

Reporting requirements for domestic trusts

where disclosure is required under the Tax Administration Act 1994

An officials' issues paper

October 2021

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First published in October 2021 by Policy and Regulatory Stewardship, Inland Revenue, PO Box 2198, Wellington 6140.

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ISBN 978-1-98-857332-8 (Online)



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CHAPTER 1

Introduction

- 1.1 In December 2020, amendments were made to the Tax Administration Act 1994 (TAA) to require trustees of certain domestic trusts to prepare financial statements. The requirements apply to trusts that have assessable income and do not fall within certain exclusion categories.
- 1.2 Trustees of such trusts must prepare a statement of profit and loss and a statement of financial position to at least a special-purpose level. These statements, unless otherwise required by the Commissioner, must be included with the annual return for the 2021–22 and later income years.
- 1.3 Inland Revenue will administer the setting of minimum requirements for these special-purpose financial statements. An Order in Council will mandate to what degree of detail the financial statements should be prepared.
- 1.4 This issues paper outlines proposals for the minimum requirements for financial statements to be included in the Order in Council. The financial statements may be prepared to any level above the minimum specified by the Order in Council.
- 1.5 Two similar Orders have been made under section 21C of the TAA:
 - the Tax Administration (Financial Statements) Order 2014¹ sets out the minimum standards for financial statements of companies, and
 - the Tax Administration (Financial Statements—Foreign Trusts) Order 2017² sets out the minimum standards for financial statements of foreign trusts.
- 1.6 The Commissioner will require certain trust financial information to be provided using prescribed forms. However, although prescribed forms may summarise financial statements, they do not replace them. The Commissioner will not require financial statements to be included with the prescribed forms, but they may be requested later.
- 1.7 The December 2020 amendments also require trustees of domestic trusts to make disclosures in their annual returns about information on settlements and distributions as well as appointer details. Inland Revenue is currently consulting on a draft operational statement setting out the Commissioner’s approach to applying the trust information gathering powers contained in section 59BA and section 59BAB of the Tax Administration Act 1994.³

¹ *Tax Administration (Financial Statements) Order 2014*.
<https://legislation.govt.nz/regulation/public/2014/0069/latest/whole.html>

² *Tax Administration (Financial Statements—Foreign Trusts) Order 2017*.
<https://legislation.govt.nz/regulation/public/2017/0258/latest/whole.html>

³ Inland Revenue. (2021). *ED0235: Reporting requirements for domestic trusts*. (Draft operational statement). <https://www.taxtechnical.ird.govt.nz/consultations/draft-items/ed0235>

Summary of proposals

Who is affected?

- 1.8 For the 2021–22 and later income years, these minimum standards apply to trustees of trusts required to comply with the disclosure requirements set out in section 59BA(2) of the TAA.
- 1.9 These minimum standards also apply to trustees of trusts required to comply with a request made by the Commissioner under section 59BAB. This section allows the Commissioner to require disclosure information from certain trustees for the previous seven years, where such information exists.
- 1.10 Sections 59BA and 59BAB are reproduced in the appendix. More information on these sections is also available in *Tax Information Bulletin* Vol 33 No 3 (April 2021).⁴
- 1.11 If a trust does not derive assessable income, it is not required to file a return and the disclosure requirements do not apply. This includes, for example, trusts that own holiday homes and derive no assessable income. If a trust is non-active and an IR633 *Non-active trust declaration*⁵ has been filed with the Commissioner, it will also be excluded from the disclosure rules. Section 59BA(3) lists other trusts that are not required to meet the disclosure requirements.
- 1.12 Inland Revenue records indicate that approximately 180,000 domestic trusts (excluding estates) report assessable income each year and may be affected to some extent by the new disclosure requirements. However, the financial statement disclosure requirements will primarily affect approximately 55,000 of these domestic trusts. These are trusts that report assessable income to Inland Revenue but do not currently report business income or file any financial statements.

Principles for the minimum proposed requirements

- 1.13 Officials propose minimum standards for financial statements based on the following principles:
- i. The statements should be based on the double-entry method of recording financial transactions and the principles of accrual accounting.
 - ii. The statements should include a statement of accounting policies and changes.
 - iii. Amounts may be disclosed using tax values, historical cost, or market values at the discretion of the preparer of the statements.
 - iv. The statements should include a reconciliation between the profit or loss in the statement of profit and loss to taxable income and a reconciliation of movements from opening to closing balances, on a line-by-line basis, of all beneficiary accounts.

⁴ Inland Revenue. (2021). Increased information required in trustees' annual returns. *Tax Information Bulletin*. vol 33 (no 3), 5–8. <https://www.taxtechnical.ird.govt.nz/tib/volume-33---2021/tib-vol-33-no3>

⁵ Inland Revenue. *IR633 Non-active trust declaration*. <https://www.ird.govt.nz/roles/trusts-and-estates/trusts-and-tax-residency>

- v. Transactions involving associated persons (as defined in subpart YB of the Income Tax Act 2007) should be included in a schedule unless they are minor and incidental to the activities of the trustee.
- vi. While disclosure of specific financial items in the annual return is proposed, there is scope for judgement on the level of detail beyond this.
- vii. There will be a de minimis exception for small trusts if the trustee has not derived annual income in excess of \$30,000, or incurred annual expenditure in excess of \$30,000, during the income year, and the value of total trust assets did not exceed \$2,000,000 within that income year. The de minimis in this proposal only provides partial relief from minimum financial reporting requirements (for example, cash accounting will be acceptable for small trusts). Small trusts will still be required to disclose amounts in any forms prescribed by the Commissioner.

How to make a submission

- 1.14 Submissions are invited on the level of detail suggested for the minimum financial reporting requirements.
- 1.15 Submissions should be made by **15 November 2021**.
- 1.16 Submissions can be made:
 - by email to policy.webmaster@ird.govt.nz with “Reporting requirements for domestic trusts” in the subject line; or
 - by post to:

Reporting requirements for domestic trusts
C/- Deputy Commissioner, Policy and Regulatory Stewardship
Inland Revenue Department
P O Box 2198
Wellington 6140
- 1.17 Submissions may be the result of a request under the Official Information Act 1982, and this may result in their publication. The withholding of particular submissions on the grounds of privacy, or for any other reason, will be determined in accordance with that Act. Submitters who consider any part of their submission should properly be withheld under that Act should clearly indicate this.

CHAPTER 2

Proposed financial reporting requirements

- 2.1 This chapter sets out the proposed minimum financial reporting requirements for financial statements for trusts to comply with their obligations under section 59BA of the TAA.
- 2.2 Financial statements must be prepared to at least these minimum requirements. They may be prepared to a higher standard or be general-purpose financial statements, provided the required information is included.

The proposed minimum requirements

Form of financial statements

- 2.3 The financial statements must consist of:
- i. a statement of financial position setting out the assets, liabilities, and net assets (equity) of the trust as at the end of the income year, and
 - ii. a profit and loss statement showing income derived, and expenditure incurred, by the trust during the income year.

Accounting principles statements must comply with

- 2.4 The financial statements must be prepared applying the following accounting principles:
- i. the double-entry method of recording financial transactions, and
 - ii. accrual accounting.

Valuations

- 2.5 The financial statements may disclose amounts using the following valuation principles:
- i. tax values, when those values are consistent with double-entry and accrual accounting
 - ii. historical cost, when tax values are not consistent with double-entry or accrual accounting or when, in the preparer's opinion, historical cost provides a better basis of valuation, and
 - iii. market values, when, in the preparer's opinion, market values provide a better basis of valuation than those in subparagraphs (i) and (ii).

Statement of accounting policies

- 2.6 The financial statements must contain a statement of accounting policies. This must set out, in sufficient detail so the material policies applied or changed can be identified:

- i. the policies and assumptions used in the preparation of the financial statements, and
 - ii. a description of the effect of any material changes in those accounting policies since the previous year for which financial statements were prepared.
- 2.7 The financial statements must disclose whether they have been prepared on a GST-inclusive or GST-exclusive basis.

Matters the statements must show

- 2.8 The financial statements must show the information prescribed in chapter 3.
- 2.9 The financial statements must disclose comparable figures for the previous income year.

How matters must be shown

- 2.10 Interest and dividends received must be shown in the financial statements grossed up for resident withholding tax.
- 2.11 Dividends received must be shown in the financial statements grossed up for imputation credits to the extent the dividends are taxable and the credits are available to satisfy the trust's income tax liability for the income year.

Small trusts exempt from some minimum requirements

- 2.12 Small trusts are exempt from the following minimum requirements:
- i. applying the principles of accrual accounting (cash accounting will be acceptable for small trusts)
 - ii. providing a statement of accounting policies, and
 - iii. disclosing comparable figures for the previous income year.
- 2.13 A trust is small for an income year if, for that income year, the trustee has not derived annual income in excess of \$30,000, or incurred annual expenditure in excess of \$30,000, during the income year, and the total value of trust assets did not exceed \$2,000,000 within that income year.

Commentary

- 2.14 The \$30,000 income and \$30,000 expenditure de minimis thresholds proposed for trustees are consistent with de minimis thresholds in the Tax Administration (Financial Statements) Order 2014 for companies.
- 2.15 The proposed introduction of an asset threshold reflects the Commissioner's interest in understanding the use of trusts for wealth accumulation. It will mean that trustees with assets above \$2 million will be subject to all of the minimum financial reporting requirements.
- 2.16 Given that some trusts may move in and out of this disclosure regime (for example, if they did not have assessable income in one year), the proposed asset test will be

limited to assets held in the income year for which a disclosure is required rather than applying the test to assets reported in previous income years.

- 2.17 The de minimis in this proposal only provides partial relief from minimum financial reporting requirements rather than full relief, which will support the integrity of the financial statements required under section 59BA(2)(a) of the TAA.
- 2.18 According to Inland Revenue estimates based on data provided in 2020 IR10 financial statement summaries, if a \$30,000 income and \$30,000 expenditure test is introduced for de minimis purposes, 44% of trustees subject to the disclosure rules will qualify for the de minimis. If trustees are also required to hold assets that do not exceed \$2 million within that income year, the proportion of trustees that qualify for the de minimis will fall to 38%.

Questions for submitters

1. Do you have any comment on the specific items proposed?
2. Should small trusts be partially exempt from these requirements? If so, is exemption from the following requirements appropriate?
 - The requirement to apply the principles of accrual accounting (cash accounting will be acceptable for small trusts).
 - The requirement to provide a statement of accounting policies.
 - The requirement to disclose comparable figures for the previous income year.
3. If there is to be a partial exemption for small trusts, is the proposed \$30,000 income and \$30,000 expenditure threshold, and the requirement that the value of total trust assets did not exceed \$2,000,000 within that income year, appropriate?

CHAPTER 3

Proposed information that financial statements must show

- 3.1 This chapter covers the information a trust must show in its financial statements. The information required will be prescribed in a schedule in the Order in Council.

The proposed information required

- 3.2 The proposed information required in the schedule covers:

- reconciliations
- trusts with a particular type of business
- items from prescribed forms, and
- associated persons transactions.

Reconciliations

- 3.3 A reconciliation of the trust's financial statements and taxable income for the income year.
- 3.4 A reconciliation of movements from opening to closing balances, on a line-by-line basis, of all beneficiary accounts, including loans.
- 3.5 An appropriately detailed, taxation-based, schedule of the trust's fixed assets and depreciable property.

Trusts with a particular type of business

- 3.6 If the trust is a forester, information about the cost of timber as at the end of the income year and a reconciliation of movements in the cost of timber during the income year.
- 3.7 If this trust is a specified livestock owner, details of livestock valuation methods, valuations, and calculations for tax purposes.

Items from prescribed forms

- 3.8 All relevant amounts from the trust's financial statements that must be disclosed in any forms prescribed by the Commissioner of Inland Revenue under section 35 of the Tax Administration Act 1994.
- 3.9 Sufficient notes to support amounts required to be disclosed as an exceptional item on any form prescribed by the Commissioner of Inland Revenue under section 35 of the Tax Administration Act 1994.

Associated persons transactions

- 3.10 The information listed for a transaction between the trust and any associated person of the trustee (within the meaning of subpart YB of the Income Tax Act 2007),

unless the transaction is minor and incidental to the activities of the trustee. For each disclosed transaction:

- i. the name of the associated person and a description of the association
- ii. interest expenses incurred by the trustee for any loan made to the trustee by the associated person
- iii. amounts paid by the trustee to the associated person in the nature of loans or other advances
- iv. expenses incurred by the trustee for services provided by the associated person (including wages, salaries, management fees, and payments for other services provided to the trustee)
- v. expenses incurred by the trustee to the associated person for rentals or leases of land or other assets
- vi. expenses incurred by the trustee to the associated person for acquiring or using intangible property, including royalty payments, and
- vii. a reconciliation of movements in trust corpus, trust capital and loans or current accounts to, and from, the beneficiaries or other persons with powers of appointment of the trust and associated persons of the trust.

Example

A trust would show in its financial statements:

- The amounts from the IR10 *Financial statements summary* form issued by the Commissioner, which generally applies to trusts with business income.
- The amounts the Commissioner will prescribe for all trusts subject to the section 59BA provisions (if they are not already provided in an IR10 form).

At the time of preparing the issues paper, the proposed amounts are as follows (items not currently recorded in the IR10 form are indicated as being “new”):

- i. Total accounting profit before tax**
- ii. Tax adjustments to reconcile accounting income with assessable income in tax return
- iii. Untaxed realised gains

- iv. Total Assets**
- v. Associated persons financial arrangements (**NEW**)
- vi. Shares/Ownership Interests*
- vii. Land*
- viii. Buildings*

- ix. Total Liabilities**
- x. Associated persons financial arrangements (**NEW**)

- xi. Total Equity**
- xii. Drawings [the nature of this item for trusts will be clarified in the operational statement]
- xiii. Closing current account balances [the nature of this item for trusts will be clarified in the operational statement]

* Trustees will disclose the valuation method adopted for these assets.

Commentary

- 3.11 The information to be shown for reconciliations, particular types of businesses, and associated person transactions are generally consistent with requirements in the minimum standards for financial statements of companies. This will provide consistent reporting across similar types of business structures.
- 3.12 The three main differences between these proposals and the minimum standards for financial statements for companies are:
- i. The proposed new requirement to disclose the name of the associated person/description of the association. This is considered necessary for the associated person information to be better understood.
 - ii. The proposed introduction of a minor and incidental test for associated person disclosures. This will reduce trustee compliance costs.
 - iii. The proposed requirement to disclose the reconciliation of movements of beneficiary accounts. This is consistent with the minimum standard for financial statements of foreign trusts and is relevant to understand beneficiary disclosures provided under section 59BA(2)(d).
- 3.13 For the reference to prescribed forms:
- i. The Commissioner will not require financial statements to be included with the prescribed forms, but they may be requested later.
 - ii. For trustees with business income, financial statements should include all relevant amounts that must be disclosed in the prescribed form IR10 *Financial statements summary*.
 - iii. If the trustee has business and non-business assets and liabilities, the IR10 amounts and the amounts in financial statements from 2021–22 should reflect both business and non-business assets and liabilities.
 - iv. The amounts the Commissioner proposes to prescribe for all trustees subject to the section 59BA provisions (if they are not already provided in an IR10 form) will be subject to consultation in the draft operational statement. They have been provided in this document as an example only. The intention is to align these amounts as closely as possible to a subset of amounts contained in the IR10 form in order to be consistent, minimise compliance costs and avoid duplication.

Questions for submitters

1. Do you have any comment on the specific items proposed to be included in the schedule?
2. Are there associated persons transactions that should be excluded from the minimum requirements for trustees? If so, why?

APPENDIX

Tax Administration Act 1994: Sections 59BA and 59BAB

Section 59BA Annual returns for trusts

- (1) A trustee of a trust who derives assessable income for a tax year must file a return for the tax year of all income derived in the corresponding income year by the trustee as trustee of the trust.
- (2) A trustee who is required to file a return for a tax year under subsection (1) and does not meet the requirements of subsection (3) must make the return in the form prescribed by the Commissioner and include, unless otherwise required by the Commissioner,—
 - (a) a statement of profit or loss and a statement of financial position:
 - (b) the amount, and nature, of each settlement that—
 - (i) is not the provision to the trustee, at less than market value, of minor services incidental to the activities of the trust; and
 - (ii) is made on the trust in the income year:
 - (c) the name, date of birth, jurisdiction of tax residence, and tax file number and taxpayer identification number, of each settlor who makes a settlement on the trust in the income year or whose details have not previously been supplied to the Commissioner:
 - (d) for each distribution made by the trustee of the trust in the income year,—
 - (i) the amount of the distribution:
 - (ii) the name, date of birth, jurisdiction of tax residence, and tax file number and taxpayer identification number, of the beneficiary who receives the distribution:
 - (e) the name, date of birth, jurisdiction of tax residence, and tax file number and taxpayer identification number, of each person having a power under the trust to appoint or dismiss a trustee, to add or remove a beneficiary, or to amend the trust deed:
 - (f) the other information required by the Commissioner.
- (3) A trustee of a trust who is required to file a return for a tax year under subsection (1) is not required to file a return in the form required by subsection (2) if—
 - (a) the trustee is excluded from the requirement to make a return by section 43B (which relates to non-active trusts):

- (b) the trustee is required to make a return by section 59D (which relates to foreign trusts):
 - (c) the trustees of the trust are incorporated as a board under the Charitable Trusts Act 1957:
 - (d) the trust is a charitable trust registered under the Charities Act 2005:
 - (e) the trustee is eligible under section HF 2 of the Income Tax Act 2007 to choose under section HF 11 of that Act to become a Maori authority:
 - (f) the trust is a widely-held superannuation fund, as defined in section YA 1 of the Income Tax Act 2007:
 - (g) the trust is an employee share scheme that is an exempt ESS, as defined in section YA 1 of the Income Tax Act 2007:
 - (h) the trustee is a debt funding special purpose vehicle, as defined in section YA 1 of the Income Tax Act 2007:
 - (i) the trustee is a lines trust established under the Energy Companies Act 1992.
- (4) If the trustee of a trust is a non-resident, a settlor of the trust who is a New Zealand resident is responsible for ensuring the performance of the obligations imposed on the trustee by this section.
- (5) The Commissioner may vary the requirements set out in subsection (2) for a trustee or class of trustees.
- (6) A variation under subsection (5) is secondary legislation (see Part 3 of the Legislation Act 2019 for publication requirements).

Section 59BAB Commissioner may require trust information for period after 2013–14 income year

- (1) The Commissioner may require a trustee of a trust to provide, in the prescribed form and by the specified date, information that—
- (a) relates to the trust and a period beginning after the end of the 2013–14 income year and ending before the beginning of the 2021–22 income year; and
 - (b) would be required to be provided under section 59BA if the period began after the end of the 2020–21 income year; and
 - (c) is in the knowledge, possession, or control of the trustee.
- (2) The Commissioner may issue a notice requiring the trustee of each trust having the characteristics specified in the notice to provide, in the prescribed form and by the specified date, information—

- (a) that is described in subsection (1) and is specified in the notice; and
 - (b) is for each period that is specified in the notice and begins after the end of the 2013–14 income year and ends before the beginning of the 2021–22 income year.
- (3) If the trustee of a trust is a non-resident, a settlor of the trust who is a New Zealand resident is responsible for ensuring the performance of the obligations imposed on the trustee by this section.
- (4) A notice under subsection (2) is secondary legislation under the Legislation Act 2019.