Tax Alert

A focus on topical tax issues

August 2016

Supreme Court delivers Trustpower decision

The Supreme Court delivered its decision in the case of Trustpower v Commissioner of Inland Revenue, and the answer was not what taxpayers were wanting to hear: "The appeal is dismissed."

The Trustpower case has been through three courts, with the initial verdict in favour of the taxpayer and all subsequent appeals siding with the Commissioner, denying a deduction for the cost of resource consents needed to evaluate the feasibility of possible windfarm projects. Our articles setting out the facts and analysis of the High Court and Court of Appeal decisions can be found here.

While the outcome will be disappointing to both Trustpower and the wider tax community, it's not all bad news as the judgment does takes some steps to reverse some of the controversial aspects of the Court of Appeal decision. The Court of Appeal decision was widely criticised

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as it took the position that expenditure analysing the feasibility of potential windfarm projects could essentially never be deductible, or only in very limited circumstances – as the expenditure did not satisfy the "general permission" (the tax legislation requires that there is a nexus between expenditure and the operation of the taxpayer's business to derive income). The Supreme Court has rejected this proposition, which is very pleasing.

While the judgment doesn't completely close the door on feasibility expenditure being deductible, the Court indicates that only very preliminary expenditure may qualify. The judgment notes: "*As is apparent, we consider that some feasibility expenditure referable to proposed capital projects might sometimes be deducted. We do not, however, see such deductibility as extending to external costs incurred in respects which do, or were intended to, materially advance the capital project in question.*"

This theme continues in the Court's concluding comments: "*The expenditure on obtaining resource consents in this case was directly related to specific projects that would be on capital account if they came to fruition. The projects could not proceed without resource consents. Obtaining the consents thus represented tangible progress towards their completion. The expenditure is thus on capital account and not deductible.*" Emphasis is put on the fact there was "tangible progress" towards the completion of a project. How taxpayers should determine if and the extent to which "tangible progress" has been made will be something Inland Revenue will need to urgently prepare some guidance on. This does appear to be based on an application of certain principles in another case (*Milburn*) in relation to resource consents, which arguably are not on all fours with Trustpower's facts.

The judgment highlights the subjectivity that is inherent in applying the capital/revenue boundary, noting that it is not up to the courts to construct a test for determining the point in time when expenditure ceases to be deductible. Although the role of a court is to decide the legal issue by reference to the facts before it, it would have been helpful for the highest court in New Zealand to articulate some general or guiding principles in this regard. The judgment also highlights that there is a degree of unfairness in the legislation, as there will be cases where no deduction at all is available to a taxpayer (this is referred to as "black hole" expenditure). While subsequent to this case arising there has been law change to remove the possibility of black hole expenditure for certain resource consents, there is still a policy problem that businesses can suffer from this complete lack of immediate or over-time deductibility (and this will likely be more prevalent following this judgment). This begs the question as whether there needs to be law reform – we say yes.

Inland Revenue has previously stated that it will continue to apply its previous interpretation statement on feasibility expenditure until this judgment was released. All eyes now turn to the Inland Revenue to find out what its next step will be.

While we see this decision as moving the capital/revenue boundary in Inland Revenue's favour, we hope they will continue to respect tax positions taken by taxpayers to date where they have been consistent with Inland Revenue's guidance. As the Court has essentially rejected the "commitment test" outlined in that guidance, at an absolute minimum there should be no issue of penalties being applied to any taxpayers who have taken tax positions consistent with that guidance.

Please contact a Deloitte tax advisor if you would like to discuss what this Supreme Court decision means for your business.

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Undeveloped software taxation

By Troy Andrews

The tax position of software developers hits at the heart of New Zealand's 3.0 export economy: technology. Inland Revenue has released an Issues Paper: Income tax treatment of software development expenditure[1]. The purpose of the paper is to revisit the guidance they provided in 1993. To give you some context, this was the year that Encarta was first released on CD Rom. The new issues paper asks the industry a number of questions to – hopefully – help frame the right policy settings to support this future economy. Inland Revenue have asked for submissions to these difficult - but important - concepts by 25 August 2016.

The issues paper is a continuation of Inland Revenue's 'inclusive' approach to policy setting which is to be commended. The inevitable difficulty is that its starting point is to test whether the 1993 'settings' are correct in today's environment when concepts like software as a service (SaaS) and 'the cloud' or an App, were still futuristic 'to be' discoveries. We would prefer a blank canvas starting point. The reality is that we need policy settings that are very clear to apply and generous to taxpayers to ensure New Zealand is a global leader. This is relevant to our pioneering giants (like Xero, Orion Health and Vista Entertainment Solutions) and to make sure our SME / start ups follow their success.

The issues paper asks a number of questions looking at three areas:

1. Trading stock
2. The depreciation regime
3. R&D

Trading stock

The 1993 guidance created uncertainty for software developers that continues today. This is because it discussed applying the trading stock rules where software was developed for sale or licence. Being within the trading stock rules could be seen as concessionary as it let taxpayers take a deduction for their costs of developing software. However, these were difficult concepts to then apply. The guidance continued that if the software was sold once, then it had a 'nil' closing stock (but with no legislation to support this). An inevitable tension would also arise if the taxpayer had an opportunity to 'exit' as trading stock is taxable when sold in an M&A context.

The current issues paper still starts with an open question of when the trading stock rules should be applied, and how. The proposal is a much narrower application – suggesting that maybe it is only when "*it is being produced for sale by way of assignment of all or part of the copyright rights*". This still feels like an unnatural application of the trading stock rules and will create uncertainty. Whenever there is continuing copyright or intellectual property that the software developer could use again, the more comfortable regime is the depreciation regime which also has challenges.

Taxpayers should work through their business model and a detailed analysis of the rights that they provide customers and those that they maintain, to help with Inland Revenue's education. Taxpayers should also consider their current tax position and whether there might be transitional rules that could impact them – if they have taken a position that it **was** trading stock, but won't be going forward.

The depreciation regime

In our view, the depreciation regime is likely to be the more natural regime to tax most software companies. This is on the basis that they build and develop an asset that is capable of being "sold" and "resold" to their

[1] IRRUIP10

customers in different legal forms. The nature of these legal forms will be varied and might include full or limited copyrights – depending on the nature of the software. A good example is 'open source' software or the increasingly 'customisable' platform licences (where customers can take solutions from a number of developers, to modify and potentially use or resell a new solution). The depreciation regime does have difficulties for taxpayers to work through. For example:

Internal costs – small developers do not have sophisticated financial reporting systems to capture internal costs that should be 'capitalised'. The development team's wages and overheads are often recognised as an expense for accounting purposes and often deducted for tax purposes. These internal costs should be capitalised and depreciated which does increase compliance.

What depreciation rate to use – software and software rights fall within the 'tangible' depreciable property regime (with a generous 50% DV depreciation rate) and within the intangible depreciable property regime (with a less generous depreciation deduction spread over its legal life). It would be useful for Inland Revenue to clarify in legislation when each rate should be used – or confirm whether it might be a choice.

Upgrades v maintenance – where continued development might comprise a capital upgrade compared to deductible 'maintenance' is another unclear area. The paper suggests that a test might be whether it materially increases the capacity or performance of the software? It gives examples of bug fixing or making minor changes, compared to adding new features. In practice, this can be difficult to apply when development teams have a continual improvement methodology – or don't track and allocate their activity. Inevitably this has a compliance cost for the taxpayer.

Feasibility – the paper also raises whether some expenditure that would otherwise be capital in nature might be deductible as feasibility expenditure. Traditionally this has been expenditure that is incurred 'before' there is a commitment to pursue a particular course of action. This particular discussion will have to be suspended while Inland Revenue considers how to digest its "new" position following the *Trustpower*[2] case where it succeeded in the Supreme Court, that such expenditure was not deductible.

In our view, the depreciation regime is likely to be the more natural regime to tax most software companies. This is on the basis that they build and develop an asset that is capable of being "sold" and "resold" to their customers in different legal forms.

Research and Development

The research and development (R&D) rules are another discussion area the paper raises. These rules provide a specific deduction (that overrides the capital limitation) where expenditure qualifies as "research" or "development" and is expensed under the appropriate accounting standard (now IAS 38). There are also a number of other benefits from falling within these rules, such as potentially cashing out losses or deferring the tax deduction (which can be a benefit for taxpayers in losses).

The principle behind the R&D rules is positive. However, the reality of how they are applied in practice is often complicated with high compliance costs. For a taxpayer to use the rules, they need to apply the full IAS 38 accounting standard (as an IFRS taxpayer). This has traditionally not been the case for taxpayers that apply the differential reporting concessions, or today, for taxpayers that do not prepare financial accounts that adopt IFRS/IAS38. Essentially, the R&D rules often become unavailable for those that need them most (startups and SMEs).

Another compliance issue – which the issues paper confirms – is that recognising an amount as an expense for accounting purposes under IAS 38 is not sufficient to be R&D. The issue is that IAS 38 is the accounting standard for 'intangibles' which is a much wider concept than "research or development". In addition to being recognised as an expense under IAS 38 a software developer will also need to review their expenditure to ensure that it qualifies as "sufficiently innovative". The paper sets out that judgement will be required and will be determined on a case by case basis which only adds to taxpayer uncertainty.

The evolution and revolution of software development as an industry will continue and probably speed up. New Zealand heralds its opportunity to finally export to a world market with a product that isn't limited by shipping logistics. The industry already has many issues around attracting and retaining talent while trying to promote increased technology education into schools. The increase of innovation hubs and generous technology grants are all great progress for the future. Inland Revenue needs to also modernise its policy settings and approach. Rather than providing taxpayers with a complex compliance challenge, a blank canvas approach could help uncover a specific and generous regime where software developers of all types are supported to build New Zealand 3.0.

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[2] Trustpower v Commissioner of Inland Revenue SC 74/2015

Safe harbours for Trans-Tasman related party loans

By Bart de Gouw and Kirstie Vervoort

New Zealand multinationals commonly engage in financing transactions with related parties in Australia. In an effort to reduce compliance costs both Inland Revenue and the Australian Tax Office ("ATO") maintain 'safe-harbour' guidance for small value loans. Where transactions fall within the scope of the guidance, the specified safe-harbour rates may be applied and will be accepted by Inland Revenue and/or the ATO as complying with the arm's length principle.

The inherent bi-lateral nature of loan agreements has left a degree of uncertainty regarding which guidance to apply and when. This article aims to outline the material differences between the two sets of guidance and when each may be applied.

Inland Revenue Guidance

In order to rely on Inland Revenue's small value loan guidance, the value of the cross border associated party loans must not exceed in aggregate NZD 10m principal. Provided this threshold is not exceeded, taxpayers may apply the safe-harbour rate specified by Inland Revenue; currently equal to an "appropriate base rate" plus 250 basis points. This rate was recently reconfirmed and is due to be reviewed by Inland Revenue on 30 June 2017. Aimed at reducing compliance costs, the guidance may generally be relied upon for qualifying transactions and no additional more robust analysis is required. A circumstance in which a taxpayer may not be able to rely on the guidance is where a debt instrument with similar terms and risk characteristics is readily available.

ATO Guidance

The eligibility criteria for the ATO guidance is more detailed than Inland Revenue's, but broadly applies to documented AUD loans *into Australia* for a group of entities that have a combined "cross-border loan balance" (including all interest-bearing and interest-free loan balances for amounts borrowed and loaned) of AUD50m or less.

Taxpayers that meet the eligibility criteria may apply a maximum interest rate equal to the Reserve Bank of Australia indicator lending rate for 'small business; variable; residential-secured; term' (published monthly). Currently this indicator rate is 6.50% per annum. Qualifying transactions priced in accordance with this guidance should not be subject to further scrutiny from an Australian transfer pricing perspective.

It is important to note when relying on such guidance, that the tax authorities continue to focus on the appropriateness of the overall arrangement to ensure all material aspects of the loan are both commercially appropriate and reflected in the interest rate applied. This includes determining and being able to support the term of the loan, interest rate reset periods and base interest rate applied.

Applying the guidance

The eligibility criteria for application of the Inland Revenue and the ATO guidance varies substantially, with Inland Revenue placing greater emphasis on the principal value of the transaction and the ATO taking a holistic view of a group's international financing arrangements. Of particular note, Inland Revenue's guidance applies to both outbound and inbound loans whereas the

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ATO guidance is limited to inbound AUD denominated loans.

For New Zealand taxpayers lending to Australian related parties, there will be scenarios where it may be possible to apply either set of safe harbour guidance.

1. Outbound loans (NZ taxpayer lending to Australian related party)

   – AUD loans which fall under both the NZD$10m and the AUD$50m thresholds may be eligible for both sets of guidance. Where the ATO safe harbour rate exceeds the Inland Revenue safe harbour, it may be favourable for New Zealand taxpayers to apply the ATO safe harbour rate to maximise interest received.

   For example, consider an AUD$5m 'on-demand' loan from a NZ entity to an associated Australian entity. Applying Inland Revenue guidance, the interest rate receivable is approximately 4.25% (being the current AUD cash rate plus 250 basis points). Applying ATO guidance, the interest rate receivable is approximately 6.50% (being the current indicator lending rate), offering a further 2.25% above that prescribed by the Inland Revenue guidance. As this rate exceeds the Inland Revenue safe harbour, no NZ transfer pricing risk arises.

   – Loans which exceed the NZD$10m threshold but fall within the AUD$50m combined cross border loan balance criteria will fall outside the scope of Inland Revenue small value loan guidance, but may be eligible for the ATO simplified record keeping option for low value loans, provided they are denominated in AUD. In such cases additional analysis may be needed to satisfy the Inland Revenue that the rate applied is not less than arm's length.

2. Inbound loans (borrowing from an Australian related party)

   For qualifying inbound loans, taxpayers may apply the Inland Revenue's safe harbour guidance in the absence of more robust analysis. As the ATO safe harbour guidance excludes loans outbound from Australia, ATO simplified record keeping guidance may not be relied upon, so in this case only the Inland Revenue guidance is available.

It should be noted that reliance on the safe harbour guidance prescribed by one tax authority may result in some exposure to transfer pricing risk in the other jurisdiction, depending on the size of the loan and the interest rates applied.

Conclusion

We therefore recommend consideration of safe harbours prescribed by both tax authorities when entering into trans-Tasman financing arrangements, as this may save compliance costs and optimise the outcome in New Zealand. Such guidance should be applied prudently and consideration should be given as to the level of documentation in place (particularly the existence of formal loan agreements), and related issues such as the impact on foreign exchange gains / losses, the borrowing entity's thin capitalisation position, and non-resident withholding tax arising on interest payments.

More information relating to Inland Revenue and ATO safe harbour guidance can be found at the respective tax authorities' websites. If you require any further information or wish to discuss a particular transaction and how this guidance may be applied please contact one of our transfer pricing specialists.

Employee share schemes? New PAYE rules will impact you

By Liz Nelson and Belinda Hagstrom

This month Inland Revenue released some early guidance on the practical application of the new tax rules affecting the collection of information and tax on benefits under employee share schemes.

The new tax rules apply from **1 April 2017** and require employers to report share benefits under an employee share scheme in the PAYE system, with the ability to withhold PAYE on such benefits (at the employer's option).

At the moment, it is up to the employee to report and pay tax on any income they receive under an employee share scheme. This creates an additional burden for the employee as they may be required to pay provisional tax during the year (exposing them to interest and possible penalties if they fail to do so), and file a personal income tax return including the employee share scheme income.

Inland Revenue was concerned that not all income was being captured, as there was no transparency around when employee share scheme benefits were received by employees.

The purpose of the new rules is to reduce the need for employees to pay tax and file a personal income tax return, as well as identify employees that should be paying tax.

From 1 April 2017, when an employee or an associate acquires shares under an employee share scheme the employer must report the benefit as employment income in the PAYE return. The employer can also opt to withhold PAYE on the benefit.

As an example, for an employer who files a monthly PAYE return, if a share benefit is received in April 2017, it would be included in the employer monthly schedule (EMS) for the period ending 30 April (due 20 May 2017).

For large employers (who file twice monthly), there is a special rule to defer the timing of the benefit:

- Where a share benefit is received in the first half of the month, it is shifted to the second half of the same month;
- Where a share benefit is received in the second half of the month, it is shifted to the first half of the following month.

This has the potential to defer the income to the employee. For example, where a share benefit is received in the second half of March 2018, the income is shifted to April 2018 (the following tax year). Inland Revenue has noted in their guidance that they may investigate cases where the deferral is exploited for personal advantage.

The new rules do not apply to Commissioner-approved schemes (employee share schemes approved under DC 12 and DC 13 of the Income Tax Act 2007).

If you have an employee share scheme, we recommend you prepare your payroll systems for the changes, and let employees know whether you will be withholding PAYE on employee share scheme benefits (this is the employer's choice, not the employee's). If you do not withhold PAYE, employees should be made aware of their tax payment and filing obligations, as Inland Revenue will have up-to-date information on when these benefits have been received.

Please contact your usual tax advisor for further information on these changes.

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Making tax simpler… for some

New government discussion document aims to simplify tax for investors

By Robyn Walker

In early July we received the sixth in a series of government consultation documents aiming to improve tax administration for New Zealanders. The purpose of this document is to ensure that more information about investment income is received in "real time" by Inland Revenue in order for individual's tax returns to be pre-populated with dividend and interest information and for social policy entitlements / obligations to be adjusted during the income year.

For Joe & Joanne Public, if they were to ever read a tax technical paper, the outcomes for these proposals may well be met with a moderate shrug of indifferent approval; however those businesses who are paying dividends and interest may be less thrilled with the additional compliance costs heading their way.

So what is proposed?

- Payers of investment income will be required to provide Inland Revenue with information about each recipient in the month following the month in which the income is paid. Information would include:
  - the amount of income paid;
  - the amount of tax withheld (if any), and any imputation or Māori authority credits attached;
  - the investor's IRD number (if held);
  - the investor's name and address, and date of birth (if held);
  - information on each owner if the investment is jointly held;
  - for approved issuer levy payments, details of relevant customers;
  - for interest exempt from withholding tax, details of relevant customers.
- Payers of interest won't have to provide end of year tax certificates to their customers who have provided them with their IRD number.
- The "non-declaration rate", the rate that applies to a taxpayer who doesn't declare their IRD number, for RWT on interest and portfolio investment entity (PIE) tax will be increased to 45% to act as an incentive to provide IRD numbers.
- A database of taxpayers holding certificates of exemption from withholding tax will be created.
- Recipients of investment income who claim an exemption from withholding tax will be required to obtain a certificate of exemption.

Our thoughts

The overall aim of the proposals is admirable if all taxpayers have basic investments and tax affairs. Sadly, this will often not be the case as those who have capital to invest will often be looking at a diverse range of investment options, including property and foreign shares. Without being able to capture this information, seeking perfection for New Zealand sourced interest and dividends is largely pointless. There is also a real lack of information in the document about the size of the problem to justify the potential costs which will be imposed on payers of investment income.

The overall aim of the proposals is admirable if all taxpayers have basic investments and tax affairs. Sadly, this will often not be the case as those who have capital to invest will often be looking at a diverse range of investment options, including property and foreign shares.

The document itself contains a number of statistics, such as:

- **16,600 interest payers filed over 5 million interest certificates.** That's a lot of payers of interest who will need to comply with these new rules.
- **Interest income is earned by 355,537 student loan holders, 239,077 recipients of working for families, and 83,315 payers of child support.** No details are provided about whether the quantum of interest earned by these investors is significant enough to have a material impact on their entitlements and obligations. Statistics indicate that the median level of deposits held by individuals in New Zealand is only $5,000[1], and at current interest rates this would equate to around $100 of interest income per annum.
- **Dividends are received by only 7,980 student loan holders, 8,804 recipients of working for families, and 2,009 payers of child support.** This seems to be a low population base to justify all dividend payers supplying information to Inland Revenue after every dividend payment.

One of the biggest complexities is how the proposals are intended to apply to jointly owned investments. Inland Revenue considers that the "current method of reporting jointly owned investment income is not considered to be sustainable going forwards". That's well and good, but the appropriate allocation of income to each owner is not something which the payer is going to be in a position to determine. The discussion document makes no attempt to quantify how many investments are jointly owned, and while Inland Revenue is unlikely to hold this information for all investments they should know this information in respect of interest[2]. The requirement for payers of interest and dividends to provide IRD numbers, addresses and birth dates for all joint account holders is an onerous task. A quick review of application forms for recent bond issues and share offers shows that this information is not currently collected – the application forms make it clear that only one Inland Revenue number and address is required even for joint applications. A date of birth is not something being routinely collected.

While it is pleasing that the discussion document refers to payers only supplying information "if held", there is no confirmation in the discussion document that these data points will not become compulsory in the future. If businesses were to be required to actively seek out this information this could be a time consuming exercise. Any businesses who are planning debt or equity issues may well wish to start collecting this information going forward.

Investors in PIEs who have not provided an IRD number will be well incentivised to do so if the proposals proceed. PIE tax is usually considered to be a final tax, with a maximum rate of 28 percent. The discussion document proposes taxing investors who have not supplied IRD numbers at 45 percent; with the suggestion that investors will not be able to include these amounts in their tax returns to claim back the excess. Investors are unlikely to view this favourably and it is the PIE who is likely to be the first port of call for complaints.

Like with the rest of the consultation documents in the series, the Government is interested in your views. Submissions can be made in writing until 19 August 2016 and feedback is also being taken through an online forum.

Proposals that the Government decides to go ahead with would be included in legislation to be introduced in 2017. The application date would allow sufficient time for system changes.

Please contact your usual Deloitte advisor if you wish to know more.

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[1]Statistics New Zealand; Household Net Worth Statistics: Year ended June 2015; Table 1.02 Assets & Liabilities by individual
[2]The annual IR 15 statement provided to Inland Revenue will state whether the investment is a joint account

Inland Revenue targeting language schools on GST issue

By Allan Bullot and Petra Safkova

There has been an ongoing focus by Inland Revenue with regard to GST on services consumed in New Zealand which are supplied through offshore intermediaries, such as travel agents and booking portals. The latest to come under scrutiny are language schools.

In recent weeks, Inland Revenue issued letters to 75 language schools providing tuition to overseas students through non-resident agents, resellers or retailers. In its letter, Inland Revenue express a strict view that local schools should apply New Zealand GST on the gross fee (not the net fee) paid by overseas students to overseas agents, resellers or retailers for education services in New Zealand. This principle is based on the *Auckland Institute of Studies v CIR* (2002) case. Inland Revenue consider GST should be returned based on the gross fee before deducting any commission paid to the overseas agent, or from a fee including any margin added by the overseas reseller or retailer. In Inland Revenue's view, any pre-arrival services are not zero-rated, as they form a component of the total fee and must share the GST treatment of the tuition service, i.e. be subject to GST at 15%.

Inland Revenue is providing taxpayers with the option of correcting their GST position by making a voluntary disclosure which would cover the past 2 years and requiring taxpayers to correct their treatment going forward, provided this disclosure is made promptly.

While we agree with many aspects of the Inland Revenue letter, we believe arrangements where a right to receive education services is in fact legally sold by the overseas reseller or retailer as a principal, and not as an agent, could be viewed differently. Depending on the model the particular school applies it is possible that a voluntary disclosure is not necessary.

If you have received a similar letter from Inland Revenue or have a business which operates similarly, we would encourage you to contact your Deloitte advisor to discuss your GST position.

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Will the Commissioner be an unlikely beneficiary of the unitary plan?

With the release of Auckland's proposed unitary plan ("the unitary plan") on 27 July 2016, some Auckland land owners may be excited about the new potential earning possibilities from the sale or development of land which has been rezoned. But there is another person who could also benefit from the change in rules: The Commissioner of Inland Revenue.

The unitary plan suggests several significant changes which will enable land owners to develop their land in new ways. In light of the current state of the property market, there are likely to be some looking to sell rezoned land and make a significant profit. But those contemplating this should ensure they seek tax advice before doing so. While the commonly applied land rules may not require you to pay tax, the less-common section CB 14 of the Income Tax Act 2007 may apply to tax income derived.

Under section CB 14, a person who sells their land within ten years of buying it, and for more than it cost, will be required to pay tax if at least 20% of the gain can be traced to a factor under the Resource Management Act 1991 ("RMA"). The list of qualifying 'factors' is very broad. If 20% of the gain is due to the rules of an operative district plan under the RMA (e.g. the unitary plan) then the person selling the land must pay tax. Equally, if 20% of the gain is due to the likely imposition of rules, or a change to the rules, or even the "likelihood of a change to the rules," the person selling the land will find themselves squarely within the rules. In other words, this rule already applies.

However before bemoaning the long arm of the law, this land tax rule will not apply where the seller initially bought the land for "residential purposes" **and** the sale was made to a person "who acquired it for residential purposes". Those who currently reside in the property and sell to a person who either purchases the land to live in or to build a house to live in, will not be subject to tax, whereas if they sell the land to a developer they will be subject to tax. And tempting as it might be for people to structure around these rules, the Commissioner has wide powers to look at the circumstances of the disposal and other relevant matters to determine whether the person acquiring the land did so for "residential purposes". Since the fate of the sellers tax position is in the hands of the buyer to a degree, the seller will want to ensure they do due diligence on the purchaser's true intentions, and perhaps document the agreed intentions of the parties. Similarly, there is a farming exclusion from these rules for land which was acquired and used for farming purposes, is subsequently rezoned and disposed of to another person who will continue to use the land for farming or agriculture.

Sellers who are subject to section CB 14 will be relieved to know that in addition to the normal range of deductions available, Inland Revenue also allows an apportioned deduction under section DB 28. The apportioned deduction is a percentage of the disposal profit proportionate to how many years the land has been held. If the land is held for 9 years, 90% of the profit is allowed as a deduction. If the land is held for 5 years, 50% is allowed.

It is likely that Inland Revenue's special property taskforce will be scrutinising Auckland land transactions in rezoned areas in light of the proposed changes to the unitary plan.

The Council have until 19 August 2016 to finalise the unitary plan. For further information about these rules in relation to property you own please contact your usual Deloitte tax advisor.

A snapshot of recent developments

Government accepts Shewan Inquiry recommendations

In last month's issue of Tax Alert, we reported on the Government inquiry into the foreign trust disclosure rules. In a joint statement on 13 July 2016, Minister English and Minister Woodhouse announced that the Government will adopt the Shewan recommendations. Minister English says that "the Shewan Inquiry's recommendations are sensible and well-reasoned and by acting on all of them, we will ensure that our foreign trust disclosure rules are strengthened and New Zealand's reputation is protected". This table summarises the Government's responses to the Inquiry.

Special report: Simplifying tax collection on employee share schemes

As noted earlier in this issue of Tax Alert, Inland Revenue has released a special report, Simplifying the collection of tax on employee share schemes, to provide more detail and practical information on the changes included in the recently enacted Taxation (Transformation: First Phase Simplification and Other Measures) Act. The new rules apply to income years beginning on or after 1 April 2017.

Use of a valid electronic signature on documents provided to the Commissioner

On 5 July 2016, Inland Revenue released a draft standard, EPR616, on the use of a valid electronic signature on documents provided to the Commissioner. The draft standard sets out the application of section 13B of the Tax Administration Act 1994 and specifies the conditions under which Inland Revenue will accept documents and information with an e-signature. Submissions close on 22 August 2016.

Income tax treatment of software development expenditure

On 13 July 2016, Inland Revenue released an issues paper on the income tax treatment of software development expenditure, IRRUIP10. The issues paper notes that the current approach, developed in 1993, does not adequately address the rapidly evolving world of software development. For more information on this topic, see our article within this issue. Submissions are due 25 August 2016.

Submissions on bill close

Submissions on the Taxation (Annual Rates for 2016-17, Closely Held Companies, and Remedial Matters) Bill closed on 29 July 2016. This is the omnibus bill that contains significant tax changes to look-through companies, the NRWT and AIL rules and changes to the related party debt remission rules amongst many other things. Refer our Alert article in May for an outline of the contents of this bill. The report back to the Finance and Expenditure Committee by Officials has been set for 15 December 2016.

Remote Services – GST Registration Form Released

Inland Revenue has released the GST registration form (IR994) for non-resident suppliers who are required, or wish, to register for New Zealand GST under remote services regime. The regime applies to supplies of "remote services" made by non-resident suppliers to New Zealand customers from 1 October 2016. Inland Revenue has also published two new webpages providing additional information on the remote services regime for both suppliers and recipients of remote services. Further information on the regime can be found in an earlier article here.

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