Tax Alert

A focus on topical tax issues – August 2015

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Landing on the "free parking" space

By Mike Williams and Conor Gates

On 22 July 2015, the Commissioner of Inland Revenue released a new draft public ruling **Fringe Benefit Tax – Exclusion for carparks provided on an employers' premises** to clarify the fringe benefit tax (FBT) treatment of car parking facilities provided to employees on the employer's premises.

The draft ruling seeks to clarify situations where the "on premises" exemption within the FBT rules might still apply to certain circumstances where the parking facilities are provided under a licence agreement rather than a lease agreement, provided the licence agreement allows the employer "substantially exclusive" use.

This is a positive development from the Commissioner to bring more clarity and certainty to this position, and a refreshing change when you consider that, not that long ago, moves were afoot to dramatically increase the exposure to FBT on employer provided car parking. When the Taxation (Livestock Valuation, Assets Expenditure, and Remedial Matters) Bill 2013 first was introduced to Parliament, it was clear that Inland Revenue's intent was to dramatically broaden the FBT net to include any and all carparks provided to employees whether provided on the employer's premises or not. After a very vocal protest from the taxpaying community the Bill was ultimately passed but the measures to increase the scope of FBT on car parking were left out (along with other unpopular changes to the FBT rules).

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Inland Revenue's position on the "on premises" exemption and car parking dates back to 1999 where the Commissioner released Public Ruling BR 99/6 setting out a view on circumstances where the on premises exemption applied under what is now section CX 23 of the Income Tax Act 2007, although this previous ruling deals primarily with owned or leased property. This new draft ruling reiterates the position taken in BR 99/6 and explains in detail the Commissioner's view of whether a car park is considered to have been provided on the employer's premises or not. Inland Revenue has provided a number of helpful examples to illustrate when a car park is considered to be provided on premises or not, expanding on the examples provided with BR 99/6.

Of greater interest in the new draft ruling is the consideration of the 'lease versus licence' argument which confirms the Commissioner's view that, where an employer has, in fact or effect, the exclusive rights to the car park, then the car park is considered to be on the employer's premises. This is the case, even if the car parking facility is secured under a licensing agreement, provided that the agreement has the effect of giving the employer exclusive usage.

Whether an employer has an exclusive right is a matter of fact. The exposure draft sets out a number of indicative factors that assist in determining whether an employer has exclusive rights of a car park or not. In essence, unless a car park is specifically identifiable, can only be used by people authorised by the employer on an as/when basis and the arrangement cannot be altered unilaterally, the car park is potentially subject to FBT. The Commissioner is clear that in instances where an employer simply provides employees with access to car parks under a traditional licence arrangement the car park is still deemed to be a benefit provided off the employer's premises and therefore subject to FBT.

Deloitte views this draft ruling as a very positive move in the right direction for New Zealand's FBT regime that rightly recognises situations in which the words may say one thing but the facts and the detail suggest another.

The draft ruling is open to submissions until 2 September 2015. Please contact your Deloitte tax advisor if you wish to make a submission or would like to discuss this, or any other issue in more detail.

The exposure draft sets out a number of indicative factors that assist in determining whether an employer has exclusive rights of a car park or not

Employee allowances

Readers will recall from previous Alerts that there have been changes to the tax treatment of employee allowances and payments towards the costs of accommodation and meals. These rules generally apply from 1 April 2015 as a result of the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014.

Recent experience tells us that there is still some uncertainty around the correct tax treatment of the costs of accommodation and meal subsidies. This is particularly the case where the payment is in the form of an allowance rather than specific expense payments. We have therefore summarised below the tax treatment of these kinds of payments.

Accommodation payments

Employers can reimburse an employee's accommodation related costs on a tax free basis in the following situations:

- Overnight stays for business trips and conference attendance – can be reimbursed on a tax-free basis where there is a business need for the travel away from the normal place of work. This can include accommodation for conferences held in the employee's home location where there is a business need for the accommodation, such as a requirement to attend networking functions;
- Accommodation for an out of town secondment – can be reimbursed for up to 24 months for a secondment to a distant workplace (i.e. not within a reasonable commuting distance). This exemption is only available if the individual is a pre-existing employee prior to the secondment. The exemption ceases at a point from which the intention to exceed the 24 month time limit occurs;
- Accommodation for an out of town secondment relating to a capital project – can be reimbursed for up to 3 years providing the project is of a capital nature under an arm's length contract with a third party (e.g. a construction company proving bridge building services to the New Zealand Government). This exemption is not restricted to existing employees and can be applied to individuals employed specifically for the project, and can be extended for up to 5 years for projects relating to the Christchurch rebuild. This exemption is based on the presence of the individual employee on the project, not the overall duration of the project. However, the exemption ceases at the point from which the intention to exceed the specified time limit occurs; or
- Multiple workplaces – where an employee operates from multiple workplaces the accommodation costs at the distant workplace(s) can be reimbursed tax-free without time limit. However, this exemption is not available if the employee has two workplaces, one of which is a workplace at home.

Pre-existing rules around reimbursement of costs relating to longer term relocations remain unchanged.

Meal allowances

The costs of meals can be reimbursed on a tax-free basis where the employee is required to work away from their normal place of work. Where this is in the form of a temporary change of workplace for a period of time, the reimbursement can be made tax-free for up to three months.

Pre-existing rules regarding overtime meals and other sustenance meal allowances remain unchanged.

Reimbursing allowances

The above tax-free reimbursements can also be made in the form of a cash allowance payment as an alternative to reimbursing based on expense claim. However, where an allowance payment is made, the onus rests with the employer to ensure that the amount paid represents an equivalent to the amount that would otherwise have been paid by way of a reimbursement of actual expenditure. There are no published or pre-set amounts for such allowances. For this reason, we would recommend that employers who choose this option take steps to record the rationale behind any amount paid as an allowance.

Deloitte has long advocated for greater clarity around employer paid tax-free allowances and we welcome these changes. However, despite the clarification these rules provide, there still exist some grey areas that employers will need to carefully consider.

Please contact your usual Deloitte tax advisor if you would like to discuss how the rules affecting employee allowances may affect you or your business. Updated guidance is also available on the **Inland Revenue website**.

New DTA with Canada in force

On 2 July 2015, New Zealand's Minister of Revenue, Todd McClay, announced that the **New Zealand-Canada double tax agreement** (DTA) entered into force on 26 June 2015. The new DTA was signed on 3 May 2012 and the accompanying protocol on 12 September 2014. The new DTA replaces the 1980 treaty.

The DTA is effective for withholding taxes from 1 August 2015; and for other provisions, the agreement is effective for income years beginning on or after 1 April 2016 for New Zealand and 1 January 2016 for Canada.

Key changes include reduced withholding taxes on dividends, interest and royalties and amendments to the permanent establishment (PE) article. This article outlines those key issues.

Withholding tax rates

One of the key features of the updated DTA is reduced withholding tax rates on dividends, interest and royalties. These reductions will help New Zealand businesses compete in Canada and encourage Canadian investment in New Zealand. A summary of these changes are as follows:

Income	1980 Treaty	New DTA
Dividends - beneficial ownership < 10%	15%	15%
Dividends – beneficial ownership ≥ 10%	15%	5%
Interest	15%	10%
Royalties (generally)	15%	10%
Royalties (relating to copyright or production of artistic work but excluding royalties relating to film or television broadcasting work)	15%	5%

Dividends

The standard withholding tax rate on dividends remains at 15%, but it will reduce to 5% where the beneficial owner is a company that holds directly at least 10% of the voting power of the company paying the dividends.

Interest

The withholding tax rate on interest is reduced from 15% to 10%. However, where interest is derived by a financial institution that is unrelated to and dealing independently with a payer, the interest may not be taxed in the state in which the interest arises.

Consistent with New Zealand's DTAs with Australia and the US, the interest article contains an approved issuer levy (AIL) clause, which provides that interest arising in New Zealand will be charged at 10% (as opposed to 0%) if the payer of the interest has not paid the AIL.

Royalties

The general withholding tax rate for royalties is reduced from 15% to 10%; however, a 5% rate will apply to the following types of royalties:

- Copyright royalties and other like payments in respect of the production or reproduction of a literary, dramatic, musical or other artistic work (excluding royalties in respect of motion picture films and royalties in respect of works on film, videotape or other means of reproduction for use in connection with television broadcasting); and

- Royalties for the use of, or the right to use, computer software or a patent or for information concerning industrial, commercial or scientific experience (but not including any such royalty provided in connection with a rental or franchise agreement).

Permanent establishment

The new DTA makes the following changes to the PE article:

- A PE will arise only if a building site, construction, installation or assembly project lasts more than 12 months (six months under the 1980 DTA).
- An enterprise will be deemed to have a PE in a contracting state if the enterprise carries on activities in connection with the exploration or exploitation of natural resources, including standing timber, for more than 183 days in a 12-month period; or if it operates substantial equipment in the other state.
- Consistent with New Zealand's other recent DTAs, a new section provides that, subject to certain exceptions, an enterprise will be deemed to be carrying on a PE in the other contracting state if it performs services in the other contracting state:
  - Through an individual who is present in the other state for more than 183 days in a 12- month period and more than 50% of the gross revenue attributable to active business activities of the enterprise during this period are derived from the services performed in that other state by the individual; or
  - For a period or periods exceeding 183 days in a 12-month period, and the services are performed for the same project or for connected projects through one or more individuals who are present and performing such services in that other state.

For more information about this DTA, please contact your usual tax advisor.

Deductibility of management fees – TRA provides warning for taxpayers

Brad Bowman and Sarah Sussman

The recent Taxation Review Authority (TRA) case of **Case 10/2015 [2015] NZTRA 10** considered the deductibility of management fees with respect to management services provided between related parties and, if amounts were found to be deductible, whether the arrangement constituted tax avoidance.

The taxpayer was the corporate trustee of a trust. The trust had trustee income of approximately $1.116m and was the beneficial owner of a number of subsidiary companies, which were largely in losses. The taxpayer claimed that one subsidiary provided management services to other subsidiaries held by the taxpayer. With respect to the provision of these management services, the taxpayer received a deduction of $1.116m (and the subsidiary returned income of $1.116m). The Commissioner denied the deduction for the management fee.

In the TRA, the Commissioner argued that the management fee was not deductible on the basis it did not have sufficient nexus with the production of the trust's income or the carrying on of its business. The Commissioner also argued that, if the management fee was deductible, it was part of a tax avoidance arrangement which was void against the Commissioner for tax purposes.

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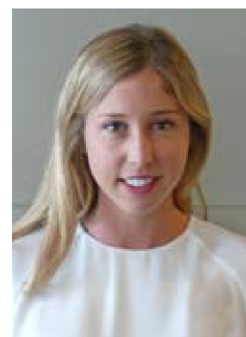

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Nexus with income

The TRA held that the management fee did not have a nexus with the trust's income. The management fee was therefore not deductible to the trust.

In drawing this conclusion, the TRA made reference to the following:

- The entry of a management fee expense paid to the subsidiary in the Trust's financial statements did not establish that management services were actually provided;
- There was no evidence of any company resolution or any agreement between the Trust and the subsidiary for the charging of management services;
- There was no invoice for the management fee or supporting accounts for any of the work allegedly done; and
- The subsidiaries held by the trust were separate legal entities. It followed that any expenses that were incurred in the management of those subsidiaries were deductible by those companies and not by the Trust.

Avoidance

If the management fee is ignored, the trust would have had income of $1.116m with tax to pay of $348,280. The payment of the management fee had the effect of reducing the trust's income to a level where it had no tax to pay (i.e. a tax benefit was obtained).

The TRA considered that Parliament would not have contemplated using provisions in relation to the deductibility of management fees in a manner which effectively shifted profits and losses between related parties. In this structure, instead of using the management fee to transfer profits to the subsidiary, Parliament would have intended a distribution of the trust's profit as beneficiary income (as the TRA had noted occurred in previous income years).

In addition to this, the TRA noted that the arrangement was effected solely by a series of journal entries and corresponding adjustments of liability for loans (as opposed to any real consideration moving between parties). This was considered to be contrived and artificial, and to make no commercial sense, which contributed towards the TRA conclusion that the tax avoidance purpose or effect of the arrangement was not merely incidental.

While the facts of this case illustrate clear avoidance, we consider that it is a timely reminder to ensure related party transactions are documented correctly. There must be actual services provided which have been valued appropriately.

The TRA therefore held that, if the management fees were deductible, the arrangement would have constituted a tax avoidance arrangement and would have been void against the Commissioner.

Deloitte comment

While the facts of this case illustrate clear avoidance, we consider that it is a timely reminder to ensure related party transactions are documented correctly. There must be actual services provided which have been valued appropriately. It is also important that taxpayers:

- Make sure agreements to provide management services are documented via a company resolution or an agreement between the related parties;
- Make sure the provision and payment of management services are accompanied by an appropriate invoice documenting the transaction; and
- Be wary of merely recording transactions by way of journal entry. Genuine consideration must move between the related parties

If you have any questions in relation to this, please don't hesitate in contacting your usual Deloitte advisor.

New Zealand and Samoa sign DTA

On 8 July 2015, it was announced that Prime Minister John Key signed a **double tax agreement with Samoa** (the NZ-S DTA). New Zealand is Samoa's second largest trading partner and the NZ-S DTA seeks to provide a platform for increased trade and investment between the two countries.

The NZ-S DTA will replace the existing tax information exchange agreement between New Zealand and Samoa when it enters into force.

The withholding tax rate that applies for dividends will be 5% where the beneficial owner of the dividend is a company which holds directly at least 10% of the voting power in the company paying the dividend. Where this does not apply, all other dividends will subject to a 15% withholding tax rate.

The withholding tax on interest and royalties will be limited to 10% by the NZ-S DTA.

It is of note that the term "royalty" is defined to include "the use of, or the right to use any industrial, scientific or commercial equipment". This runs against the more recent trend of moving the taxing of rental or leasing of equipment to fall under the business profits article.

Like a growing number of DTAs, the NZ-S DTA contains a limitation of benefits article. Article 21 prescribes that a benefit under the NZ-S DTA shall not be granted where that benefit was one of the principal purposes of any arrangement or transaction.

Unlike recent DTAs, the NZ-S DTA does not contain a non-discrimination article.

As the NZ-S DTA has been signed, it is now awaiting Parliamentary examination before being considered by the relevant select committees.

If you have any questions in relation to the NZ-S DTA, please contact your usual Deloitte advisor.

OECD provides update on transfer pricing issues

On 7 July 2015, the Organisation for Economic Co-operation and Development (OECD) provided an update on the status of various transfer pricing matters in connection with Actions 8, 9 and 10 of the Base Erosion and Profit Shifting (BEPS) Action Plan. The update highlights areas in which progress has been made and those in which additional work will be needed to reach consensus. Although the information provided reflects only Working Party 6 (WP6)'s current thinking, and is not necessarily indicative of where WP6 will end up, progress appears to have been made since the public consultation on 19 March 2015.

The revised transfer pricing guidelines will be submitted to the OECD Committee on Fiscal Affairs for formal approval in September this year and then finally to the G20 Finance Ministers Meeting in October for ratification. However, guidance on financial arrangements, the use of the profit split method and profit attribution to permanent establishments will not be part of the final deliverables to the G20 and are expected to be developed in 2016 and 2017 (and possibly later for financial arrangements).

More information can be found **here**.

While no legislative changes have yet been made in New Zealand to manage transfer pricing related BEPS issues, Inland Revenue Officials have repeatedly highlighted transfer pricing as a key focus area going forward. Taxpayers can in future years expect Inland Revenue to place an even higher level of scrutiny on their transfer pricing policies and their implementation. We understand that Inland Revenue is currently increasing the size of their transfer pricing investigations team.

If you require further guidance or for more information please contact a member of the Deloitte transfer pricing team.

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