bill proposes to introduce new section EZ 32G to override non-compliance under the FIF rules in two situations. The first is where the person derived no payments from their foreign superannuation interest before 1 April 2014 and receives only pension payments from 1 April 2014. The second situation is when the person received only pension payments from the foreign superannuation scheme *before* 1 April 2014 and included all of these pension payments in their income tax returns for the appropriate income years by the due date for each of those returns.

Corresponding sections are also being introduced in the Income Tax Act 1994 (proposed new section CC 5) and Income Tax Act 2004 (proposed new section CF 4).

This change is proposed to apply from 1 April 2014 and would apply to pension payments made from 1 January 2000. This would be in line with the override in section CZ 21B available for certain lump-sum withdrawals and transfers.

Example

Eva has an interest in a foreign superannuation scheme, which, before 1 April 2014, was an attributing interest in a FIF. Eva did not realise that she had to return her FIF income or loss in her income tax return every year.

In 2009, Eva started to receive pension payments from her foreign superannuation interest and assumed she should be paying New Zealand tax on her foreign pension, so she included all of these pension payments in her income tax return each year.

From 1 April 2014, Eva's interest in her foreign superannuation scheme does not meet the definition of "a FIF superannuation interest", so her interest is no longer an attributing interest in a FIF. This means that from 1 April 2014, Eva should be including her pension payments in her income tax return.

New sections EZ 32G and CF 4 in the Income Tax Act 2004, and section CC 5 in the Income Tax Act 1994 provide that because Eva included all of pre-1 April 2014 pension payments in her income tax returns (albeit mistakenly), the FIF income and losses that she should have actually returned before 1 April 2014 have been overridden.

Example

Leo has an interest in a foreign superannuation scheme which, before 1 April 2014, was an attributing interest in a FIF. Leo did not realise that he had to return his FIF income or loss in his income tax return every year.

Leo received no distributions from his scheme before 1 April 2014.

From 1 April 2014, Leo's interest is not a FIF superannuation interest and so it is no longer an attributing interest in a FIF.

In January 2015, Leo starts to receive a periodic pension from his foreign superannuation scheme. He is required to include these as income in his income tax returns.

New sections EZ 32G and CF 4 in the Income Tax Act 2004), and section CC 5 in the Income Tax Act 1994 provide that Leo has no FIF income or loss arising from his foreign superannuation interest before 1 April 2014.

TAX POOLING AND INTEREST LIABILITIES

(Clauses 207 to 212)

Summary of proposed amendment

The amendment proposes to enable purchased tax pooling funds to be used to meet outstanding interest liabilities on increased amounts of tax resulting from an amended assessment or the resolution of a tax dispute that is subject to challenge proceedings.

The current rules allow taxpayers to transfer purchased funds from a tax pool to cover the increased tax owed as a result of an amended assessment, or the resolution of a dispute which is subject to challenge proceedings but not any interest that might be due on these amounts. This change addresses this.

Application date

The amendment will apply on and from 3 July 2014, being the date of the Government's announcement of its intent to change the legislation.

Taxpayers who had an amended assessment issued or challenge proceedings resolved before 3 July 2014 will be able to access tax pooling funds to pay the interest outstanding if the 60-day period to access tax pooling funds was current on 3 July 2014.

Key features

Section RP 17(1) currently enables tax pooling funds to be used to meet an obligation to pay provisional tax, terminal tax or an increased amount of tax. The proposed change will enable purchased tax pooling funds to be used to pay interest outstanding on increased amounts of tax resulting from an amended assessment or the resolution of a dispute that is subject to challenge proceedings.

Changes are also proposed to sections RP 17B(2), (5), (6) and (7), RP 17B(10) and RP 19B(5) to insert after the term "increased amount of tax", a reference to "interest payable under Part 7 of the Tax Administration Act 1994 on the increased amount of tax". Amendments are also proposed in these sections to insert after the term "deferrable tax" a reference to "interest payable under Part 7 of the Tax Administration Act on the deferrable tax".

Section RP 19(1B) is being amended to clarify that this section only applies to the payment of provisional tax or terminal tax. This section determines the order in which the provisional tax payment is applied and ensures this is consistent with the specific provisions relating to provisional tax set out (as applicable) in sections 120J to 120V of the Tax Administration Act 1994. For non-income tax revenues, the normal ordering rule in section 120F of the Tax Administration Act 1994 applies.

A transitional provision is proposed to be inserted in section RZ 12. This will enable minor errors to be corrected in the calculation of the amount of interest required to be accessed from a tax pooling intermediary during the period from the date of the Ministerial announcement (3 July 2014) until the legislation is enacted. Taxpayers will have 60 days from the date of the enactment of the legislation to amend the previously requested interest amount.

Background

The tax pooling rules were introduced in 2003 to deal with concerns with the difference between the interest rates charged on underpayments of tax and paid on overpayments of tax. In essence, the tax pooling rules enable tax pooling intermediaries to provide a market for businesses to pool their tax with that of other businesses, so that underpayments can be offset by overpayments within the pool, and the taxpayers receive a more attractive interest rate than would be available through Inland Revenue.

The current rules enable taxpayers to transfer funds from a tax pool to pay increased amounts of tax resulting from either an amended assessment of their tax liability or the resolution of a tax dispute that is subject to challenge proceedings.

The intent of this change was to stop further interest from accruing on these payments once funds were accessed from a tax pool. However, the interaction of two legislative provisions in the Taxation Acts has resulted in interest continuing to be charged, namely:

- in the case of purchased funds that can be accessed from a tax pooling intermediary, these are limited to the amount of tax outstanding, and do not include any interest outstanding; and
- payments of tax are first applied to interest and then any remainder is applied to the tax outstanding.

This results in a shortfall in tax that then attracts interest until further payments are made.

The following example illustrates this situation.

Example

A provisional taxpayer's tax liability for the 2010–11 tax year has been reassessed, resulting in an increased liability of $9,000. For use-of-money interest purposes this amount was due in three equal instalments of $3,000 on 28 August 2010, 15 January 2011 and 7 May 2011. The taxpayer applies to a tax pooling intermediary to purchase backdated funds, but funds are only available on 7 April 2013. The taxpayer is therefore subject to use-of-money interest (of say $1,000) for the period 29 August 2010 to 7 April 2013.

The legislation restricts the amount of purchased funds that can be accessed by a taxpayer from a tax pooling intermediary to the tax of $9,000. However, once this amount is transferred to Inland Revenue to pay the taxpayer's outstanding tax as at 7 April 2013, the legislation requires the amount to be first applied to the payment of interest ($1,000), and the remaining $8,000 is applied to tax. This leaves a shortfall of $1,000 in tax, which would continue to attract interest from 8 April 2013 until the $1,000 tax and all further accrued interest is paid in full.

The proposed amendment will enable the taxpayer in the above example to purchase both the tax of $9,000 and use-of-money interest of $1,000 on 7 April 2013 and thereby fully pay the tax and interest owing as at that date.

MIXED-USE ASSETS

(Clauses 89 to 95)

Summary of proposed amendment

The bill proposes several remedial changes to the mixed-use asset rules in subpart DG of the Income Tax Act 2007.

Application date

The amendments apply for the 2013–14 and later income years for land and improvements, and the 2014–15 and later income years for aircraft and boats.

Key features

The amendments:

- clarify the basis for interest apportionment for close companies that have excessive debt;
- ensure that the share of interest expenditure of a close company related to the capital use of an asset is allowed as a deduction; and
- clarify that the use of a mixed-use asset by an associated-person employee in the course of their employment is not private use.

Background

The mixed-use asset rules were introduced as new subpart DG and related provisions by the Taxation (Livestock Valuation, Assets Expenditure, and Remedial Matters) Act 2013.

The rules generally apply from the 2013–14 income year to prevent excessive deductions for assets that have a significant element of private use, as well as income-earning use, and periods of non-use. An example of such mixed-use is a bach that is used privately and rented out to third parties, but remains empty for most of the year.

Detailed analysis

Interest expenditure of a close company

Under section DG 11(3), if a company's debt is equal to or less than the value of its mixed-use asset, it is assumed that the debt relates solely to the mixed-use asset and all interest is apportioned under the formula in section DG 9(2).

Conversely, under section DG 11(4), if the company's debt is more than the value of the mixed-use asset, the debt is first allocated to the mixed-use asset and then the balance is assumed to relate to other assets held by the company. Only interest expenditure arising from the debt allocated to the mixed-use asset is subject to the apportionment formula in section DG 9(2) (see section DG 11(6)).

The interest expenditure related to the balance of the debt should be deductible under normal principles, which for a company, usually means it is fully deductible under section DB 7.

This policy intention is not clearly achieved by the current rules as there is some ambiguity regarding the treatment of the balance of the debt and associated interest expense.

Accordingly, the remedial amendment clarifies that this balance is dealt with under the general interest deductibility rules for companies.

Interest expenditure of a close company related to capital use of an asset

The primary expenditure apportionment formula is contained in section DG 9(2). This formula was amended by the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 to deal with situations when there is capital use of an asset (such as use of an airplane to travel to assess potential capital acquisitions), as well as income-earning use and private use. The amendment ensured that an appropriate proportion of mixed-use expenditure was denied when it related to capital and private use of an asset, but allowed when it related to income-earning use.

A related amendment is needed in the apportionment rule for interest expenditure incurred by a close company – contained in section DG 11(3).

In contrast to the recent amendments, the rules relating to deductibility of interest will be amended to ensure that a proportionate share of interest expenditure of a close company related to capital use of an asset *is allowed* as a deduction. This is necessary to ensure that, except in relation to private use of the asset, the mixed-use asset interest deduction rule for companies aligns with the general interest deductibility rule for companies. This means all interest for a company is automatically deductible and, unlike other expenditure, there is no denial of deductions when the expenditure relates to a matter of capital.

This will ensure a company that owns a mixed-use asset is no worse-off than a company that does not own a mixed-use asset in relation to deductions for interest that relate to capital matters. The mixed-use asset-owning company will still be denied interest deductions for private use of that asset, which was the purpose of the mixed-use asset reforms.

For example, assume an airplane owned by a close company is:

- used 30 days for income-earning purposes;
- used 30 days for private purposes;
- used 30 days for capital purposes; and
- not in use for 275 days.

There is $1,000 of insurance, $1,000 of hangar fees and $1,000 interest expense that should be apportioned under the mixed-use asset rules.

The **hangar fees** and **insurance** should be apportioned allowing deductions for income-earning days only.

The formula in section DG 9(2) achieves this as follows:

$$\$2{,}000 \text{ expenditure} \times \frac{\text{30 income-earning days}}{\text{(30 income-earning days + 60 counted days)}}$$

$$= \$667$$

In contrast, for a close company the **interest** expense should be apportioned allowing deductions for income earning days *and* capital days.

The formula in section DG 9(2) currently does not achieve this outcome – under the current rules the outcome would be as follows:

$$\$1{,}000 \text{ expenditure} \times \frac{\text{30 income-earning days}}{\text{(30 income-earning days + 60 counted days)}}$$

$$= \$333$$

To address this issue, the proposed new formula in section DG 11 will apportion the interest expense of a close company as follows:

$$\$1{,}000 \text{ expenditure} \times \frac{\text{30 income-earning days } \mathbf{+ 30 \text{ capital-use days}}}{\text{(30 income-earning days + 60 counted days)}}$$

$$= \$667$$

We note that if the airplane was held by an individual or trust (or any entity other than a company), the standard apportionment formula would apply and there would be no deductions for capital-use days.

Use of an asset by an associated person employee

Currently, if an associate of the asset owner (for example, a 25 percent shareholder in the asset-owning company) uses the asset in the course of their employment, this will be deemed to be private use even though it relates to an income-earning use of the asset. Treating this use as private use results in more deductions being denied than was intended. It could also mean that certain assets are subject to the mixed-use asset rules when they should not be (for example, because there is minimal or no true private use).

An example of this is a company ("Asset Co") owning an aircraft that is used in Asset Co's business. Asset Co's two individual shareholders are also employees of Asset Co. When the aircraft is used in the business, this use requires the shareholder-employees to travel on the aircraft to various work destinations.

Even though this use is entirely for business purposes (and for the shareholder-employees, for the purpose of deriving their employment income), the mixed-use asset rules currently treat this as private use. This may lead to the asset being subject to the mixed-use asset rules when it would not have been otherwise. It may also lead to an inappropriately high proportion of expenditure of Asset Co being denied as a deduction.

There is currently an exclusion from the definition of "private use" for assets used solely in the ordinary course of a taxpayer's business (section DG 4(3)); this does not, however, extend to employees.

Accordingly, the bill proposes that the current exclusion be extended to cover all situations when the asset is being used to derive assessable income of the natural person using the asset, including fees earned as a contractor, and employment income.

The bill also makes an associated minor clarifying amendment to the description of the "person" who has private use of an asset in section DG 4(2)(b). Section DG 4(2) currently states that "the person referred to in subsection 1(a) is a natural person who is:

(a) the person who owns, leases, licences, or otherwise has the asset; or

(b) a person associated with ***them***." [emphasis added]

The use of the term "them" in paragraph (b), seems to refer to the person referred to in paragraph (a) that is, a natural person who owns, leases, licences or otherwise has the asset. If the asset is owned, leased, licensed, or otherwise held by a non-natural person (for example, a company) it is arguable that use of that asset by a natural person associated with the non-natural person owner, lessee, licensee or holder of the asset will not be caught by paragraph (b), when it is intended it should be.

The amendment clarifies that use of an asset by a natural person associated with the non-natural person (for example, company or trust) owner of the asset is considered to be private use.

PROPERTY TRANSFER RULES

(Clauses 149 to 152, 213(53), (54) and (62))

Summary of proposed amendments

Subparts FB and FC of the Income Tax Act 2007 specify the tax treatment of property transfers in certain circumstances, including: transfer under a settlement of relationship property, transfer upon death, transfer by a trustee of a trust to a beneficiary, and the making of a gift.

A number of areas have been identified where the rules in subparts FB and FC do not clearly achieve the intended policy and may have unintended consequences. The proposed remedial amendments address these areas; all of these proposed amendments are consistent with the policy intent of the property transfer rules.

Application date

The amendments apply from 1 April 2008, the date that the Income Tax Act 2007 came into force.

Key features

The amendments propose the following changes:

- In the case of distributions of property from a trustee of a trust to a beneficiary of the trust, section FC 2(1) will only apply to deem the transfer to occur at market value if another provision in the Income Tax Act 2007 does not already provide a value for the property.
- Subpart FB will contain a default rule for the treatment of property transfers under a settlement of relationship property when none of the specific provisions in sections FB 2 to FB 21 apply. Currently, there is no clear provision in subpart FB that applies to certain types of property – for example, attributing foreign investment fund (FIF) interests – and accordingly, there is scope for uncertainty about the outcome of certain transfers.
- Other clarifying amendments to remove uncertainty – the headings of sections FB 1 and FC 1 will be changed to reflect their operative nature (the headings are currently those of purpose provisions), the definition of "settlement of relationship property" has been clarified; an incomplete section cross-reference in section FC 4(1)(b) will be corrected and cross-references to relevant sections in subpart FB will be included in applicable sections in subpart FC to assist readers.

Background

The Income Tax Act 2007 intends to accord concessionary treatment to certain types of property transfers, such as a transfer under a settlement of relationship property or a transfer upon death to a close relative or spouse in certain circumstances (see subpart FB and section FC 3). Broadly speaking, this concessionary treatment involves deferring any tax consequences of transfer until the transferee ultimately disposes of the property. This is often referred to as "rollover relief". It generally involves two steps:

- deeming the transferor to have no tax consequences on disposal; and
- deeming the transferee to acquire not only the property, but all the characteristics of the transferor with respect to that property – for example, the date of acquisition, cost at acquisition and intention of acquisition.

This treatment contrasts with the general treatment under subpart FC which crystallises tax consequences on transfer between parties not accorded the concessionary treatment. Section FC 2 achieves this by deeming the transfer to be a disposal by the transferor and acquisition by the transferee at market value. Subpart FC was introduced as a generic set of rules to clarify the income tax treatment of "in kind" or "in specie" distributions and gifts – in particular, but not limited to, upon death.

A number of areas have been identified where the rules in subparts FB and FC do not clearly achieve the policy intent and may have unintended consequences. The proposed remedial amendments described below deal with these problems.

Detailed analysis

Transfer by a trustee of a trust where another provision provides an appropriate transfer value

Under sections FC 1(1)(c) and FC 2(1), a distribution of property from a trustee to a beneficiary of the trust will be deemed to be a disposal and acquisition at market value. In some circumstances this is an inappropriate outcome.

For example, an investor purchases shares for $2,000 and settles those shares on a fixed trust. The shares are distributed to the investor two years later, at which time they are worth $3,000. The cost base of the shares under sections FC 1(1)(c) and FC 2(1) would be $3,000, rather than the $2,000 the investor actually paid for the shares. This means that if the shares are held on revenue account, upon sale of those shares, the investor will be taxable on the difference between the sale price and the higher cost base. So for example, if the shares further increased in value to $4,000 and the investor sold them, they would, under current law, be subject to tax on $1,000 ($4,000 sale proceeds – $3,000 new cost base) but should be subject to tax on $2,000 ($4,000 sale proceeds – $2,000 original cost base).

The reverse is also possible. If the value of the shares falls to $1,000, the shares are distributed (thus setting a $1,000 cost base) and are subsequently sold for $1,250, the investor will derive $250 of assessable income even though they have made a $750 economic loss.

The cost base in these circumstances should be the amount the investor paid for the shares, not the market value of the shares on the date of distribution, as this more correctly reflects the economic cost of acquiring the shares. Further, if the current law was correct, there would be a difference in tax treatment between acquiring shares under a structure that involves the shares being held in trust for a period of time – for example, as part of a security arrangement – and acquiring them directly, but with restrictive covenants attached which restrict dealing in the shares for the same period as under the trust arrangement. These arrangements are economically substitutable, yet currently have different tax treatments, which is undesirable.

Accordingly, the proposed amendment will ensure section FC 1(1)(c) will apply unless the tax treatment is determined under another provision. In the example above, the cost of revenue account property provision (section DB 23) would provide an appropriate cost base for the shares. This is consistent with the intent of subpart FC, which was to provide a cost base for certain transfers when there was no clear cost base provided by the Act.

Clarifying the treatment of certain types of property not covered specifically by sections FB 2 – FB 21

There is currently uncertainty over the tax treatment of transfers of certain types of property (for example, attributing FIF interests) on a person's death in circumstances when the transfer qualifies for concessionary rollover relief. This is because the relevant provisions in subpart FC (for example, section FC 3(2)) refer to subpart FB to determine the treatment of the transfer – that is, subpart FC feeds into the existing provisions in subpart FB in certain cases. Because subpart FB deals with specific types of property in each section,[5] without a clear catch-all provision, some types of property covered by subpart FC (such as an attributing interests in a FIF) do not have a clear corresponding provision in subpart FB. While the policy intent of the legislation is clear, the provisions do not currently achieve that intent.

While it is arguable that section FB 1(2) could be seen as a default provision for property not otherwise covered by a specific provision, there are a number of issues with this provision. First, it is currently structured as a purpose, rather than an operative, provision (see the discussion of other changes below). Secondly, it currently only specifies the tax consequences of the transfer for the transfer*ee* and is silent on the position of the transfer*or* (even though the section FB 1(2) heading purports to cover both positions). Thirdly, it states that the tax consequences for the transferee on a settlement of relationship property are the same as if the transferor had continued to hold the property. Read literally, this would mean that when the transferee disposes of the property, there are no tax consequences for them because the transferor is deemed to still hold the property. This is contrary to the policy intent of the rollover relief intended to be provided by subpart FB.

These issues make it undesirable to rely on section FB 1(2), as currently drafted, as a default provision.

Accordingly, the amendments re-write section FB 1(2) as an operative default rollover relief provision (now contained in section FB 1C) to deal with property that does not have a corresponding specific provision in sections FB 2 to FB 21. The default provision ensures:

- the transferor has no tax consequences on disposal; and

[5] Sections FB 2 to FB 21 of the Income Tax Act 2007.

- the transferee acquires not only the property, but all the characteristics of the transferor with respect to that property – for example, date of acquisition, cost at acquisition, and intention of acquisition.

Other clarifying changes

The current headings of sections FB 1 and FC 1 ("What this subpart does") are headings more appropriate for general purpose provisions, rather than operative provisions. Accordingly, they will be changed to reflect the operative nature of the provisions.

The definition of "settlement of relationship property" (currently in section FB 1(3) and to be included in new section FB 1B) has been amended to remove a potentially circular reference to a relationship agreement that creates a disposal and acquisition of property "under this subpart". The reference to a transaction "between parties" to a relationship agreement has also been removed in case the transfer of property occurs between one of the parties to the agreement and a third party (say, a family trust).

An incomplete section cross-reference in section FC 4(1)(b) will be corrected. The policy underlying section FC 4 is to accord rollover relief to property transferred on a person's death to a beneficiary who is a close relative or a charity. However, the wording refers to "a person exempt under section CW 43". The problem is that charities are not generally exempt under section CW 43. Instead, the section exempts the income of a deceased person's executor or administrator when it relates to a charitable bequest. It is sections CW 41 and CW 42 that exempt income derived by tax charities.

Accordingly, the reference in section FC 4(1) to section CW 43 will be extended to persons "exempt under sections CW 41, CW 42 or CW 43".

To help readers find the correct corresponding provision in subpart FB, cross-references to the relevant sections will be included in applicable sections in subpart FC (for example, a cross-reference in section FC 6 "Forestry assets transferred to close relatives" will cross-refer to sections FB 6 and FB 7).

FOREIGN INVESTMENT PIES: ACCESS TO LOWER TREATY RATE

(Clause 215)

Summary of proposed amendment

The bill amends the treatment of unimputed dividends derived from New Zealand-resident companies that are attributed to non-resident investors in a foreign investment variable-rate portfolio investment entity (PIE). This will ensure they are subject to the same rate of tax as if the shares were held directly by the non-resident.

Application date

The amendment will apply for the 2012–13 and later income years to align with the application date of the foreign investment PIE rules.

A "savings" provision will apply for taxpayers who filed returns based on the current wording of table 1B in schedule 6 up until the date of introduction of the bill.

Key features

The amendment restricts access to the lower 15% rate to investors in foreign investment PIEs who reside in a country that has a DTA with New Zealand that reduces the dividend NRWT rate. This is achieved by amending the relevant rows in table 1B in schedule 6 of the Income Tax Act 2007. The amendment is consistent with the policy intent of the foreign investment PIE rules.

Background

A non-resident investor in a foreign investment variable-rate PIE is subject to a 30% tax rate on all unimputed New Zealand dividends if they do not reside in a country that has a double tax agreement (DTA) with New Zealand. This rate is reduced to 15% if the investor resides in a country that has a DTA with New Zealand.

These rates were chosen so that a non-resident investor owning New Zealand shares through a foreign investment variable-rate PIE would be subject to the same amount of tax as if they owned the shares directly and were subject to non-resident withholding tax (NRWT) on the dividends. The non-DTA rate of NRWT on unimputed dividends is 30%; this rate is normally reduced to 15% under a double tax agreement (for portfolio dividends).

New Zealand has DTAs with certain countries which do not reduce the rate of tax on dividends – for example, those that only facilitate the exchange of information. When an investor from one of these countries holds New Zealand-resident company shares directly any unimputed dividends received will be subject to a NRWT rate of 30%.

INCOME STATEMENTS AND INCOME TAX FILING EXEMPTIONS

(Clauses 231 and 225 to 226)

Summary of proposed amendments

The bill introduces a number of amendments to the Tax Administration Act 1994 relating to when the Commissioner is required to issue an income statement and when an individual is required to file an income tax return.

Application dates

The amendment to income statements for IR 56 taxpayers and the amendment to the schedular payment filing exemption will apply on 1 April 2014.

The amendments for an employee's obligations and other section 33AA amendments will have the same application date as the current section 33AA, which is scheduled to come into force on 1 April 2016.

Key features

Income statements for IR 56 taxpayers

The Taxation (Annual Rates, GST, Trans-Tasman Imputation and Miscellaneous Provisions) Act 2003 removed the requirement for most IR 56 taxpayers to file end-of-year income tax returns.[6] Instead the Commissioner was required to issue an income statement to IR 56 taxpayers. The drafting of this provision did not, however, make it clear that it was only intended to apply to IR 56 taxpayers, leaving open the possibility that income statements could be required to be issued to many other taxpayers, including those who would not otherwise have to file an income tax return. An amendment in this bill clarifies the application of the relevant provision.

Schedular payment filing exemption

The bill aligns the legislation with the current practice that an individual, who is not otherwise required to file an income tax return, will only have to do so when they derive more than $200 of schedular payments, irrespective of their total income. This replaces the current requirement that an individual, who is not otherwise required to file an income tax return, will have to do so if their total income is more than $200 and they derive any amount of schedular payments.

[6] These taxpayers include private domestic workers, staff of foreign consulates and embassies, New Zealand-based representatives of foreign companies and Operation Deep Freeze personnel.

Employee's obligations

Section 33A of the Tax Administration Act 1994 – which sets out when an individual is not required to file an income tax return – is scheduled to be replaced by section 33AA with effect from 1 April 2016. One provision within section 33A requires an individual to file a return if the employee's obligations are not met. The equivalent provision in section 33AA requires an individual to file a return if the employer's or PAYE intermediary's obligations are not met. An employer has additional obligations to those of an employee, such as having to pay to Inland Revenue tax that has been withheld. To maintain current policy settings this bill includes an amendment so that section 33AA will refer to the employee's (rather than employer's) obligations not being met.

Exceptions to requirement for return of income

An individual is required to consider whether their income falls within the criteria in section 33AA(1) to (3) of the Tax Administration Act 1994 to determine whether they are required to file an income tax return. The bill includes amendments to these three subsections which will simplify their interpretation without changing their application.

GST RATIO METHOD FOR CALCULATING PROVISIONAL TAX

(Clauses 200 and 201)

Summary of proposed amendments

An amendment clarifies that a person must stop using the GST ratio method to determine the amount of provisional tax payable for a tax year, if:

- the person files a return of income during that tax year; and
- the residual income tax (RIT) calculated in that return of income means the taxpayer no longer meets the requirements of section RC 16(2) and (5) of the Income Tax Act 2007.

The person must cease using the GST ratio method from the date on which the return of income is filed. The taxpayer must then apply either the estimation method or a standard method for calculating their provisional tax. The method used depends on whether the return of income was filed before or after the due date for Instalment A of provisional tax.

Application date

The amendments apply from the beginning of the 2016–17 income year.

Background

A taxpayer may choose to use the GST ratio method to calculate provisional tax payable for a tax year if all of the following requirements in section RC 16 are satisfied:

- RIT for the preceding year from which the GST ratio is calculated must be within the range of $2,501 to $150,000 for the year;
- they must be GST-registered for the entire prior year; and
- their ratio of RIT to total taxable supplies for the prior year (GST ratio) must not exceed 100 percent or be less than 0 percent. The GST ratio is applied to taxable supplies (turnover) in each GST period to determine the provisional tax payable.

Once a year has started, if a taxpayer does not satisfy the above requirements, the GST ratio method for calculating provisional tax is not intended to continue to be available to the taxpayer. At present, the legislation does not clearly address this issue if RIT calculated in a return of income for an earlier tax year and filed during the current tax year means that the above requirements are not satisfied.

Detailed analysis

The residual income tax calculated in an income tax return filed for an earlier tax year may result in either the RIT or GST ratio falling outside the required thresholds to use the GST ratio method for calculating provisional tax. This is illustrated in the following example.

Example

For provisional tax payments for the 2014–15 tax year, a taxpayer having an extension-of-time arrangement for filing the income tax return for the 2013–14 year, might not file the return until 31 March 2015.

For due dates for payment of provisional tax falling before this return is filed, the taxpayer would not know the RIT and annual turnover figures from the 2013–14 tax year. The taxpayer is then permitted to use the RIT and annual turnover data from the 2012–13 year to calculate provisional tax due for the 2014–15 tax year.

After filing the 2013–14 annual return of income, if the RIT for the 2013–14 tax year exceeds the $150,000 threshold, the taxpayer becomes ineligible to use the GST ratio method for the 2014–15 year.

In this case, the proposed amendment clarifies that the taxpayer must cease to use the GST ratio method for calculating provisional tax. Instead, they must use either:

- the standard or estimation method of determining provisional tax, if the return is filed before the due date for Instalment A of provisional tax for the tax year. In this case, the taxpayer is also treated as never having elected to apply the GST ratio method for the tax year; or
- the estimation method, if the return is filed after Instalment A of provisional tax for the tax year.

Some minor consequential amendments are also proposed to clarify that:

- the date the taxpayer is treated as ceasing to use the GST ratio method is the date on which the relevant return of income is filed; and
- if the taxpayer is a borrower under the Student Loan Scheme Act 2011, the requirement to cease using the GST ratio method for calculating provisional tax does not change the due dates for student loan repayments.

REPORTING REQUIREMENTS OF EMPLOYERS IN THE AGRICULTURE, HORTICULTURE AND VITICULTURE INDUSTRIES

(Clause 224)

Summary of proposed amendment

The bill repeals section 24O of the Tax Administration Act 1994 that obligates employers in the agricultural, horticultural or viticultural industries to provide Inland Revenue with information about employees covered by an exemption certificate or special tax rate certificate.

These requirements would have imposed unreasonable costs on employers and Inland Revenue while not being effective at identifying non-compliant employees. Accordingly, the provision has not been enforced and instead employers can check the validity of an employee's certificate directly with Inland Revenue.

Application date

The amendment applies for the 2008–09 and later income years to align with the original introduction of this provision.

REPEAL OF REDUNDANT COST OF TIMBER PROVISION

(Clause 237)

Summary of proposed amendment

The bill repeals section 92AAA of the Tax Administration Act 1994, which requires the Commissioner to issue a determination on the cost of timber incurred. This provision was introduced when the cost of timber was recorded in a separate account and carried forward to be offset against future forestry income.

The cost of timber is now deductible in the year incurred without the need for the Commissioner to issue a determination, rendering section 92AAA redundant.

Application date

The amendment will apply for the 2015–16 and later income years.

NON-MONETARY CONSIDERATION IN THE CONTEXT OF SALES

(Clauses 102 and 219)

Summary of proposed amendments

The bill amends a number of references to "sale" and similar terms in the Income Tax Act 2007 to ensure that transfers or supplies in exchange for non-monetary consideration are covered by the relevant provisions. These amendments address concerns that references to "sale" and similar terms may require an exchange of money and may therefore exclude transactions involving an exchange for non-monetary consideration such as a disposal of shares in exchange for a financial arrangement.

The terms that have been amended include "sale", "buy", "purchase" and variations of these terms.

Application date

The amendments will apply for the 2015–16 and later income years.

FINANCIAL MARKETS (REPEALS AND AMENDMENTS) ACT 2013 – RELATED CHANGES

(Clauses 213(55) and 266)

Summary of proposed amendments

The bill makes several amendments relating to the Financial Markets (Repeals and Amendments) Act 2013.

Application date

The amendments will come into force on the date of enactment.

Key features

Approved unit trusts

The Financial Markets (Repeals and Amendments) Act 2013 amended the definition of an "approved unit trust" in the Finance Act (No 2) 1990 to refer to the definition of a unit trust in the Income Tax Act 2007 rather than the Unit Trusts Act 1960, which is to be repealed.

A further amendment is proposed so that the definition in the Finance Act (No 2) 1990 excludes paragraph b(x) of the unit trust definition in the Income Tax Act 2007. Paragraph b(x) excludes an approved unit trust from being a unit trust so this amendment is necessary to allow an approved unit trust to meet the Finance Act (No 2) 1990 definition.

Public unit trusts

The Financial Markets (Repeals and Amendments) Act 2013 amended the definition of a "public unit trust" in the Income Tax Act 2007 to refer to regulated offers made under the Financial Markets Conduct Act 2013 rather than securities offered to the public under the Securities Act 1978, which is to be repealed. A regulated offer under the Financial Markets Conduct Act 2013 is not a direct equivalent to an offer of securities to the public under the Securities Act 1978; as a result, this amendment altered the scope of what could qualify as a public unit trust.

A further amendment to the definition of a public unit trust in the Income Tax Act 2007 is proposed, to remove the requirement that regulated offers are made under the Financial Markets Conduct Act 2013 (there being no equivalent concept of offers to the public in the Financial Markets Conduct Act 2013). Paragraph (a) of the public unit trust definition will now require 100 or more unit holders, treating all associated persons as one person, who meet the current requirements in subparagraphs (i) to (iii). Paragraph (b)(vi) and (vii) will have their thresholds reduced from 25 percent to 5 percent to ensure public unit trusts qualifying under these provisions are sufficiently widely held.

THIN CAPITALISATION

(Clauses 153 to 156 and 158)

Summary of proposed amendment

The changes to the thin capitalisation rules in the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 included a provision to deem the worldwide group of a New Zealand company to be the same as its New Zealand group in certain situations. These are when the company is subject to the thin capitalisation rules only because it:

- is controlled by a non-resident owning body; or
- is controlled by a trustee that is subject to the thin capitalisation rules.

This section does not operate as intended in every situation. Accordingly the bill proposes a re-drafting of the provision to ensure it operates as described above.

The bill also corrects minor errors such as cross-references in their clauses.

Application date

The amendments will apply from the beginning of the 2015–16 income year, the application date of the thin capitalisation changes introduced in the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014.

RESPONSE PERIOD FOLLOWING DISPUTES RESOLUTION PROCESS DOCUMENT

(Clauses 234 and 235)

Summary of proposed amendments

The proposed amendments will clarify that the Commissioner's response period when a taxpayer is late in issuing a disputes document starts from the time when it is decided that "exceptional circumstances" exist and the taxpayer's late dispute document is to be allowed.

Application date

The amendments will come into force on the date of enactment.

Key features

Amendments to section 89AB of the Tax Administration Act 1994 will clarify that the Commissioner's response period when a taxpayer is late in issuing a disputes document starts from the time when it is decided that "exceptional circumstances" exist and the taxpayer's late document is to be allowed. If the response period applied while a decision was being reached, the Commissioner would be required to issue a substantive response to a dispute that may not have a procedural basis.

Background

Certain documents that form part of tax disputes procedures are subject to mandatory response periods. A breach of a response period can see a disputant forfeit their right to begin or continue with a dispute. If exceptional circumstances are found to exist, however, a notice issued by the taxpayer that is late will be treated as if it had been given within the required response period.

The decision about whether there are "exceptional circumstances" is at the discretion of the Commissioner. A taxpayer may challenge the Commissioner's refusal notice by filing proceedings with the Taxation Review Authority within two months of the notice being issued.

The proposed change clarifies uncertainty in the current law, where it could be argued that if a taxpayer issues an initiating document late, the Commissioner may be required to file a response document prior to the establishment of any exceptional circumstances that would allow the dispute to continue.

COMMISSIONER'S ABILITY TO TRUNCATE THE DISPUTES PROCESS UNDER A TAXPAYER-INITIATED DISPUTE

(Clauses 236 and 241)

Summary of proposed amendments

The proposed amendments ensure that truncation is allowed in a taxpayer-initiated dispute after the taxpayer has issued a Statement of Position without requiring the Commissioner to first issue a Statement of Position.

Application date

The amendments will come into force on the date of enactment.

Key features

An amendment to section 89M(6BA) of the Tax Administration Act 1994 will ensure that after the taxpayer has issued a Statement of Position the Commissioner and the taxpayer can agree in accordance with section 89N(1)(c)(viii) to submit the dispute to the court or Taxation Review Authority without requiring the Commissioner to issue a Statement of Position. The change is only relevant for taxpayer-initiated disputes.

An amendment to section 138G will mean that if a taxpayer-initiated dispute proceeds in this way, the taxpayer will be bound by the exclusion rule and the Commissioner will not. This avoids the Commissioner not being able to raise any issues in the challenge and ensures the Commissioner can rely on information that would otherwise have been included in her Statement of Position.

Background

In a taxpayer-initiated dispute, the completion of the disputes procedures is either by the Commissioner agreeing to make any amended assessment or by issuing a challenge notice at which point the disputant is able to file challenge proceedings in the High Court or Taxation Review Authority.

Section 89P(3) of the Tax Administration Act 1994 provides that the Commissioner cannot issue a challenge notice without Statements of Position being exchanged. An exception to this rule is when the Commissioner and taxpayer agree in writing not to follow the full disputes procedures and go directly to court. However, section 89M(6BA) states that the Commissioner is required to issue a Statement of Position when the taxpayer has issued a Statement of Position.

The combination of these provisions means that, under the current law, the Commissioner must issue a Statement of Position in response to a taxpayer's Statement of Position even though both parties agree that the dispute should proceed to the challenge phase. This has the potential to delay a dispute unnecessarily and also impose unnecessary administration costs.

PETROLEUM MINING RULES

(Clauses 97, 98, 100, 101, 213(49), (50), (72) and (73))

Summary of proposed amendment

Amendments to the definitions of "mining permit", "petroleum exploration expenditure" and "existing privilege":

- correct unintended legislative changes made in rewriting those definitions into the Income Tax Act 2007; and
- implement a "savings" provision for taxpayers to protect tax positions taken in relation to the definition of petroleum exploration expenditure on arrangements entered into before the introduction of the bill.

Application date

The amendments will apply from the beginning of the 2008–09 income year.

Key features

The Rewrite Advisory Panel has agreed with a submission that the petroleum mining rules contain unintended legislative changes in the definitions of "mining permit" and "petroleum exploration expenditure". The submitter noted that the use of the term "existing privilege" was potentially ambiguous as it refers to both mineral mining and petroleum mining privileges issued under the 1937 Act.

The change identified is that these definitions inadvertently do not refer to petroleum mining privileges issued under the Petroleum Act 1937 (1937 Act). The policy intention is that the tax treatment for costs relating to mining privileges issued under the 1937 Act is intended to be determined under the petroleum mining rules.

The bill amends the definitions of "mining permit" and "petroleum exploration expenditure" to clarify that they include petroleum mining privileges issued under the 1937 Act. The use of the definition of "existing privilege" is clarified in the bill to distinguish more clearly when it refers to petroleum privileges issued under the 1937 Act.

The "savings" provisions protect a taxpayer's tax position taken in relation to an arrangement for the acquisition of a petroleum mining asset that was entered into before the introduction of the bill.

TREATMENT OF EXPENDITURE FOR COMMERCIAL FIT-OUT

(Clauses 82 and 83)

Summary of proposed amendment

A specific rule relating to expenditure on items of commercial fit-out (section DA 5) is proposed to be removed from a subpart intended for general provisions relating to deductions and re-enacted in a more appropriate place (section DB 22B).

No change in effect of the provision is intended.

Application date

The amendment applies from the beginning of the 2011–12 income year.

Background

Section DA 5 is concerned with how the capital limitation rule applies to certain expenditure incurred on commercial fit-out. In particular, it is intended to ensure that:

- capital expenditure incurred for commercial fit-out is not immediately deductible as repairs and maintenance on the building; and
- the replacement or improvement of a previously separately depreciated item of commercial fit-out is capitalised and depreciated over its estimated useful life.

The Rewrite Advisory Panel noted that section DA 5 is inconsistent with the scheme and purpose of subpart DA, which:

- contains the general permission; and
- sets out principles and rules for understanding the relationship of the general permission with specific deduction provisions in Part D.

The Rewrite Advisory Panel noted that the risks of retaining the current section DA 5 in subpart DA are the potential for:

- misunderstanding and misinterpretation of the scheme and purpose for subpart DA; and
- section DA 5 to be cited as an example/precedent in support of placing other targeted provisions in subpart DA.

ELECTION TO BE A COMPLYING TRUST

(Clauses 167 and 170)

Summary of proposed amendment

Amendments to sections HC 10 and HC 33 of the Income Tax Act 2007 (election to be a complying trust):

- correct an unintended legislative change made in relation to an election to be a complying trust; and
- allow a trust to continue to be treated as a complying trust after the settlor migrates from New Zealand if, since that time, the trustee has continued to comply fully with New Zealand income tax obligations.

Application date

The amendments will apply from the beginning of the 2008–09 income year.

Key features

Rewrite matter

The Rewrite Advisory Panel has agreed with a submission that the rules relating to the election for a trust to be a complying trust (sections HC 10 and HC 33 of the Income Tax Act 2007):

- are partially ineffective and this is caused by an unintended legislative change; and
- do not reflect the policy intention.

A complying trust is a trust for which the trustees:

- are liable for tax at the trustee rate on all their world-wide trustee income; and
- have always met their income tax compliance obligations.

A foreign trust is a trust which does not have a settlor resident in New Zealand at all times since the trust was formed, but is not a complying trust because the trustee either:

- is not liable for tax at the trustee rate on foreign-sourced income; or
- derives non-resident passive income that is not subject to full rates of tax in New Zealand.

It is intended that a foreign trust may be treated as a complying trust if:

- a settlor, trustee or beneficiary of the trust elects for the trust to pay tax at the trustee rate on its world-wide trustee income; and
- the trustees continue to meet their income tax compliance obligations.

However, due to the unintended legislative change, a foreign trust is restricted to choosing to satisfy the income tax liability for taxable income of the trust. The taxable income of a foreign trust does not normally include foreign-sourced income. This unintended legislative change could prevent the trust from meeting the requirements to be a complying trust. The amendment ensures that the election to be a complying trust relates to paying tax at the trustee rate on the world-wide trustee income of the trust.

Remedial matter

The amendments also address a minor remedial matter, mainly relating to situations that have arisen for trustee companies, such as the Public Trust. These trustees act for many trusts and are not always made aware when a settlor's residence changes.

If the trustee is not aware when a settlor migrates from New Zealand, the trustee may:

- continue to treat the trust as a complying trust, calculating and paying tax at the trustee rate on the world-wide trustee income of the trustee; and
- indicate in the annual return of income that the trust is a complying trust.

The amendment clarifies that if a settlor of a complying trust migrates from New Zealand, the trust will continue to be treated as a complying trust if:

- the trustee continues to pay New Zealand tax at the trustee rate on the world-wide trustee income of the trust; and
- the trustee indicates in the annual return of income the intention for the trust to be a complying trust.

BAD DEBT DEDUCTION AND CAPITAL LIMITATION

(Clauses 84(4), (7) and 257)

Summary of proposed amendment

The amendment to section DB 31(6)(b)(iii) of the Income Tax Act 2007 (and section DB 23 (6)(b)(iii) of the Income Tax Act 2004) clarifies that the capital limitation does not prevent a deduction for a bad debt of the principal amount of a financial arrangement entered into in the normal course of business.

This amendment does not alter the current treatment of debts owed by associated persons.

Application date

The amendments will apply from the beginning of the 2008–09 income year (2007 Act) and the 2005–06 income year (2004 Act).

Key features

The Rewrite Advisory Panel has agreed with a submission that there is an unintended legislative change in the bad debt deduction rule relating to taxpayers carrying on a business of holding or dealing in financial arrangements (business holder or dealer).

The Panel recommended that the unintended legislative change to the bad debt deduction rule should be corrected retrospectively to the beginning of the 2005–06 income year (the first year to which the 2004 Act applied).

The retrospective remedial amendment addresses the potential adverse consequence identified by the Panel that the bad debt rule in section DB 31 may deny a deduction to a business holder or dealer for the principal amount of a financial arrangement. An example of this possible adverse consequence is for a holder of securitised financial arrangements, if those securitised assets are entered into in the normal course of business.

The policy intent for the bad debt deduction rule for a business holder or dealer is to allow a bad debt deduction to a business holder or dealer for both accrued interest and the principal amount of a debt entered into in the ordinary course of business.

This policy stems from the 1987 recommendations of the Consultative Committee on Accrual Tax Treatment of Income and Expenditure (the Brash Committee)[7] to maintain the common law position in relation to bad debt deductions, except for bad debts entered into between associated persons.

[7] Report of the Consultative Committee on Accrual Tax Treatment of Income and Expenditure, April 1987, paras 32-41, comment on drafting para 2.632-41, comment on drafting para 2.6.

Under the common law,[8] a bad debt suffered by a business holder or dealer which related to a financial arrangement entered into in the ordinary course of business was considered to be on revenue account. In this circumstance, the common law held that a bad debt deduction was allowed for a loss of principal and accrued interest, provided some procedural requirements were satisfied.

The common law also considered that a debt entered into outside the normal or ordinary course of business would be usually treated as a non-deductible capital loss as a result of applying the capital/revenue tests.

The bad debt deduction rule has always been intended to replicate this common law effect for business holders and dealers.

The Brash Committee also considered that the common law treatment for bad debts should not apply to debts between associated persons. The policy concern identified was that the common law treatment of bad debts could allow associated persons to convert truly capital losses into revenue deductions simply by substituting what would ordinarily be equity capital for a debt instrument.

Current legislation ensures that the principal amount of a debt between associated persons is not deductible as a bad debt. The amendment does not change that outcome.

[8] Summarised in *Levin and Co., Ltd. v Commissioner of Inland Revenue* [1963] NZLR 801.

TRANSFER OF FINANCIAL ARRANGEMENTS ON AMALGAMATION

(Clause 160)

Summary of proposed amendment

The proposed amendment will ensure that when two companies amalgamate, the income or expenditure arising in the year of amalgamation under a financial arrangement held by the amalgamating company (the company that ceases to exist) is allocated on a fair and reasonable basis between the amalgamating company and the amalgamated company (the company that continues to exist).

Application date

The proposed amendment will apply to amalgamations occurring in the 2008–09 and later income years. There will be a "savings" provision for tax positions taken by taxpayers in these income years based on the current legislative wording.

Key features

When two companies amalgamate, and as a result, a financial arrangement is transferred by the amalgamating company to the amalgamated company, in most cases the amalgamating company must perform a base price adjustment (BPA).

In calculating the BPA, the amalgamation rules intend to ensure that the amalgamating company is allowed a deduction for expenses incurred (or returns any income derived) up until the date of the amalgamation. Any amounts incurred or derived after this point should be incurred/derived by the amalgamated company. This ensures that the rules give the correct amount of expenditure or income over the remaining life of the financial arrangement.

The current wording of section FO 13(2) of the Income Tax Act 2007 does not achieve this result. This is because section FO 13(2) provides the incorrect amount of "consideration" to be included in the BPA formula. The BPA formula (found in section EW 31) is:

$$\text{BPA} = \text{consideration} - \text{income} + \text{expenditure} + \text{amount remitted}$$

Section FO 13(2) states:

> The amalgamating company is treated as having disposed of the financial arrangement. In calculating the base price adjustment, the <u>consideration</u> [emphasis added] is the amount that would fairly and reasonably represent the income or expenditure that the amalgamating company would have derived or would have incurred in the income year if the amalgamation had not taken place.

Before 1999 (section FE 7(3) of the Income Tax Act 1994 and section 191 WD(17)(b) and (18)(b) of the Income Tax Act 1976), the provision read:

> The consideration for which the succession has taken place shall be deemed to be equal to such amount as will result in the base price adjustment [emphasis added] in relation to the amalgamating company calculated in respect of the succession under section EH 4 being such amount (whether negative, positive, or a nil amount) as will result effectively in a fair and reasonable allocation, having regard to the tenor of section EH 1, between the amalgamating company and the amalgamated company, of the expenditure or gross income which would have been deemed to be incurred or derived by the amalgamating company in respect of the financial arrangement in the income year in which the amalgamation takes place had the amalgamation not taken place.

The difference between the sections is that the pre-1999 legislation deemed the *result* of the BPA to be a fair and reasonable allocation of income and expenditure between the amalgamating and amalgamated companies. The post-1999 provision deems the *consideration* component in the BPA formula to be a fair and reasonable allocation of income and expenditure between the amalgamating and amalgamated companies.

As demonstrated by the example below, the latter approach gives the incorrect result and will sometimes result in too much income being derived and sometimes result in excessive deductions.

The proposed amendment restores section FO 13(2) to the pre-1999 position.

Example

An amalgamating company borrows $100 and pays interest in year 1 of $3, in year 2 of $3 and in year 3 an amalgamation takes place and the amalgamating company only pays $1.50 interest. The amalgamated company pays the remaining $1.50 for year 3.

Under the current drafting of section FO 13, the BPA for the amalgamating company gives the following result:

BPA = **consideration** − income + expenditure + amount remitted
= –**$1.50** – $0 + $6 + $0
= $4.50

Accordingly, the amalgamating company has $4.50 income in the year of amalgamation, whereas it should receive a $1.50 deduction.

Under the proposed amendment, section FO 13 will give the following result under the BPA for the amalgamating company:

Result of the BPA = –$1.50

Therefore, the amalgamating company will be entitled to a $1.50 deduction in the year of amalgamation. The amalgamated company will also be entitled to a $1.50 deduction in the year of amalgamation.

TRANSITIONAL RESIDENT DEFINITION

(Clause 176)

Summary of proposed amendment

Amendments to section HR 8 are proposed to clarify the position that persons who would otherwise be transitional residents are not treated as such if they have elected not to be a transitional resident. This was clear in the Income Tax Act 2004 and the proposed amendments will make this clear for the Income Tax Act 2007.

Other wording changes to section HR 8(2) to (4) are proposed to improve clarity in the section as a whole.

Application date

The amendments will apply from the beginning of the 2008–09 income year.

DRAFTING AMENDMENT TO SECTION 10(7A) OF THE GOODS AND SERVICES TAX ACT 1985

(Clause 251)

Summary of proposed amendment

Currently, section 10(7A) requires that if goods and services are deemed to be supplied by a person under sections 5(3) **and** (3B), the consideration in money for the supply is treated as being the open market value of the supply. However, section 5(3) and (3B) would never apply simultaneously. Instead, the value of the supply should be at market value where either 5(3) **or** (3B) apply [emphasis added].

Application date

The amendment will apply beginning on 1 April 2014.

HERD SCHEME LIVESTOCK PURCHASED OR SOLD BY COMPANIES

(Clause 69)

Summary of proposed amendment

Herd scheme livestock are held on capital account. Section CD 44 of the Income Tax Act 2007 provides that the net tax-free herd scheme gains of a company are a capital profit, and therefore tax-free upon a liquidation of the company, to prevent their eventual taxation as a dividend. A consequential amendment is proposed, to ensure that new capital amounts created by the recent livestock valuation reforms are also tax-free upon their eventual distribution by a company.

Application date

The amendment will apply from 28 March 2012, the date the original amendments came into effect.

Key features

Section CD 44 is being amended to extend the definition of "capital gain" to ensure that new capital amounts created by the livestock valuation reforms are tax-free upon liquidation of a company. This is necessary to recognise that the recent amendment that provides that herd scheme livestock transfers between associated parties are at herd values for taxation purposes. However, the parties may have agreed a different valuation for the actual transaction and this amendment provides that the difference between the valuations, which is on capital account, is regarded as a capital gain or a capital loss by parties to the transaction that are corporates.

REMOVAL OF SPENT TERMINOLOGY

(Clauses 77, 123, 213, 245 and 252)

Summary of proposed amendment

References to *"new start grants"* are being repealed in the Inland Revenue Acts as they are no longer part of the suite of responses the Government uses for primary sector adverse events.

Application date

The amendments will apply from the day after the date of enactment.

BAD DEBTS REMEDIAL

(Clause 84)

Summary of proposed amendment

Amendments were made to the tax rules last year to ensure taxpayers take bad debt deductions only when they suffer economic losses. Further technical amendments are required to ensure that the correct outcomes are achieved.

Application date

These amendments will apply from 20 May 2013 to align with the application of the original amendments.

Key features

The new base maintenance rules included in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Act 2014 for deductions for bad debts for financial arrangements had the policy objective of ensuring taxpayers take bad debt deductions only when they suffer economic losses. The operation of the rules is quite complex, and as currently drafted, the application of subsections DB 31(4B) to (4E) does not give the intended result. The proposed amendments ensure that the subsections give the correct bad debt deductions at appropriate times, consistent with the policy objective.

The requirement for these changes was signalled to taxpayers in the *Tax Information Bulletin* published in May 2014, which discussed the original amendments.

FINANCIAL ARRANGEMENT REMEDIAL – SPREADING INCOME

(Clauses 121 and 146)

Summary of proposed amendments

In very limited circumstances, International Financial Reporting Standards (IFRS) allow an amount associated with a financial arrangement to be taken directly to equity as a contribution to capital, and not be further dealt with. Accordingly it is then argued that this amount is not recognised for taxation purposes. The proposed amendment requires the amount to be recognised as taxable income, and provides for a catch-up calculation for past years, to be completed by companies that have taken this position.

Application date

The core amendment will apply from the start of the 2014–15 tax year. The catch-up will be required to be done in the 2015–16 tax year.

Key features

Most types of debt are taxed under the financial arrangement rules. These rules require taxpayers to spread the income or expenditure that is expected to arise over the term of the debt.

There is an issue with how the IFRS financial reporting spreading method operates because of a particular transaction between two companies. Under the specific wording of that spreading method, one of the companies can exclude a portion of its income from the ambit of the spreading method (technically, because the company has been able to treat the income as a contribution to capital). This means the company will not be required to pay tax on the income until the debt expires, which will provide it with a significant timing advantage. This is inappropriate.

Technical amendments are proposed to section EW 15D of the Income Tax Act 2007 to address this.

When a catch-up is necessary, proposed section EZ 36B will provide for this.

REWRITE AND OTHER MINOR TECHNICAL AMENDMENTS

(Clauses as shown)

Summary of proposed amendments

The following amendments reflect minor technical maintenance items arising from both the rewrite of Income Tax legislation and subsequent changes.

Until its disestablishment on 2 December 2014, the Rewrite Advisory Panel monitored the working of the Income Tax Act 2007 and reviewed submissions on what may have been unintended changes in the law as a result of its having been rewritten. The Panel recommended legislative action, when necessary, to correct any problems. Since the Panel's disestablishment, this process is being managed by Inland Revenue within its normal remedial tax policy work programme.

Application dates

Unless otherwise stated, all the amendments to the Income Tax Act 2007 (2007 Act) 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 to 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.

Clause	Section	Act	Amendment	Commencement date
68	CD 39	2007 Act	Repeal redundant provisions	Assent
74(2)	CQ 2	2007 Act	Repeal redundant provisions	Assent
78	CX 56C	2007 Act	Terminology corrected	1 April 2010
79	CZ 10	2007 Act	Repeal redundant provision	Assent
80	CZ 29(3)	2007 Act	Insert subsection heading	4 September 2010
86	DB 35	2007 Act	Terminology corrected	1 April 2015
103	EC 41	2007 Act	Terminology corrected	
108	EE 32	2007 Act	Terminology corrected	
120	EW 9	2007 Act	Cross-references corrected	
131	EX 25	2007 Act	Repeal redundant provisions	Assent
144	EZ 5	2007 Act	Terminology corrected	
157	FE 28	2007 Act	Grammar corrected	
159	FO 12	2007 Act	Ambiguity and cross-reference corrected	
161-164	GB 8, GB 9, GB 11, GB 13	2007 Act	Repeal redundant provisions	Assent
185	LP 6	2007 Act	Repeal redundant heading	Assent
186	LU 1	2007 Act	Terminology corrected	1 April 2014
193	OB 1	2007 Act	Drafting consistency	
196-198	OP 27, OP 50, Table O19	2007 Act	Terminology corrected	
199	RC 7	2007 Act	Terminology corrected	
202	RD 27	2007 Act	Terminology corrected	
213(16), (17)	YA 1 “employee”, “employer	2007 Act	Cross-reference corrected	5 Jan 2010
213(33)	YA 1 “mineral miner”	2007 Act	Insert index entry for definition	1 April 2014
213(41), (42)	YA 1 “non-filing taxpayer”	2007 Act	Cross-reference corrected	
213(64), (65)	YA 1 “tax position”, “tax situation”	2007 Act	Cross-reference and terminology corrected	Assent
190	MC 5	2007 Act	Terminology corrected	