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Tax Alert
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Tax Alert

A focus on topical tax issues – March 2013

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Tax pooling might be worth a thought

By Pippa Watson

In the current economic environment a greater number of companies are finding it more and more difficult to forecast their provisional tax obligations and accurate forecasting is becoming more important as cash flow issues arise. To provide greater flexibility, and to reduce your Inland Revenue (IR) interest costs, tax pooling might be worth a thought.

Tax pooling is used by thousands of New Zealand companies to help manage their provisional tax needs; however there are still many people who have not heard of tax pooling or do not understand how it works.

For those who have not yet utilised tax pooling, we summarise below some of the benefits of tax pooling and what it can do for your business in reducing the stress of meeting your provisional tax obligations, as well as for dealing with increased liabilities resulting from tax audits and voluntary disclosures.

To give you some background, tax pooling is a government approved scheme whereby 'approved intermediaries' operate tax pooling accounts with IR. Instead of making payments directly to their account at IR, taxpayers can deposit their funds into a tax pooling trust account at IR held by trustees. IR approved intermediaries are then able to offset under and overpayments to increase the return on overpayments and reduce Use of Money Interest (UOMI) exposure on underpayments for those taxpayers in the pool. It essentially allows a business to offset any underpayments of provisional tax made with any overpayments within the pool and most importantly, at a more favourable interest rate than IR UOMI rates. Further, tax pooling can assist businesses that are not yet members of the pool, by allowing them to buy tax credits where a company or individual has missed their provisional tax or terminal tax due date; for audit settlements or a voluntary disclosures. Tax credits for other tax types, such as GST, can also be purchased from tax pooling intermediaries, however, certain conditions apply.

"We regularly hear from clients who have underpaid 2012 tax, believing it was going to be another hard year. They now have additional provisional tax and interest to pay" says Chris Cunniffe, CEO of Tax Management NZ. "We are generally able to reduce their IR UOMI cost by up to 30%".

Tax pooling intermediaries provide various services; the main services include pooling, purchasing and financing. The below examples demonstrate each of these.

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Pooling

Growing Fast Limited (GFL) has overpaid its provisional tax by $50,000 at each of its first and second provisional tax dates. This overpayment, based on the IR rate (1.75%), would return only $1,150 of interest 6 months later. If GFL had paid its provisional tax into a tax pool instead of directly to the IR, the tax intermediary may be able to offset this with another taxpayer's underpayment and return approximately $2,900 (of say 4.4%) of interest to GFL (an increase of approximately 50%).

Purchasing

Summer Seasons Limited (SSL) identifies 6 months late that it has underpaid its third instalment of provisional tax by $50,000. This underpayment, based on the IR rate (8.40%), would leave SSL with $2,120 of interest to pay as well as late payment penalties, because it did not meet its uplift liabilities. If SSL approaches a tax pooling intermediary to purchase this tax based on an intermediary's rate (of say 6.3%), it would have $1,580 of interest to pay and zero late payment penalties.

Financing

Slow Winter Limited (SWL) is coming up to its second provisional tax payment date however it has been experiencing a decrease in business in recent months and is unable to make its next provisional tax payment of $50,000 until 3 months later. Based on the IR rate (8.40%), paying this payment 3 months later would leave SWL with $1,050 of interest to pay as well as late payment penalties, because it did not meet its uplift liabilities.

However, since SWL knows what its liability is going to be on its provisional tax date, SWL could approach a tax pooling intermediary to finance this payment on its due date. By financing the payment SWL would be able to purchase tax paid at the due date but in 3 months' time when it has sufficient cash flow. The cost of financing this transaction would be $840 which is calculated at the intermediary's rate (say 7.0%) for 3 months. This payment would be required to be paid on the date of entering into the finance arrangement.

"Clients really appreciate the ability to defer the payment of their tax to match their business's cash flow, rather than having to pay on the provisional tax dates stipulated by Inland Revenue" says Chris Cunniffe. "Tax Financing is the fastest growing part of the tax pooling industry".

When considering the use of tax pooling it is a good idea to shop around the various intermediaries to ensure the most favourable interest rates are received.

Tax intermediaries are easy to deal with and can be approached directly however, Deloitte is happy to help out with any tax pooling queries you may have. For more guidance, please contact your Deloitte advisor.

"Clients really appreciate the ability to defer the payment of their tax to match their business's cash flow, rather than having to pay on the provisional tax dates stipulated by Inland Revenue"

OECD releases new base erosion and profit shifting report

Diana Maitland and Bart de Gouw

The ability of multinationals to exploit differences in domestic tax rules and international standards to significantly reduce their tax liabilities continues to be a pressing and current issue for a number of jurisdictions. This has lead the Organization for Economic Cooperation and Development (OECD) to release its first report on base erosion and profit shifting on 12 February 2013. The report sets out the business case for further action from the OECD in relation to combatting base erosion and profit shifting. This 91-page report was presented at the meeting of the G-20 finance ministers and central bank governors in Moscow on 15 – 16 February 2013.

The report concludes that a global response from governments is required in addressing the problem, noting that it may be difficult for any single country acting on a standalone basis to fully address the issue. This is because base erosion and profit shifting strategies capitalise on the interface between differing tax rules across jurisdictions.

Revenue Minister Peter Dunne has endorsed the report, commenting that "the issue of large multinationals shifting their profits to countries in order to gain the most favourable tax result is of huge importance to OECD member states who are concerned about how this practice can distort and erode their respective tax bases".

He goes on to say, "The OECD work will help New Zealand and other countries to identify weaknesses in their rules and to ensure that international tax frameworks keep pace with new business models."

Highlighted in the report is the need for current international tax standards to catch up with changes in the global business climate, in particular with regard to intangible property and the development of the digital economy. The report also recommends increased focus on improving the transparency of effective tax rates of multinationals.

The G-20 welcomed the OECD report on addressing base erosion and profit shifting. It is determined to develop measures to address base erosion and profit shifting, taking necessary collective actions and looks forward to the comprehensive action plan the OECD will present in July 2013. The primary purpose of the plan is to provide countries with the tools to align the right to tax with real economic activity.

Of note, the action plan will include a proposal to further develop improvements to transfer pricing rules that address specific areas where the current rules produce undesirable policy outcomes. The action plan also includes proposals in relation to the tax treatment of intangibles, intra-group financial transactions, and instruments that neutralise the effects of hybrid instruments which take advantage of asymmetries in domestic and international tax regimes.

The report can be accessed at **http://www.oecd.org/ctp/BEPSENG.pdf.**

To learn more register for the free Dbrief webcast which will run on 13 March 2013 (see details on page 5).

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It's not too late to pay out those old imputation credits, but it soon will be

31 March 2013 is an important date in the world of tax and not just because it's the tax year end for most taxpayers. It also marks the end of the ability for companies to pay dividends attaching imputation credits using the old 30/70 ratio. After this date, companies will pay all imputed dividends using the 28/72 imputation credit ratio.

When the company tax rate dropped from 30% to 28% for the 2012 income year, the default imputation ratio also changed from 30/70 to 28/72. However a transitional rule has operated since the beginning of the 2012 income year to permit companies to pay dividends to shareholders attaching imputation credits arising from tax paid at the 30% rate using the old 30/70 ratio. This rule ends on 31 March.

Therefore if companies still have imputation credits that arose from tax paid at the old 30% rate, urgent consideration should be given to paying a dividend to pass out these imputation credits to shareholders prior to 31 March 2013 if it makes sense to do so.

There is a potential trap with this rule in that Companies that have paid out dividends using the old ratio during the transitional period need to make sure that such 30% rate imputation credits are in fact available to be attached to dividends and that the balance of these credits will not be in debit at 31 March 2013. It is therefore necessary to track those credits and debits to the ICA which relate to tax paid at the 28% rate and those credits and debits to the ICA which relate to tax paid at the 30% rate. Refunds of tax which relate to the 2011 and earlier years will reduce the balance of 30% credits and if these refunds have not been taken into account when working out what credits are available, then companies may find that the balance of 30% credits is in a debit position at 31 March 2013. If a debit balance results from the balance of credits arising from 30% tax paid, a one off transitional penalty will arise. In this case it does not matter that the overall ICA may be in credit.

Therefore the key message is, it's not too late to pay a dividend and pass out those old 30% imputation credits to shareholders, but care needs to be taken in doing so. Please contact your Deloitte tax advisor for more information.

Inland Revenue issues warning on salary packaging voucher schemes

On 21 February 2013, Inland Revenue issued Revenue Alert RA 13/01, which warns against an arrangement which is being entered into by employers whereby employees select that a part of their salary or wages is substituted for vouchers (e.g. supermarket or petrol vouchers).

What is the arrangement?

Under this arrangement, the employee's salary is treated as being reduced by the amount of the salary or wages sacrificed for the vouchers. The vouchers may be subject to FBT but because many of the participant employers are charities, these employers can treat the provision of vouchers as exempt for FBT purposes, provided they are not short term charge facilities. There is also a view with this scheme that GST output tax does not need to be paid when the vouchers are given to the employees. As well as paying less tax, employees will also have reduced "income" and so will pay less child support, decrease their student loan repayment obligations and KiwiSaver contributions as well as claim a larger Working for Family Tax Credit.

It is Inland Revenue's view that this is not a genuine salary sacrifice arrangement and that employees have not reduced their salary but merely redirected part of the cash remuneration towards fuel or supermarket vouchers. The Inland Revenue also consider that the supply of the vouchers is a supply which is subject to GST and that output tax ought to be returned by the employer on that supply.

Inland Revenue advises that it is currently investigating a number of taxpayers that have entered into this scheme. If you have any concerns about your tax position in this regard, please contact your usual Deloitte tax advisor.

Upcoming Dbriefs

Base Erosion and Profit Shifting (BEPS): Changing the Rules

The last few months have seen an extraordinary attack on the tax planning activities of the world's largest companies. The attack has come from multiple directions:

- the UK Parliament's Public Accounts Committee has publicly criticised the transfer pricing practices of Google, Amazon, and Starbucks;
- governments in Australia, New Zealand, France, and Germany have made similar public criticisms;
- in the United Nations Practical Manual for Transfer Pricing, China and India articulate why the existing application of transfer pricing rules does not leave an adequate level of taxable profits in developing countries;
- the tax authority leaders of the BRICS countries pledge to promulgate international tax and transfer pricing guidance which is appropriate for developing countries; and
- on 12 February, the OECD released its report on "base erosion and profit shifting" (BEPS), which was subsequently endorsed by the G20 countries.

What does it all mean? And more importantly, where will it all end? In this Dbrief, we'll discuss:

- BEPS: the story so far
- The road forward: what is the OECD's plan and will the BRICS countries accept it?
- Where will we end up? In particular, what changes do we predict to the established international tax and transfer pricing rules?
- Implementation: how?

BEPS will probably be the biggest story in international tax and transfer pricing in this decade. Find out what it is all about and how fundamental rules might be about to change. Presenters: Leonard Khaw, Eunice Kuo, and Peter Madden. The host for this one hour session is Steve Towers which will run on Wednesday 13 March 2013 at 2.00pm HKT (GMT +8). Attendance will count towards CPD.

Register for this webcast >

International tax: What Can We Learn from the Top Tax Cases of 2012?

Fascinating court decisions have emerged in 2012 involving the interpretation of double tax treaties and other international tax issues. What do these cases reveal? In this Dbrief, we'll discuss:

- Permanent establishment cases in India, Spain, and Italy, as well as Indian cases involving the application of the royalties definition to telecommunications and other transactions.
- Non-discrimination article cases in the UK and India, and cases dealing with the "other income" article.
- "Beneficial ownership" cases in Canada and Switzerland, and a landmark transfer pricing case in Canada.
- Anti-avoidance cases in the UK and Australia.
- A business restructuring case in France, and a debt vs. equity characterization case in the U.S.

Understand technical and practical implications of key rulings and discover how they apply to your company's international tax planning. Presenters: Leonard Khaw, Neil Pereira, and Sunil Shah. The host for this one hour session is Steve Towers which will run on Thursday 21 March 2013 at 2.00pm HKT (GMT +8).
Attendance will count towards CPD.

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Alesco decision released - Inland Revenue continues its winning streak

As we were finalising this month's Tax Alert, we received news that the Alesco Judgement from the Court of Appeal had been released. The taxpayer, Alesco New Zealand Limited, appealed against the 2011 High court decision in the Commissioner's favour (see our **December 2011 Tax Alert article**). Broadly the case concerned the deductibility of interest claimed arising from the use of optional convertible notes (OCNs) in intra group arrangements to finance the acquisition of two New Zealand businesses.

The Court has found in favour of the Commissioner, concluding that the OCNs entered into by Alesco were a tax avoidance arrangement. In addition the Court has found that Alesco took an abusive tax position within the meaning of s141D of the Tax Administration Act, upholding the High Court's decision on the Commissioner's imposition of shortfall penalties.

We will digest the case over the next few days and share our thoughts on what this means for taxpayers in an upcoming edition of Tax Alert. In the meantime the full judgement can be found **here**.

Snippets

31 March 2013 is fast approaching

While many clients and tax practitioners are focused on finalising and filing 2012 tax returns by 31 March 2013, it is also time to give consideration to the next year end for entities with a 31 March balance date before it passes. While most issues can be dealt with after 31 March 2013, some (e.g. writing off bad debts, check on the thin capitalisation ratio, dealing with debit imputation accounts) must be considered before 31 March to ensure tax paid is no more than it should be. We have written about these matters on many occasions before, so for a reminder of the issues to check, please see our **Alert article** from last year on this topic.

KiwiSaver contribution rates increase from 1 April 2013

Just a reminder that the minimum contribution rate for employers and employees will increase from 2% to 3% of gross salary or wages from the first pay period commencing on or after 1 April 2013.

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