POLICY AND REGULATORY STEWARDSHIP

Tax policy report: **Summary of submissions and recommended changes for the officials' report for the Taxation (Annual Rates for 2022–23, Platform Economy, and Remedial Matters) Bill (No 2): policy items**

Date:	5 December 2022	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2022/542

Action sought

	Action sought	**Deadline**
Minister of Finance	**Agree** to the recommendations	15 December 2022
Minister of Revenue	**Agree** to the recommendations	15 December 2022

Contact for telephone discussion (if required)

Name	**Position**	**Telephone**
Melissa Siegel	Bill Manager	s 9(2)(a)
Natisha Jones	Policy Advisor	

5 December 2022

Minister of Finance
Minister of Revenue

Summary of submissions and recommended changes for the officials' report for the Taxation (Annual Rates for 2022–23, Platform Economy, and Remedial Matters) Bill (No 2): policy items

Executive summary

1. This report seeks your approval on recommendations to be included in the officials' report to the Finance and Expenditure Committee (FEC) on the Taxation (Annual Rates for 2022–23, Platform Economy and Remedial Matters) Bill (No 2) (the Bill).

2. The Bill is currently being considered by the FEC, and the officials' report is due with the Committee by 20 January 2023.

3. The Bill received approximately 800 written submissions. Oral hearings of evidence commenced on 9 November 2022 and are scheduled to continue on 7 and 19 December 2022.

4. Most of the recommendations in this report are in response to issues raised by submitters. Subject to your approval, we will include these recommendations in the officials' report.

5. In addition to the specific policy and remedial changes outlined in this report, we seek your approval to recommend drafting changes to the Committee where the Bill as introduced does not achieve the policy intent or where the drafting could be improved or clarified.

6. None of these proposed amendments are significant enough to require Cabinet approval.

7. One proposed change, relating to the proposal to exempt public transport from fringe benefit tax, has a fiscal cost

8. None of these changes give rise to any material compliance or administration costs, or any significant systems or technology implications.

9. Treasury has been consulted on this report.

Next steps

10. Subject to your agreement, recommendations outlined in this report will be drafted for inclusion in the officials' report. Subject to the FEC's agreement, these changes would be included in the revision-tracked version of the Bill to be reported back to the House by 2 March 2023.

11. The finalised officials' report is due to the FEC no later than 20 January 2023. We will report to you with a draft version of the officials' report for noting in the week beginning 16 January 2023.

Recommended action

We recommend that you:

Recommendations	Minister of Finance	Minister of Revenue
12. **indicate** in the body of this report where you agree or do not agree with the recommended amendment;	Indicated	Indicated
13. **agree** to minor and technical changes to proposals in the Bill to improve the drafting of provisions or to give effect to the policy intent;	N/A	Agreed/ Not agreed
14. **note** that agreed amendments will be included in the officials' report to the Taxation (Annual Rates for 2022–23, Platform Economy, and Remedial Matters) Bill (No 2);	Noted	Noted
15. **note** that the final version of the officials' report on the Bill will be sent to your office in the week beginning 16 January 2022 and then to the Finance and Expenditure Committee no later than 20 January 2023.	Noted	Noted

s 9(2)(a)

Melissa Siegel
Bill Manager
Inland Revenue

Hon Grant Robertson
Minister of Finance

/ /2022

Hon David Parker
Minister of Revenue

/ /2022

Background

16. The Taxation (Annual Rates for 2022–23, Platform Economy, and Remedial Matters) Bill (No 2) is currently being considered by the Finance and Expenditure Committee ("FEC"). The officials' report on submissions is due to the FEC no later than 20 January 2023 to enable the Committee to report back to the House by 2 March 2023.

17. Written submissions on the Bill closed on 2 November 2022. The first hearing of oral evidence was held on 9 November 2022 and subsequent hearings are scheduled for 7 and 19 December 2022. A submitter's oral submission should align with their written submission, so we do not anticipate new issues to arise at the two remaining hearings. However, if new issues do arise, we will co-ordinate with your offices to seek your approval where appropriate.

18. Approximately 800 written submissions were received. In addition to submissions by stakeholders such as law and accounting firms, most of the submissions relate to either the proposed exemption from FBT for public transport or the GST platform economy proposal.

19. Around 415 submissions were received on the proposed exemption from FBT for public transport which were largely connected to a campaign launched by the Cycling Action Network in early October. Many of these submissions submit that clause 6 of Hon Julie Anne Genter's Income Tax (Clean Transport FBT Exclusions) Amendment Bill should be adopted to exempt bicycles from FBT. The Income Tax (Clean Transport FBT Exclusions) Amendment Bill is a Member's Bill that has not yet been drawn from the ballot.

20. 310 submissions were received on the proposal to apply GST to certain types of services provided on digital platforms. Many of these were from individuals following an email from Airbnb to them encouraging them to submit against the proposal in the Bill. Most of these submitters opposed the proposal for different reasons, including being worried about the compliance costs associated with GST registration (though, we note that under the proposals in the Bill, hosts would not need to register for GST unless they were above the $60,000 registration threshold and this is the status quo) and being concerned about the impact of GST on demand for their accommodation.

21. This report sets out recommended changes that could be included in the officials' report to the FEC.

22. Only one recommended change has a fiscal impact and requires approval by the Minister of Finance and Minister of Revenue. The recommendation relates to the proposed fringe benefit tax exemption for certain public transport fares.

23. None of the other proposed amendments in this report have a fiscal impact and require approval by the Parliamentary Under-Secretary to the Minister of Revenue and endorsement by the Minister of Revenue.

24. We do not consider that the recommended changes in this report require Cabinet approval.

Fringe benefit tax exemption for certain public transport fares

25. The Bill proposes an exemption from fringe benefit tax (FBT) for public transport fares that are subsidised by an employer mainly for the purpose of their employees travelling between their home and place of work. The proposal seeks to produce a more neutral FBT outcome between two modes of transport between home and work:

- by car, with an FBT exemption currently in place for employer-provided on-premises car parks, and
- by more environmentally friendly public transport, which is currently subject to FBT.

26. The proposal received more than 400 submissions, with most relating to a campaign launched by the Cycling Action Network to include bicycles. Overall, submitters supported the proposal to exempt public transport from FBT. However, one submitter pointed out that the proposal added a distortion to the tax system relative to other fringe benefits and another submitted that the proposal would be a move away from the principle that home-to-work travel is a private expense.

27. Some suggested that coverage of the "public transport" exemption should be clarified or extended to include on-demand services, transport covered by the Total Mobility Scheme, and all public transport beyond the home-to-work commute. As noted above, the majority of submitters suggested an FBT exemption for bicycles. Some also suggested additional FBT exemptions to encourage environmentally desirable behaviours, such as electric vehicles (EVs), e-scooters, ridesharing, and bike locks.

28. Several submissions suggested an equivalent exemption for employers reimbursing or paying an allowance towards their employees' public transport fares. These would not be covered by the proposed FBT exemption but would be taxed as salary and wages under PAYE system and therefore subject to income tax.

29. Submitters considered that guidance for employers needs to be published on the boundary between fringe benefits and PAYE payments, particularly in the context of the proposed FBT exemption. We agree with this and will include guidance in the relevant Tax Information Bulletin item on the Bill following enactment.

Proposed changes

30. Based on submissions, we recommend two changes to the FBT exemption proposal:
    - including the Total Mobility Scheme in the proposed exemption, and
    - confirming on-demand services are covered by the proposed exemption.

Total Mobility Scheme (Minister of Finance and Minister of Revenue approval required)

31. The Total Mobility Scheme is a nationwide scheme administered by regional councils and Waka Kotahi to support people who cannot use public transport all or some of the time. Total Mobility customers pay 50% of the cost of travel (for example, by shuttle with a wheelchair hoist) up to a regional cap and any additional cost that is over the regional cap. Their regional council reimburses the transport operator directly for the remaining 50% of the cost.

32. Subject to your agreement, we will recommend that employer-provided fringe benefits for travel between home and work that are part funded by the Total Mobility Scheme should be covered by the proposed FBT exemption. While the original policy intent of the exemption focused on environmental and neutrality concerns, including this situation within the exemption addresses equity concerns. It would ensure that employers are able to provide fringe benefits for transport part funded by the Total Mobility Scheme for employees with impairments without attracting FBT.

33. The impact of the proposed change is hard to quantify. There is no data available on how many Total Mobility card holders are employed and how many Total Mobility

trips are for work purposes (as the purpose of the trip does not need to be specified).

34. The proposed amendment is likely to have a very small fiscal cost. For this reason, we have estimated a nominal revenue loss of approximately $0.2 million a year, with a corresponding impact on the operating balance funded through the Tax Policy Scorecard:

	$m – increase/(decrease)				
Vote Revenue Minister of Revenue	**2022/23**	**2023/24**	**2024/25**	**2025/26**	**2026/27 & outyears**
Crown Revenue and Receipts: Tax Revenue	-	(0.200)	(0.200)	(0.200)	(0.200)

On-demand services

35. On-demand services are increasingly being offered by public transport providers in areas of lower demand. These public transport services are booked and service a set area, rather than having a set timetable and route. Standard public transport fares apply.

36. Based on the current wording of the provision, on-demand services may not be covered by the proposed exemption.

37. We agree with submitters that this service forms part of the public transport network. We recommend clarifying that on-demand services are included in the proposed FBT exemption, where the service is part of a public transport provider's network and is subject to a public transport fare.

Submissions to be declined

Widening the proposed public transport exemption to all transport, not just commuting

38. Some submitters suggested extending the exemption to all public transport, not just commuting, would further encourage environmentally desirable behaviour. However, we think that limiting the exemption to between home and work travel would best achieve the policy objective of improving neutrality in the FBT rules. Widening the proposed exemption would increase distortions and further reduce coherence and neutrality in the tax system.

Additional exemption for bicycles

39. Submitters suggested that bicycles should be exempt from FBT to increase the number of people commuting by bicycle, as this has positive effects on the environment as well as on wellbeing and health.

40. The proposed public transport FBT exemption seeks to achieve a more neutral FBT outcome between travelling to and from work by car and parking in an employer-provided car park (currently FBT exempt) and travelling by the main alternative transport for that commute (i.e., public transport). This is in line with the specific Tax Working Group recommendation.

41. New Zealand's tax system uses a broad-base framework. This means that taxes are applied neutrally with few exemptions and subsidies, which minimises the distortion of economic activity. There is a high threshold to depart from this neutrality approach and there are few exemptions from FBT. Where exemptions are provided, the scope of the exemption is important in managing the potential distortion. The proposed FBT exemption for public transport and the existing FBT exemption for car parks share a similar focus that manages this risk. Both exemptions relate to providing access rather than funding or enabling the purchase of an underlying asset, such as a bicycle or EV.

42. Further FBT exemptions, particularly for underlying assets, would increase the distortion between the taxation of transport benefits and other fringe benefits. This would reduce the overall fairness of the tax system. While many other employer-provided benefits could also provide socially desirable outcomes, introducing additional exemptions would further reduce the coherence and neutrality of the tax system.

43. We therefore do not recommend an FBT exemption for bicycles.

Equivalent income tax exemption for public transport reimbursements and allowances

44. Some submitters were concerned that the application of the proposed FBT exemption will be administratively difficult for employers, resulting in a low usage of the exemption.

45. Submitters considered that it would be more effective to provide an income tax exemption for allowances for, or reimbursements of, public transport costs to encourage environmentally friendly outcomes. Allowances and reimbursements are not covered by the proposed FBT exemption but are subject to income tax through the PAYE system. Submitters emphasised this was important given recent announcements about the new National Ticketing Solution project (to be piloted in Canterbury in 2024 and expanded to other regions by 2026) which would allow for the use of debit or credit cards and other digital payment methods on public transport.

46. The existing neutrality issue the exemption tries to address does not arise in relation to reimbursements and allowances. This is because reimbursements and allowances for both car parks and public transport costs are subject to income tax. Integrity concerns also arise for tax free allowances, which means that there are very few tax-free employer allowances in the income tax rules. Existing tax-free allowances are mostly limited to unusual work circumstances that cause additional costs, such as certain additional transport costs when there is no adequate public transport for the place of work, or short out-of-town secondments and conferences.

47. We have talked to some large public transport providers that are in the process of developing products that may address some of the administrative difficulties of providing these fringe benefits. They also stated that, while the national ticketing solution is in the initial stages of development, they understand that specific public transport ticketing solutions will be available alongside the ability to use debit, credit cards and other digital payment methods.

48. We do not recommend an equivalent income tax exemption for allowance or reimbursements relating to public transport costs.

Recommendations

Agree to include Total Mobility Scheme fringe benefits for between home and work travel in the proposed exemption for public transport from fringe benefit tax.

Agreed/Not agreed Agreed/Not agreed

Note the following changes to tax revenue as a result of the policy decision above, with a corresponding impact on the operating balanced and net debt:

	$m – increase/(decrease)				
Vote Revenue Minister of Revenue	**2022/23**	**2023/24**	**2024/25**	**2025/26**	**2026/27 & outyears**
Crown Revenue and Receipts: Tax Revenue	-	(0.200)	(0.200)	(0.200)	(0.200)

Noted Noted

Agree that the fiscal implications resulting from this change will be managed through the Tax Policy Scorecard.

Agreed/Not agreed Agreed/Not agreed

Agree to clarify that on-demand public transport services are covered by the proposed FBT exemption, where it is part of the public transport provider's network and charges a public transport fare.

Agreed/Not agreed Agreed/Not agreed

Agree that there should be no FBT exemption for bicycles.

Agreed/Not agreed Agreed/Not agreed

Agree that no equivalent income tax exemption should be proposed for employer reimbursements and allowances towards their employees' public transport costs.

Agreed/Not agreed Agreed/Not agreed

Platform Economy

49. The Bill contains proposals that would:

- **Implement an information reporting and exchange framework designed by the Organisation for Economic Co-operation and Development (OECD).** The information reported and exchanged would relate to taxpayers' income-earning activities on digital platforms. It is estimated to raise an additional $11 million to $22 million per annum through improved income tax collection arising from Inland Revenue having more information about taxpayers' incomes. This would apply from the 2024 calendar year; and

- **Require digital platforms to collect and return GST on supplies of short-term accommodation, ridesharing, and food and beverage delivery services.** These changes are estimated to raise an additional $47 million per annum in GST revenue. This would apply from 1 April 2024.

50. We have provided the Minister of Revenue's office with a more detailed overview of submissions on the Bill (BN2022/530 refers). Other than the change recommended below, we are not recommending any substantive or material changes to the Bill that would require Ministerial or Cabinet approval. The other changes we intend to recommend in the officials' report will be of a technical and minor nature, focused on detailed aspects of the proposals and ensuring there is sufficient clarity and guidance available within the rules.[1]

Proposed changes: recent developments at the OECD on the reporting rules

51. At the November 2022 OECD meeting, the digital platform information reporting requirements were discussed. At that meeting, the European Commission provided an update on the interaction between their rules (DAC7, which applies to digital platforms based in Europe) and the OECD's reporting rules.

52. The European Commission confirmed that European jurisdictions would be able to exchange information with jurisdictions outside of Europe that had "partial equivalence" with DAC7. This means that New Zealand could receive information from tax authorities in Europe on income earned by New Zealand taxpayers through European-based digital platforms in relation to accommodation and personal services.

53. This also means we would no longer be required to implement the "full" reporting rules that would require digital platforms in New Zealand to report to Inland Revenue regarding income earned by non-residents operating through New Zealand platforms from the sale of goods and vehicle rentals. The downsides to not implementing the "full" reporting rules are still being considered in consultation with affected New Zealand digital platforms, but these include:

    - New Zealand not receiving information from foreign tax authorities about income earned by New Zealand tax residents from the sale of goods and vehicle rentals facilitated by foreign digital platforms; and
    - New Zealand-based digital platforms would have to report to foreign tax authorities in respect of income earned by non-residents in relation to the sale of goods and vehicle rentals (as opposed to New Zealand digital platforms instead reporting only to Inland Revenue, which would then share information with foreign tax authorities). It is possible that digital platforms would prefer to report this information to Inland Revenue for exchange purposes as it means they do not need to navigate foreign laws and processes. This is something we are exploring with them.

54. Since these implications are still being worked through, subject to your agreement, we intend to recommend to the FEC that the extended reporting rules (which covers the sale of goods and vehicle rentals) be brought into force by Order in Council at some point within the next three years (otherwise, the extended reporting rules would not be given legislative effect in New Zealand). This provides the Government with an opportunity to implement the rules if it is considered desirable, but also provides sufficient time for us to work with New Zealand-based digital platforms to determine the implications of the sale of goods reporting requirements and their preferences.

[1] For example, some submitters sought additional guidance and clarity on aspects of the reporting rules and the GST proposals through further legislative amendments (for example, including definitions within the Bill instead of leaving it to supplementary guidance).

55. This decision does not have financial implications because the original decision to implement the OECD's extended reporting rules covering the sale of goods and vehicle rentals did not affect the estimated additional revenue. The $11 million to $22 million of additional revenue was based on income earned from accommodation rental and personal services only.

Submissions to be declined

Implementation should be delayed

56. Submitters considered that both proposals should be delayed providing more time for affected digital platforms to consider and implement the required changes.

57. We note that the OECD's information reporting and exchange framework is being implemented in Canada and the United Kingdom on the same timeline as is proposed for New Zealand, and in Europe from 2023. The proposed GST changes would also come into force 12 months following the expected enactment of the Bill, which is what digital platforms signalled was sufficient development time for changes of this scale. For these reasons, we do not recommend deferring implementation of either change proposed in the Bill.

    Submitters also said that the proposals should not be implemented in New Zealand until there was clearer evidence that this was direction being headed in by other jurisdictions.

58. We do not agree with these submissions. The information reporting and exchange framework is being implemented by approximately two-thirds of OECD members on a faster, or comparable, timeframe as is proposed in New Zealand. We consider there are strong arguments for implementing the GST changes, and do not agree that there are benefits in waiting to see what other jurisdictions decide to do in this area.

Scope of the rules

59. A common concern raised by submitters is that under the reporting rules, New Zealand digital platforms would be required to report to Inland Revenue by 31 January in relation to the preceding calendar year. Submitters have suggested this date be deferred because staff will be on annual leave.

60. While we understand submitters' concerns, the due date for this information is driven by the desire of foreign tax authorities to use the information from the exchange for pre-populating tax returns of their tax residents. Under the rules, Inland Revenue would need to share information with foreign tax authorities by the end of February. We are therefore unable to shift the 31 January platform to Inland Revenue reporting date of without compromising Inland Revenue's ability to fulfil New Zealand's obligations under the OECD's rules.

61. We do, however, intend to work with affected digital platforms to provide them with additional time where practical. We also note that, as the OECD's rules require information to be broken down into quarterly periods, 75% of the information could be collated well in advance of the 31 January reporting date. This means that digital platforms with a reporting obligation would only need to verify information for the last quarter of the calendar year before reporting by 31 January.

Recommendations	
Agree that the application date for implementation of the OECD's information reporting and exchange framework for accommodation rental and personal services remains 1 January 2024.	
Agreed/Not agreed	Agreed/Not agreed
Agree that the application date for the GST changes requiring digital platforms to collect GST on short-term rental accommodation, ridesharing, and food and beverage delivery services remains 1 April 2024.	
Agreed/Not agreed	Agreed/Not agreed
Note that deferring the implementation date of either of these proposals would have a fiscal cost equal to the estimated additional revenue which would be foregone.	
Noted	Noted
Agree to defer implementation of the OECD's extended reporting rules (covering the sale of goods and vehicle rentals) until such time that an Order in Council, made on recommendation of the Minister of Revenue, brings them into force.	
Agreed/Not agreed	Agreed/Not agreed
If you agree to the recommendation above, **agree** that the extended reporting rules would not be given legislative effect in New Zealand unless brought into force by Order in Council within three years following enactment of the Bill.	
Agreed/Not agreed	Agreed/Not agreed

Cross-border workers

62. The Bill contains proposals which seek to clarify and modernise the administrative aspects of the rules applying to cross-border workers and to reduce the cost of complying with New Zealand's pay as you earn (PAYE), fringe benefit tax (FBT) and employer's superannuation contribution tax (ESCT) and non-resident contractor tax (NRCT) rules.

63. Submitters broadly welcomed reform to the tax settings that apply to employers of cross-border employees and payers of NRCT. Submitters made helpful suggestions to improve the implementation of the policies.

64. Some submitters felt that the proposals could have gone further. One common concern raised by submitters relates to practical difficulties in obtaining an IRD number. These submitters felt that legislative change was required to simplify the process for cross-border workers and non-resident employers. We acknowledge this concern but changes to IRD number requirements are out of scope of the current project and would be better addressed through operational change or as part of wider reforms.

Proposed changes

65. Two proposals attracted widespread comment:

- the proposal to introduce an NRCT reporting requirement, and
- the proposal to transfer FBT and ESCT obligations to an employee where the employer does not have a sufficient presence in New Zealand to be subject to New Zealand employment-related tax obligations.

NRCT reporting and the "single payer" view

66. The rationale behind the proposed reporting requirement is that it would support the proposed simplification of the NRCT withholding thresholds (the "single payer" view). Submitters were concerned that the information required was broad and likely to require manual intervention to prepare and submit reports. Further, the information requirements were out of balance to the purpose of supporting the proposed NRCT reforms or the cost of compliance.

67. Subject to your agreement, we intend to recommend in the officials' report that proposals relating to the "single payer" view of the NRCT withholding thresholds and NRCT reporting be removed from the Bill. We consider that these proposals require further consideration and consultation before reintroduction in a future tax bill.

68. This change does not have a fiscal impact because it would be a postponement of an administrative measure that does not have a fiscal impact.

Transfer of FBT and ESCT obligations to an employee

69. Submitters were concerned that FBT and ESCT are ordinarily paid by employers and the transfer of these obligations to the employee may cause the employee cashflow difficulties. In addition, the calculation of these taxes requires information that may not be readily available to the employee.

70. Conversations with submitters indicate that the most common fringe benefits received by remote employees are employer contributions to foreign superannuation schemes and the payment of insurance premiums. One submitter had seen company vehicles used by remote employees.

71. Subject to your agreement, we will recommend that a de minimis for fringe benefits be introduced for employees managing their employment-related tax obligations. We propose that the de minimis be set at $2,500 per income year. Domestic employers are entitled to a de minimis threshold of $1,200 per income year per employee for unclassified benefits (subject to conditions). The higher proposed de minimis for remote employees recognises that, in these limited circumstances, the employee bears the tax cost and compliance burden.

72. This means that an employee would not be required to report or pay tax on fringe benefits if their total taxable benefits per income year was $2,500 or less. Where fringe benefits provided exceed this amount, the benefits would be taxed in full.

73. We consider that this FBT change has no fiscal impact as the original fiscal impact was small and unquantifiable. As such, it falls within the costing of the original proposal.

74. We do not recommend a similar de minimis for employer contributions to foreign superannuation schemes. Employer contributions to foreign superannuation schemes may be a valuable element of an employee's total remuneration. A meaningful ESCT de minimis for remote workers would not be possible without creating a significant gap between the treatment of non-resident employers (who do not have a sufficient presence in New Zealand) and their employees, and New Zealand employers and employees.

Drafting clarifications

75. We will recommend a clarification to ensure any tax due on fringe benefits is paid via PAYE at the employee's marginal tax rate. This is necessary for the payment of the tax to be processed correctly by Inland Revenue's systems. This will result in a small under-taxation of the benefit compared to the employer paying FBT. FBT is paid at a grossed-up tax rate (63.93% for an individual on the top income tax rate of 39%), but the employer can claim the tax paid as a deduction from its own income. This reduces the tax paid from the headline rate to an effective rate that is close to but lower than the employee's marginal tax rate. Inland Revenue will monitor taxpayer behaviour and may recommend further policy changes if taxpayers begin to exploit this difference.

76. We will also recommend a further drafting clarification to reflect that the employer superannuation contributions to foreign schemes should be subject to ESCT. ESCT enables the contribution to be excluded income for certain purposes, such as entitlement to Working for Families. Under existing rules, an employer and employee may, in some circumstances, opt out of ESCT and choose taxation under PAYE instead. This option will be preserved as it enables employers and employees to agree the appropriate treatment for their circumstances.

77. There are no fiscals associated with these clarifications because the original fiscal impact was small and unquantifiable. As such, it falls within the costing of the original proposal.

Submissions to be declined

Commencement date

78. Submitters considered that all proposals which apply to employers and cross-border employees should have a consistent application date of 1 April 2023.

79. The proposals to address PAYE, FBT and ESCT integrity measures would apply from 1 April 2023. The later application date for other proposals allows time for the development of systems and guidance by Inland Revenue for employers and tax advisors. We consider that having different commencement dates for different proposals remains appropriate.

Shadow payroll rule

80. The existing shadow payroll rule applies where an employee works in New Zealand but remains on the employer's payroll system in a different jurisdiction. The rule treats the income as being derived 20 days after payment to ensure that employers of cross-border workers have sufficient time to collate and report information to Inland Revenue. The Bill proposes to rationalise the legislation by relocating the shadow payroll rule to a new section for cross-border employees.

81. Submitters suggested that the current shadow payroll rule should be changed from a deeming rule to a rule which better aligns with the employee's actual payment date.

82. From a policy perspective, we do not oppose the submission, but it is outside the scope of the current Bill and would require significant systems changes. This would require further work and would be better suited for a future tax bill.

Annual PAYE arrangement

83. Two submitters did not support an annual payment basis for PAYE in special circumstances because of the risk of non-compliance.

84. We do not consider non-compliance to be a material risk. Employers who engage with Inland Revenue (which is required to access the annual payment basis) are more likely to be seeking to lower their compliance burden than to avoid their tax obligations.

Payroll subsidies

85. Two submitters thought that the Government should reinstate payroll subsidies considering the proposals to transfer FBT and ESCT obligations to an employee who manages their own employment taxes.

86. We do not recommend the reintroduction of payroll subsidies. We do not provide them for other taxpayers, and we do not consider it appropriate to make an exception for cross border workers as it would undermine the coherence of the tax system.

Longer period for retroactive NRCT exemptions

87. The Bill proposes a period of 92 days for retroactive NRCT exemptions. We do not support extending this period as this may reduce the incentive to apply for an exemption or conflate the exemption with a reclaim of overpaid tax via a tax return. We think that 92 days is sufficient to enable a contractor to obtain an exemption on a timely basis which covers the relevant contract payments.

Exemption from NRCT withholding for GST-registered persons

88. GST-registered non-resident contractors are already able to obtain an NRCT withholding exemption. Exemptions are available based on a good compliance history. GST registration is only part of that picture. Further, GST registration is not indicative of tax residence or presence in New Zealand. They may be registered for GST to claim input tax. This does not signify the kind of connection with the New Zealand tax system required to reduce the integrity risk which NRCT seeks to address.

Recommendations

Agree to remove the "single payer" view and the non-resident contractor's tax reporting requirement from the current Bill for further consultation.

Agreed/Not agreed　　　　　　　　Agreed/Not agreed

Agree to include a $2,500 de minimis where an employee is responsible for paying fringe benefit tax.

Agreed/Not agreed　　　　　　　　Agreed/Not agreed

Agree to Inland Revenue officials informing affected submitters of these changes to minimise impacts on stakeholders' systems and processes.

Agreed/Not agreed　　　　　　　　Agreed/Not agreed

GST apportionment and adjustment rules

89. The Bill proposes a package of changes to the GST apportionment and adjustment rules to reduce the compliance costs they impose on businesses and better align them with current taxpayer practices. These changes include:

    - introducing a principal purpose test for goods and services acquired for $10,000 or less (GST exclusive) that would allow a registered person to claim a full GST input tax deduction for taxable use instead of applying the apportionment rules, and
    - allowing GST-registered persons to elect to treat certain assets that have mainly private or exempt use, such as dwellings, as if they only had private or exempt use.

90. Submissions supported the GST apportionment proposals and suggested some small changes to make the proposals easier for the affected taxpayers to comply with.

Proposed changes

91. We intend to recommend that the FEC accept most, but not all, of the changes suggested by submitters. The main submissions we agree with are described below. None of these submissions would have a fiscal cost as they either provide the affected taxpayers with the same GST outcome as the existing proposal in the Bill or allow them to continue with their current tax practices which are in the revenue baselines.

92. Other suggested changes that we do not support were because they would undermine the policy intent, may not be effective at reducing overall compliance costs, or could have a fiscal cost.

Principal purpose test: optionality for GST registered persons

93. Deloitte and PwC submitted that the proposed principal purpose test for goods and services acquired for $10,000 or less should be optional for GST-registered persons. We agree that this could reduce compliance costs for some businesses, as it would mean they would not need to apply a different method for goods or services depending on whether they were acquired for $10,000 or less. However, as most businesses will face lower compliance costs under the proposed principal purpose test, we expect that few businesses would be likely to opt out in practice. To prevent "cherry picking," we recommend that the registered person (or GST group if relevant) would be required to "opt out" of applying the principal purpose test for all goods or services they acquire for $10,000 or less for a minimum period such as 24 months.

Private use election: change from exempt to non-taxable supplies

94. The Bill proposes some new rules which would allow GST-registered persons to elect to treat certain assets that have mainly private or exempt use, such as dwellings, as if they only had private or exempt use. The current Bill provisions would achieve this by making the sale of these assets an exempt supply. Chartered Accountants Australia and New Zealand submitted it would be better to make the sale of the assets a non-taxable supply.

95. We agree this would be more intuitive (as goods used for private purposes are generally non-taxable supplies) and could prevent some unintended complexity (as other rules can apply when a person makes exempt supplies).

Use of agreed apportionment methods

96. The Goods and Services Act 1985 (GST Act) allows registered persons or industry associations to apply to the Commissioner to agree an apportionment method as an alternative to applying the general apportionment rules. The scope of these alternative methods is being widened in the Bill. Deloitte submitted that registered persons should be able to adopt an alternative apportionment method that Inland Revenue have published (if it is appropriate for the registered person's situation).

97. We agree that providing an ability for the Commissioner to publish acceptable methods could reduce compliance costs as the affected persons would not have to develop and agree their own bespoke methods with the Commissioner.

98. We also agree with a submission from KPMG that businesses that are members of an industry association which has agreed an alternative apportionment method with Inland Revenue should be able to choose whether they either apply the method agreed by the industry association or the general apportionment rules.

Recommendations

Agree that the proposed principal purpose test for goods and services acquired for $10,000 or less should be optional for GST-registered persons to use.

Agreed/Not agreed Agreed/Not agreed

Agree that the proposal to allow GST-registered persons to treat certain assets that have mainly private or exempt use as an exempt supply when sold, should be amended to make the sale of these assets a non-taxable supply instead.

Agreed/Not agreed Agreed/Not agreed

Agree to expand the existing ability whereby registered persons or industry associations can apply to the Commissioner to agree an apportionment method, so the Commissioner can also publish acceptable methods that the relevant registered persons can then choose to use.

Agreed/Not agreed Agreed/Not agreed

Agree that businesses that are members of an industry association which has agreed an alternative apportionment method with Inland Revenue should be able to choose whether they either apply the method agreed by the industry association or the general apportionment rules.

Agreed/Not agreed Agreed/Not agreed

Build-to-rent exclusion from interest limitation

99. The Bill proposes to exempt large-scale "build-to-rent" assets from the interest limitation rules for residential investment properties in perpetuity. The Bill defines this new asset class as 20 or more dwellings in a single development. Tenants must also be offered a 10-year tenancy under the Residential Tenancies Act 1986 (RTA) with the ability for the tenant to exit the lease with 56 days' notice and personalisation policies that set out the alterations a tenant can make under the RTA.

100. Feedback on the build-to-rent exclusion has generally supported the introduction of a defined asset class and in-perpetuity exclusion from the interest limitation rules for build-to-rent developments. Submitters who did not favour the policy were concerned that it was unfair to give tax breaks to large wealthy investors, and not to small-scale developers or landlords who were still increasing housing supply.

101. Submitters requested clarification on some aspects of the policy, for example, what the term ‘contiguous land’ covered, what was required in a personalisation policy, and whether the term ‘single ownership’ allowed for business structures such as joint ventures and limited partnerships.

102. In addition to the proposed changes outlined below, Te Tūāpapa Kura Kāinga has reported separately to the Minister of Housing regarding an issue with the RTA. The RTA does not explicitly permit landlords to offer fixed term tenancies that can be terminated with 56 days’ notice. An amendment to the RTA is required to ensure the build-to-rent exclusion operates as intended. Subject to the Minister of Housing’s agreement, this will be raised as a matter raised by officials in the officials’ report. A copy of that report will be referred to the Minister of Revenue.

Proposed changes

Information sharing between Inland Revenue and Te Tūāpapa Kura Kāinga

103. A register of assets is required to be set up and maintained by Te Tūāpapa Kura Kāinga to enable Inland Revenue to correctly apply the exclusion to eligible taxpayers. Setting up and maintaining the register requires taxpayer information to be shared between Te Tūāpapa Kura Kāinga and Inland Revenue. This would include:

- a reactive information share where Inland Revenue requests information from Te Tūāpapa Kura Kāinga for auditing purposes, and
- a proactive information share from Inland Revenue to inform Te Tūāpapa Kura Kāinga that an asset no longer meets the build-to-rent requirements and should be removed from the register.

104. Information would only be shared if it is necessary for the administration of the build-to-rent exclusion from interest limitation.

105. We recommend inserting a disclosure provision into the Tax Administration Act 1994 to allow Inland Revenue to share the necessary information with Te Tūāpapa Kura Kāinga. This provision would apply from 1 April 2023.

106. The proposed change has no impact on the costing of the policy as it simply allows for the sharing of information between Inland Revenue and Tūāpapa Kura Kāinga.

Other minor changes

107. Following submissions on the Bill, we will recommend to the FEC minor technical amendments to ensure the language better reflects the original intent of the policy. For example, some submitters raised the concern that the term ‘contiguous land’ applied too narrowly and would bar certain build-to-rent configurations (such as mixed tenure developments that also contain owner-occupied dwellings) from qualifying. We agree that the term ‘contiguous land’ is not consistent with the policy intent and recommend that a project-based requirement should be used instead.

Submissions to be declined

No 20-unit dwelling requirement

108. Several submitters considered that the proposed exclusion should be available to anyone increasing housing supply and the requirement for the development to consist of at least 20 dwellings should be removed.

109. We do not agree with this submission as the intent of the proposal to encourage the development of new housing supply at scale. The minimum requirement was chosen to reflect both the international standards for build-to-rent, and the New Zealand context. Small-scale investors who contribute to new housing supply already benefit from the 20-year new build exemption from interest limitation, and the five-year new build bright-line test.

Application of 20-dwelling requirement to all properties owned by a person

110. Other submitters considered that the 20-dwelling requirement should not be restricted to properties in one location. Instead, submitters suggested that as long as the person owns at least 20 properties in any location, the requirement should be satisfied.

111. The exemption targets build-to-rent accommodation which is a specific model of housing that delivers quality rental housing at pace and scale in a given location, rather than having a wider application to accommodation generally. Build-to-rent also provides tenant benefits that are associated with the configuration of the development including professional asset and tenancy management, shared amenities and increased sense of community generated by medium-high density housing.

112. We do not consider it appropriate to extend the proposed exemption to a landlord who simply owns 20 dwellings around New Zealand as it would not be in line with the goal of build-to-rent to provide cohesively managed developments that encourage a sense of community.

Removal of the requirement to offer personalisation policies

113. Submitters consider that the requirement to offer personalisation policies should be removed because the protections are already afforded under the RTA, and it would create confusion and lead disputes between tenants and landlords. Many submitters were also unclear on what a personalisation policy had to allow, and whether they could require a tenant to rectify or "make good" any alterations at the end of the tenancy.

114. The requirement for landlords to offer personalisation policies to tenants is intended to ensure that tenants are aware of their right to make certain alterations as set out under the RTA. This will likely mitigate the likelihood of disputes between landlords and tenants.

115. The level of personalisation set out in the policy can, but does not have to, go beyond what is already afforded under the RTA. It does not prohibit the use of "make good" penalties. We will propose minor drafting changes to clarify these points.

Removal of "same person" requirement

116. Some submitters considered the requirement that the development be owned by a single owner should be removed as it is not necessary given the other build-to-rent requirements (such as the requirement for 20 dwellings to be on contiguous land).

117. This requirement ensures that assets accessing the build-to-rent exclusion are cohesive developments.

118. Some submitters were also concerned that the current drafting would exclude joint ventures and limited partnerships. The term is not intended to exclude joint ventures or limited partnerships.

Use of other policy tools to encourage build-to-rent developments

119. Submitters in the build-to-rent industry suggested that other policy tools should be used to encourage build-to-rent developments. Examples included the reinstatement of depreciation deductions, an exclusion from the bright-lines rules, or changes to the Overseas Investment Act 2005.

120. We recommend these submissions be declined for reason of being outside the scope of the Bill.

Recommendations

Agree to amend the Tax Administration Act 1994 to allow Inland Revenue to share build-to-rent provider information with Te Tūāpapa Kura Kāinga.

Agreed/Not agreed Agreed/Not agreed

Dual-resident companies *(Minister of Revenue only)*

121. The recommendations in this section do not require approval by the Minister of Finance.

122. The Bill contains proposals that:

- Amend the loss grouping, consolidation, and imputation credit account (ICA) rules to ensure New Zealand resident companies can continue to access certain beneficial tax regimes that are not ordinarily available to dual-resident companies, and

- Amend the domestic dividend exemption and corporate migration rules to ensure companies within a wholly-owned group can no longer shift income out of New Zealand without the anticipated New Zealand income tax by changing their tax residence and obtaining relief from taxation under a double tax agreement (DTA).

123. Submitters welcomed the amendments to the loss grouping, consolidation, and ICA rules. Several submitters suggested the ICA amendments should be extended beyond Australia. However, this would be a significant change to the overall imputation credit regime and would require substantial further policy analysis.

124. Submitters raised several concerns with the integrity proposals, mainly focused on the risk of overreach of the rules for taxpayers that may inadvertently change their residence under a DTA but continue to pay tax as if they were New Zealand DTA resident. Submitters suggested changes that would reduce the risk of overreach and compliance costs, while still ensuring that aggressive tax planning arrangements are prevented.

Proposed changes

125. Both the dividend integrity and corporate migration integrity proposals received extensive comments from submitters.

126. Submitters were concerned that the dividend integrity proposal would impose additional compliance costs. The proposal may result in companies conducting tax residence checks when a dividend is paid between members of the same wholly-owned group to determine whether the recipient is potentially a dual-resident company. Where a dividend has not been on-paid by a dual-resident company to a non-resident, and where New Zealand has not lost its taxing rights or non-resident withholding tax (NRWT) has been assessed, then these dividends should not be subject to the proposed dividend integrity rules.

127. Submitters were also concerned that the corporate migration proposals will impose significant risk on some companies inadvertently falling into the integrity rules. This would result in the company being liable for income tax based on a deemed liquidation. This would be the case even where the company has not deliberately sought to undermine the integrity of the New Zealand tax base. For many companies, this tax liability may be significant. Consequently, in response to this risk, many companies would incur additional compliance costs, including making permanent changes to their corporate structure (for example, using a branch structure).

128. In response to these concerns, we propose several changes to the proposals. The proposed changes would have the same application date as the underlying integrity proposals (30 August 2022). There is no change to the fiscal costing associated with the recommended changes to the proposals. This is because the initial fiscal costing had a nominal annual benefit (about $200k per annum) and the recommended changes would still capture the arrangements that give rise to integrity concerns.

Dividend integrity

Exclusion of dividends paid to companies that are dual resident in Australia and New Zealand

129. We recommend the dividend integrity rules should exclude dividends paid to companies that are dual resident in Australia and New Zealand. We believe this will reduce the compliance costs for many companies, while ensuring the integrity rules achieve their intended purpose. This is because New Zealand retains its taxing rights under the Australia/New Zealand DTA on New Zealand sourced dividends paid by dual resident companies whose residence tie-breaks to Australia, so the risk to the New Zealand tax base is minimal.

On-payment of fully-imputed dividends

130. Where a dividend has been on-paid by a DTA non-resident company to a non-resident company, to the extent the dividend is fully imputed (that is, imputation credits attached to the dividend), it does not pose any integrity risk because company income tax has been paid. We recommend that fully-imputed dividends paid by a DTA non-resident company should be excluded from the proposed integrity rules.

Retrospective imputation credit attachment

131. Under the existing proposal, dividends paid to a DTA non-resident company that are fully imputed are excluded from the proposed dividend integrity rules. This is because New Zealand income tax has effectively already been paid on this income at the company level. There is a concern that some companies may pay an unimputed dividend believing they are a New Zealand resident company, whereas it is later found the taxpayer was actually DTA non-resident and the dividend is subject to NRWT.

132. In this situation, we recommend that the company should be able to retrospectively impute the dividend, provided sufficient imputation credits were available at the time the dividend was paid. There is legislative precedent for allowing retrospective attachment of imputation credits.

Reinstatement of New Zealand residence where dividends have not been on paid

133. The proposed changes allow for the NRWT liability to be eliminated if the dividend recipient is treated as New Zealand resident under the relevant DTA within a two-year period of the dividend payment, assuming the recipient has not paid a dividend to its shareholders. However, if the recipient has only on-paid a portion of the dividend it received and then becomes resident in New Zealand under the DTA, New Zealand would have taxing rights on any future dividend payments by the company.

134. For this reason, we suggest a change to the proposals so that that NRWT is only imposed on the payer to the extent the DTA non-resident company pays a dividend while it is DTA non-resident.

Corporate migration

Limit application of corporate migration integrity rules

135. Several submitters have suggested that the scope of the integrity rules should be narrowed so they only apply in circumstances where the company is aware they are

DTA non-resident. Based on these submissions, we recommend that the integrity rules should apply at the earlier of either:

- The company files a return claiming relief under a DTA on the basis it is DTA non-resident; and
- Two years after the company has received a competent authority determination it is DTA non-resident, and it has not reverted their tax residence back to New Zealand for the purposes of the relevant DTA.

136. While this approach would be a substantial shift away from what is currently proposed, we believe there is merit in the approach suggested by submitters. It would ensure that significant consequences from the corporate migration rules will not apply to inadvertent residence changes but integrity risks will still be addressed.

Retrospective attachment of imputation credits to deemed dividends

137. Any tax resulting under the proposed rules from a DTA residence migration should be the same as under the current domestic law for a formal corporate residence migration. We believe a taxpayer should be able to retrospectively attach imputation credits against a deemed dividend arising from the application of the proposed DTA corporate migration rules, provided imputation credits were available at the time the dividend was paid. The existing corporate migration rules already allow for retrospective imputation credit attachment, so this would be an extension of that approach.

Submissions to be declined

Extension of imputation credit changes beyond Australia

138. Some submitters suggested that the ICA changes should be extended beyond Australia. The rationale for the ICA changes being limited to Australia is because Australian-resident companies can already elect to maintain an ICA (known as an Australian ICA company). The proposed amendments allow a New Zealand resident company to automatically carry over its accumulated imputation credits at the point of becoming Australian tax resident, rather than having to make an election. This will prevent the forfeiture of a company's ICA balance if it inadvertently becomes Australian tax resident and has not made an election to be an Australian ICA company.

139. Our view is that expanding the imputation credit regime beyond what was proposed would be a significant change to the overall imputation credit regime and would require substantial further policy analysis.

Income tax treatment of dual-resident look-through companies

140. One stakeholder was concerned that the existing criteria for New Zealand look-through companies excludes dual-resident companies – including New Zealand companies that have inadvertently become dual resident in Australia. This submission is out of the scope of the proposals in the Bill.

141. Our view is that the issue will be resolved if, as expected, Australia enacts legislation with retrospective effect to revert to the prior corporate tax residence interpretation. If Australia does not achieve this, then we will consider whether the criteria for look-through companies requires amendment.

Two-year grace period for the dividend integrity proposal

142. The proposed two-year grace period provides time for the company to undertake due diligence to determine its tax residence if there is some doubt about the tax residence of the dividend recipient. Submitters suggested a number of changes to the two-year grace period for the dividend integrity proposals, including that the Commissioner of Inland Revenue should have the discretion to extend the period, that the period should begin following a competent authority residence decision (rather than the payment of the dividend), and that the integrity rule should only apply if the dividend is then on-paid within two years following a competent authority residence decision.

143. We do not agree with these submissions.

144. Given the company will be aware of relevant dividend transaction and has control when the dividend will be paid, we do not consider it necessary to extend the period.

145. We believe the two-year period should commence at the time the dividend is paid, which is a clear transaction at which time an assessment can made of the tax residence of the recipient company. There is no guarantee the payer of the dividend will subsequently be informed that the recipient is DTA non-resident, especially if the respective companies are no longer commonly owned. In most circumstances, the recipient company will have up to two years to revert to New Zealand tax residence under a DTA before the integrity rules will apply and NRWT must be paid.

146. Providing a two-year period to change a company's residence only after a competent authority residence determination has been provided would significantly increase the period from which the dividend is paid to any potential NRWT liability is due. This is undesirable and would give rise to additional risks (e.g., that the payer may not be informed of the residence determination, the payer may no longer have the capacity to meet the NRWT obligation).

Recommendations *(Minister of Revenue only)*

Agree to amend the dividend exemption integrity proposal by excluding dividends paid to companies that are dual resident in Australia and New Zealand.

Agreed/Not agreed

Agree to allow imputation credits to be retrospectively attached to dividends where the proposed changes to the domestic dividend exemption or corporate migration rules apply.

Agreed/Not agreed

Agree that where a recipient of dividends reinstates its New Zealand residence under the relevant DTA within the two-year grace period, the dividend integrity proposal should apply only to the extent of the amount of non-fully imputed dividends paid by that company while it was DTA non-resident.

Agreed/Not agreed

Agree to amend the corporate migration integrity proposals so they only apply at the earlier of a DTA non-resident company claiming tax relief under a DTA in a return, or once two years have passed since the company received a competent authority determination that it is DTA non-resident, and it has not become New Zealand resident for the purposes of the relevant DTA.

Agreed/Not agreed

Agree the recommendations above apply from 30 August 2022, in line with the application date for the integrity measures in the Bill.

Agreed/Not agreed

Housing: remedial amendments *(Minister of Revenue only)*

147. The recommendations in this section do not require approval by the Minister of Finance.

148. The Bill proposes remedial amendments to the rollover relief provisions introduced in the previous omnibus bill for the bright-line test and interest limitation rules. Submitters were generally supportive of the proposed amendments, although a few submitters commented that the legislative drafting could be made clearer and suggested refinements.

149. Several commented on the application date (being date of enactment of the Bill) and stated that the amendments should be retrospective to 27 March 2021, with application for the purposes of the bright-line test to transfers occurring on or after 1 April 2022. We note that most of the amendments were intended to apply retrospectively, which the Minister of Revenue agreed to in July 2022 (IR2022/293 refers). We intend to recommend the submissions be accepted except where a specific amendment is intended to apply prospectively because it would be a change in policy.

Proposed changes in response to submissions

150. Based on submissions, we propose the changes below to the rollover relief amendments in the Bill.

151. The changes recommended to the rollover relief and changes in co-ownership provisions do not have any fiscal implications as they are mere clarifications of the policy intent or, in the case of our suggested amendment at paragraph 159, would ensure that an existing proposal in the Bill works as intended.

Permissible charitable beneficiaries

152. Submitters suggested that for discretionary family trusts, the class of permissible charitable beneficiaries should be expanded.

153. At present, permissible charitable beneficiaries are limited to charities registered under the Charities Act 2005. However, most discretionary trusts in New Zealand (many of which are family trusts) have a standard clause in their trust deeds that defines a charitable/non-profit beneficiary class very broadly, beyond entities registered under the Charites Act 2005. As a result, transfers to or from these discretionary trusts are never eligible for rollover relief, which was not intended.

154. We recommend amending the definition of 'close family beneficiary' to include the types of organisations listed in the standard discretionary trust clause.[2]

155. We consider the potential integrity risk to be low as rollover relief does not apply to distributions to beneficiaries. This means that if residential land is transferred to a beneficiary, then the transfer would be subject to the bright-line test if relevant.

156. However, we do recommend inserting a criterion that there is at least one natural person beneficiary (other than the principal settlor, if there is just one principal settlor) who is a close family associate of the principal settlor. This would limit the amendment's scope to discretionary trusts that are family trusts and thus avoid

[2] The standard clause includes within the beneficiary class any association, club, institution, society, organisation or trust not carried on for the private profit of any person whose funds are to be applied wholly or principally to any civic, community, charitable, philanthropic, religious, benevolent or cultural purpose, whether within New Zealand or elsewhere.

making the rules inappropriately broad in their application. We recommend an effective date of 27 March 2021.

Relevant bright-line test settings for recipient

157. Submitters suggested that clarification is needed to ensure that when rollover relief applies to a transfer, the recipient is subject to the same bright-line settings or bright-line test length as the original transferor. Amendments in the Bill would address most of these situations, but there are two examples that submitters have raised that are not currently addressed by the Bill. This includes when inherited property is transferred by a settlor of a family trust to the trust. Inherited property is exempt from the bright-line test, but at present the trustee in this situation would be taxed under the bright-line test on a subsequent transfer of the property if it occurs within 10 years of the date it was inherited by the settlor. An effective date of 27 March 2021 is recommended for this change.

Proposed changes: matters raised by officials

158. The Minister of Revenue previously agreed that the rollover relief provision applying to a transfer of residential property from an eligible family trust to a settlor of the trust should be clarified to ensure that rollover relief applies in the situation where a settlor previously made cash settlements on the trust or guaranteed its obligations to enable it to acquire the property (IR2022/293 refers).

159. Subject to your agreement, we will also recommend further amendments so that the proposed new rule would only apply in limited circumstances when the settlor receiving the property from the trust was not the original owner of the property. This is in line with the purpose of the amendment. If the settlor was the original owner of the property, then the pre-existing rule for transfers to settlors would apply to determine whether the transfer qualifies for rollover relief. We recommend this change apply from the date of enactment.

160. We also propose further drafting changes to clarify the provisions that apply to changes in co-ownership of residential property. While submitters did not submit on the proposed amendments to these provisions, we have had some discussion with stakeholders about remaining errors and ambiguities in these provisions that ought to be fixed. This includes making these changes retrospective to 1 October 2015, the date the original two-year bright-line test applied from.

Submissions to be declined

A rollover relief provision providing for transfers between spouses, civil union, and de facto partners

161. The law provides rollover relief when residential property is transferred on a settlement of relationship property. There is nothing that requires the transaction to occur as part of a separation or relationship breakup, so the law already applies broadly. We do not consider there to be a convincing case for having rollover relief apply in situations where, for example, a person transfers a 50 percent interest in their property to their new partner without there being a formal relationship agreement providing for this.

Look-through companies (LTCs) and partnerships

162. Several submitters commented on the application of the rollover reliefs for LTCs and partnerships. They suggested that rollover relief should be available for:

- transfers of shares in a land-rich LTC from an individual to a family trust,
- transfers of residential property to partners/LTC owners on the dissolution of the partnership or liquidation of the LTC, and
- extending rollover relief to deemed transfers arising on the cessation of an LTC.

163. The intent of the rollover relief rules is to provide rollover relief for the most common and straightforward ownership change scenarios where economic ownership of residential property is unchanged.

164. The rollover relief rules explicitly prevent relief from applying for the transfer of shares in a land-rich LTC to a trust. This provision was added out of concern that providing rollover relief might incentivise holding assets in a trust structure, which could lead to unintended outcomes and raise integrity concerns.

165. The partnership and LTC rules have specific rules concerning the transfer of assets upon the dissolution of the partnership, or liquidation or cessation of an LTC and provide that these are treated as disposals occurring at market value. These rules have wider application than just the bright-line rules and apply to assets other than residential property. As such, there is a clear policy intention for these events to trigger a taxable event with the amount of tax calculated on the market value of the property. The purpose is to ensure there is not a permanent avoidance of tax on partnership or LTC assets held on revenue account.

166. Submitters consider the rollover relief rules should address the issue of latent tax liabilities for dual-resident LTCs that, following a change in interpretation by the Australian Tax Office, have ceased to meet the definition of LTC because they are now treated as not resident in New Zealand for the purposes of the Australia—New Zealand DTA. We note that the previous Australian Government announced in 2020 that remedial changes would be made to Australia’s corporate tax residence test with retrospective application. The problem the submitter has raised would be resolved if the announced changes proceed.

Residential property transfers between mirror trusts or to a newly resettled unified trust

167. Mirror trusts, while not commonly used today, were common in the 1990s and early 2000s. According to the submitter, there are many mirror trusts still in existence. A typical structure was for one spouse to settle a trust with the other spouse and their children as beneficiaries, and for the second spouse to also settle a trust of their own with the first spouse and the children as beneficiaries. The first spouse would not be a beneficiary of their own trust, and likewise, the second spouse would also not be a beneficiary of the trust they settled for the benefit of the first spouse and the children.

168. The issue is that, in their current form, the rollover relief provisions do not apply when a property is transferred from one mirror trust to the other, as may occur when one settlor dies. While we consider there is a case for providing rollover relief in this scenario, given the complexities in drafting a rule that does not give rise to an integrity risk and the amount of time available, we think it would be better to consider this issue further with a view to including any resulting amendment in the next tax bill, rather than make a change to this Bill at the Select Committee stage.

Recommendations *(Minister of Revenue only)*

Agree to expand the class of permissible charitable beneficiaries for a discretionary family trust for the purpose of the rollover relief provisions to include the types of organisations listed in the standard discretionary trust clause.

Agreed/Not agreed

Agree that rollover relief should only apply for a transfer to or from a family trust if there is at least one natural person beneficiary, other than the principal settlor, who is a close family associate of the principal settlor.

Agreed/Not agreed

Agree to remedial changes to ensure that, when rollover relief applies to a transfer of residential property, the recipient is subject to the same bright-line settings or bright-line test length as the transferor in all instances.

Agreed/Not agreed

Agree that the proposal expanding the circumstances in which rollover relief applies to a transfer from a family trust to a settlor should only apply when the settlor receiving the residential property from the trust is not the original owner of the property.

Agreed/Not agreed

Agree to further clarify the legislative provisions applying to changes in co-ownership of residential property.

Agreed/Not agreed