



Tax Alert

A focus on topical tax issues

February 2017

No tax holiday for short term rental accommodation

By Conor Gates

With the advent of online accommodation marketplace services such as AirBNB, Book-a-bach, and similar holiday home rental sites, it has never been easier to turn a spare room, a holiday home or any other usable space into some easy cash.

More and more New Zealanders are making the most of the new

accommodation craze and it is easy to see why when the hassle of advertising, managing bookings and collecting payment are provided through a third party platform. However, many people are using these services without consideration of the potential tax implications which can transform a little extra income on the side into an unexpected tax bill.

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We have set out some of the issues below, including a few traps for the unwary that might arise when making property available for use as short term accommodation.

The basics – calculating and paying income tax

New Zealand's tax laws require that income earned in a business which is carried on for profit is subject to tax. Income earned by providing short term accommodation through a peer-to-peer service is no exception to the rule.

A taxpayer may deduct the costs incurred from operating the short term accommodation with deductions determined on a reasonable basis to reflect the costs actually attributable to the activity, particularly where the expenses have both private and business elements (e.g. insurance, interest and rates).

Taxpayers may also fall within the provisional tax rules if their tax liability in a prior year exceeds \$2,500. Provisional tax requires a taxpayer to make advance payments of tax in expectation of their future tax liabilities.

The less obvious – the mixed use asset rules

The available deductions against the income can be greatly affected by the mixed use asset rules which apply in scenarios where a property is partly used in a year to derive income, is partly used for the owners (or associated persons) personal enjoyment and is not used at all for a period.

The mixed use asset rules alter the apportionment of expenses between business and personal use and can have a material impact on the calculation of taxable income. To the extent that expenses are not directly attributable to providing the short term accommodation (e.g. rates, insurance and interest) the available deductions are decreased based on proportionate business and private use.

The mixed use asset rules apply to properties owned by individuals, partnerships, look-through companies, trusts and other close companies and therefore capture the most common investment or asset protection vehicles used in New Zealand.

The spanner in the works – short term accommodation and the GST rules

While it may not be apparent to many, providing short term accommodation is a taxable supply for New Zealand GST purposes. Taxpayers need to be aware of the potential impact of falling into the GST net because once they are caught there is no escape.

The whole spectrum of GST issues relating to short term accommodation are greater than can be put in this article so we have listed some of the most common issues below.

GST registration

The GST issues start with the question of GST registration which can either occur voluntarily or otherwise is required if taxable supplies exceed (or are expected



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to exceed) \$60,000 in any 12 month period. While this seems a lot, this threshold can easily be exceeded in tourist hotspots. For voluntary registrations in an accommodation context it is often necessary to provide a comprehensive business plan to Inland Revenue.

Returning GST on rent received and commissions paid

Commonly taxpayers will receive a net payment from the provider for the rent charged less any commission or other expenses that the provider is entitled to withhold. For New Zealand GST purposes the gross rent must be returned as a taxable supply and any costs subject to GST must be included as a cost in making that taxable supply – the net amount cannot simply be included in the GST return.

Making second hand goods claims for costs incurred in the past

Once in the GST net, generally a taxpayer can recoup (over time) the GST costs paid when the property was acquired. The GST rules provide a specific mechanism for calculating how much GST can be recouped with each return.

Accounting for GST on the property at deregistration or on sale

Potentially, the greatest impact of falling into the GST net is that any eventual sale of the property (or deemed disposal on deregistration) is also subject to GST. As a result, 15% of the sale price of the property must be returned to Inland Revenue (except where the sale occurs between two GST registered parties and the property is going to continue to be used for making taxable supplies). This effectively creates a tax on any capital gain while the property was owned and possibly can end up costing the taxpayer more in GST than would have been made in profits from short term accommodation.

Ownership structure and GST

Where properties are held in family trusts, companies or other investment vehicles and are used for both short term accommodation and private use, there may be requirements to charge a deemed market rental for the private use, with GST on the deemed rental being paid to Inland Revenue.

Warning - Inland Revenue and local government bodies are paying attention

In recent years, Inland Revenue has been focusing on taxing New Zealand's black economy which is made up in part by taxpayers providing short term accommodation. However, unlike a plumber's cash job or handshake agreements between friends, using an online platform to arrange short term accommodation generates readily accessible electronic records.

Inland Revenue has wide information gathering powers and the ability to request information from online platforms. Inland Revenue can use this information to quickly identify who is providing short term accommodation and request evidence that income has been declared in a tax return and taxes paid.

Similarly with the recent requirement for IRD numbers to be associated with property transactions it is now much easier for Inland Revenue to identify that GST should be paid on the sale of a property.

Local governments are also focused on short term accommodation being provided. Under local council regulations a property used for short term accommodation is generally considered to be a commercial property which may affect rates charges and result in other administrative requirements such as consents to operate. Taxpayers should also consider other contracts held if they are providing short term accommodation to ensure that items such as insurance over the property remains valid.

Providing short term accommodation potentially exposes taxpayers to a variety of different New Zealand tax and other issues that should be considered by hosts when making property available to rent. We recommend potential or current hosts seek tax advice on their situation.

If you require any additional information about this, please contact your usual Deloitte advisor.

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Why New Zealand is unlikely to introduce a diverted profits tax (as such)

On 14 December 2016, Inland Revenue released a [Cabinet Paper](#) which had been prepared by the Ministers of Finance and Revenue, for the purpose of seeking the agreement of the Economic Growth and Infrastructure Committee to prepare and issue a Government discussion document primarily on measures to strengthen New Zealand's transfer pricing rules and prevent overseas companies from avoiding having a permanent establishment.

This is likely in response to growing political and media pressure for the New Zealand Government to follow Australia and the United Kingdom and introduce a diverted profits tax which would tax profits of multinationals that divert profits offshore (rather than allocate them to their New Zealand operations).

The cabinet paper does not contain any firm proposals; rather it outlines a planned approach of releasing a comprehensive discussion document in early 2017 for public consultation. The document also states that "while the majority of multinationals operating here are compliant there is a minority that engage in aggressive tax practices". Thus the discussion document and these proposals are targeted at this minority.

The cabinet paper outlines possible responses to addressing transfer pricing (TP) and permanent establishment (PE) avoidance setting out possible actions, namely:

- To adopt the OECD recommendations associated with TP and PE avoidance

that were set out in the Base Erosion and Profit Shifting (BEPS) Action Plan, or

- To go beyond the OECD recommendations and introduce a unilateral measure to address diverted profits from TP and PE avoidance in the form of a diverted profits tax (DPT).

In considering whether a DPT would be good for New Zealand or not, the cabinet paper states (at para 18):

"A DPT would counter non-residents who try to avoid having a taxable presence in New Zealand or who use transfer pricing strategies to reduce the tax payable. Its assessment and collection features would also address some of the practical difficulties of taxing multinationals.

Introducing a DPT would mean that there would be a new type of tax, separate to income tax, to deal with a minority of aggressive multinationals. It could impact on foreign investor's perceptions of the predictability and fairness of New Zealand's tax system for foreign investment. As a separate tax from our general income tax it may produce unintended adverse consequences for taxpayers – especially with regard to normal grouping of tax attributes (for example income tax losses would not be able to be set off against diverted profits). A DPT may also have an unintentional negative impact on compliant taxpayers.

The more we get into imposing arbitrary taxes the greater the risk of other countries doing the same to our exporters. Overall a DPT chips away at the consistency, neutrality and

relative simplicity of our tax system from a global perspective.

Finally, the DPTs that have been proposed in Australia and enacted in the UK respond to particular problems with the application of their own income tax rules to multinationals. While a DPT may be appropriate for the issues Australia and the UK face, it seems more straightforward for us to fix New Zealand's problems with our income tax rules rather than implement a new tax."

While a DPT has not been ruled out, the Ministers' preference at this stage is to recommend that New Zealand not introduce a DPT as such, but instead develop a package of anti-avoidance measures to counter TP and PE avoidance. This approach would likely take certain features of a DPT, combine them with the OECD's BEPS measures and make further amendments to domestic tax legislation, particularly to the transfer pricing rules. It is noted that the package would not change the fundamental basis on which non-residents are taxed and like the Australian and UK DPTs would not tax non-resident suppliers without a material presence in New Zealand. We will have to wait for the discussion document on this package of reforms in early 2017 for more detail.

Does complying with complex tax rules for motor vehicles drive you crazy?

By Robyn Walker and Brad Bowman

As reported in our [December 2016 Tax Alert](#), business tax simplification measures are a step closer after the report back of the Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill (“the Bill”). A number of these measures are targeted at reducing compliance costs faced by businesses, particularly small and medium-sized businesses.

This Tax Alert article will specifically look at measures aimed at simplifying the complex rules around motor vehicles. We will also touch on a few other compliance saving measures for small and medium businesses.

Motor vehicle expenditure

Under existing motor vehicle expenditure rules, sole traders and partnerships are able to claim tax deductions for the business proportion of the running costs of a motor vehicle. Companies however are able to claim all motor vehicle expenses as a tax deduction but must pay fringe benefit tax (“FBT”) if the vehicle is available for private use. The requirement to pay FBT can overtax the business relative to just denying a deduction for the private portion of the vehicle use.

Proposals included in the Bill will extend the current motor vehicle expenditure rules to close companies providing 1 or 2 vehicles to shareholder-employees and no other fringe benefits. As a result, a close company will be able to elect to apply the motor vehicle expenditure rules with a resulting denial of the deduction to the

extent the motor vehicle expenditure relates to the shareholder-employee’s private use.

This means, instead of registering for and paying FBT, close companies can deduct motor vehicle expenditure in accordance with the proportion of business use, which can be calculated using actual records, a logbook or in accordance with Inland Revenue’s mileage rates.

Before celebrating too much, the election to apply the motor vehicle expenditure rules (instead of the FBT alternative) can only be made for motor vehicles acquired by taxpayers after the beginning of the 2017-18 income year or when a motor vehicle is first used as part of the taxpayer’s business after the same date. It is important to note that no other fringe benefits can be provided by the business, which may be a tough test to meet. Once an election is made, it will continue to apply until the close company either disposes of the motor vehicle or stops using it for business purposes.

In addition to the above proposal, the Bill also includes amendments to the “per kilometre rate method” for determining motor vehicle deductions. Under this method, instead of deducting the actual costs incurred (or a portion of them), a taxpayer can deduct a fixed amount per kilometre travelled for business purposes based on rates published by Inland Revenue.



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Currently this method is limited to taxpayers whose business travel is 5,000km or less in the income year. This 5,000km or less requirement is set to be removed and replaced with an election requirement. This election would be made via the taxpayer's income tax return. The election is irrevocable and would apply to all income years until the taxpayer disposes of the motor vehicle.

This proposal also applies from the 2017-18 income year.

Other compliance saving proposals that you should be aware of

The Bill includes a number of other compliance saving proposals (a few of which are outlined below). These proposals generally apply from 1 April 2017 or the beginning of the taxpayer's 2017-18 income year.

- The self-correction threshold is set to increase to \$1,000 (previously \$500). This means minor errors of less than \$1,000 in tax can be corrected in the taxpayer's subsequent return (whether it is income tax, GST, FBT or another tax), which has the effect of eliminating the need to request the Commissioner to correct the error. This will also eliminate potential penalties and use of money interest. Note: our article on proposals to modify the Tax Administration Act 1994 includes details on further improvements to this rule.

- Under current RWT rules, taxpayers may be required to renew their certificate of exemption annually. Proposals seek to require Inland Revenue to issue RWT exemption certificates for an unlimited period. This should eliminate compliance costs associated with renewing these certificates.
- The annual FBT threshold is set to be increased from \$500,000 to \$1 million of PAYE/ESCT. This means more taxpayers would qualify for annual rather than quarterly FBT returns.
- The 63-day employment income rule is set to become optional. Taxpayers who do not wish to incur the compliance cost involved with tracking payments paid within 63 days of the end of the income year will not have to and can simply claim a deduction for expenditure paid within the income year.

Deloitte comment

We welcome the changes included in the Bill. These changes are appropriately targeted at areas where taxpayers currently incur significant compliance costs for very little return. We are particularly pleased to see pragmatic and logical changes with respect to the complex tax implications of providing motor vehicles to shareholder-employees. Changes included in the Bill are likely to result in reduced compliance costs for businesses, particularly small and medium-sized businesses.

If you have any question in relation to this article, please contact your usual Deloitte advisor.

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Making Tax Simpler: A New Tax Administration Act

By Robyn Walker and Rebecca Osborn

As kids are all returning to start a new school year and dreading upcoming Shakespearian reading assignments, the tax community has its own summer reading project with a looming deadline. Just before Christmas the latest and seventh chapter of “Making Tax Simpler” was released. At 93 pages Making Tax Simpler: Proposals for modernising the Tax Administration Act: A Government Discussion Document (the discussion document) is tough going and could suffer a bad case of TL;DR (urban slang for “Too long; didn’t read”).

Fortunately we’re providing you with a summary of the key points of the document, while also trying to not have this article labelled as TL;DR.

The purpose of the discussion document is to provide greater details of the Government’s proposals towards a new Tax Administration Act (TAA), having released an earlier discussion document on the same topic. While it would be easy to write the discussion document off as a bit of a bore, it’s important to remember that the TAA outlines the fundamental rights and obligations of taxpayers and provides Inland Revenue with expansive powers to collect information and impose penalties.

A key theme running through the proposals is greater flexibility. More discretion for the Commissioner, greater use of regulations, wider powers of information collection and sharing. Overall we think these are positive changes for the tax system. The current TAA is restrictive and often hampers the smooth and efficient administration of our tax system.

A common theme from submissions on the first discussion document was that there is a need for the Commissioner to have greater flexibility in the application of the law but that this shouldn’t be at the expense of transparency in her decision making

There are some real wins for taxpayers in these proposals. We outline below some of the major proposals to be aware of.

The role of the Commissioner of Inland Revenue (the Commissioner)

The current TAA charges the Commissioner with responsibility for the care and management of the tax system. As part of this responsibility, the Commissioner’s duty is to collect the highest net revenue over time. This allows the Commissioner discretion in how she collects tax if overall it will be beneficial to the tax system, for example by encouraging voluntary compliance. Inland Revenue has come under criticism in the past for how narrowly these provisions have been interpreted. Many have argued the Commissioner’s care and management responsibilities allow the Commissioner to apply the tax law as the policy intends, despite errors or gaps in legislation, however the Commissioner does not see her current powers as extending this far.

A common theme from submissions on the first discussion document was that there is a need for the Commissioner to have greater flexibility in the application of the law but that this shouldn’t be at the expense of transparency in her decision



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making. The discussion document outlines proposals to extend the care and management powers to allow the Commissioner greater administrative flexibility in limited circumstances. These include where minor legislative anomalies are discovered, where a strict interpretation of the legislation would be contrary to long-established practice of both the Commissioner and taxpayers or where the result under the law would create inequity to a broad group of taxpayers.

This is a very welcome proposal. Taxpayers have long been frustrated by situations where everyone is in agreement that the law is broken or doesn't quite work as intended, yet the Commissioner has felt constrained to a strict interpretation of the tax acts. Greater flexibility for the Commissioner does raise a natural concern of whether such a power could be abused. In this regard, instead of a blanket criterion that the discretion could only be exercised in a way that is taxpayer favourable, it is proposed that taxpayers would be able to choose whether to apply any care and management decision to their particular circumstances. This is a clever solution, and is consistent with one of the overall goals of the Business Transformation programme to empower taxpayers to take control of their tax obligations. Additional safeguards are also proposed, such as a three year time limit before legislative amendments are required.

Further, under the role of the Commissioner it is proposed to make greater use of regulations for tax administration processes. This is also a positive change as the current TAA often constrains Inland Revenue's ability to just get the job done.

Confidentiality

An integral part of the current TAA is the obligation on the Commissioner to keep information collected secret and to only use such information for tax purposes. This is a key pillar in New Zealand's system of voluntary tax compliance and self-assessment. However, the cliché that information is power has never been truer and there is increasing pressure on Inland Revenue to share information with other government departments and agencies. A major component of the Government's Better Public Services initiatives is the wider and smarter use of data held by the government.

While Inland Revenue does already share some information with other government agencies, the Government's aim is to modernise the rules to better allow for sharing in the future while maintaining taxpayer confidentiality. The Government is proposing to replace the existing "tax secrecy" rule with a rule that Inland Revenue must keep confidential information that relates to the affairs of, or identifies a taxpayer. The intention is that this will protect sensitive taxpayer information but allow for the release of generic, not-taxpayer-specific information.

It is also contemplated that some taxpayer specific information should be shared across agencies when it is in the interests of the public good, such as ensuring people receive their correct entitlements from the government. It is not intended to limit the government agencies that are able to obtain information from Inland Revenue, however, there will be a safeguard in place that the agency must be able to lawfully collect the information in its own right.

There has been a slow erosion of tax secrecy over the last few years and the changes proposed are a continuation of this. For the majority of taxpayers these may be welcome proposals as increasingly citizens expect greater co-operation between government agencies to maximise efficiencies and reduce duplication of effort.

Information collection

Continuing the theme of the power of information, it is proposed that the new TAA will include a provision that allows for the making of regulations covering the repeat collection of external data sets. While the Government's view is that Inland Revenue's existing data collection powers are working well, greater powers are required to access large third-party data sets. It is envisaged that the collection of such information would assist Inland Revenue in pre-populating returns and also be used for education and tax compliance purposes.

From an integrity of the tax system point of view, this is a positive change. It has been estimated that the “black economy” in New Zealand (i.e. income not reported to Inland Revenue) could be in the vicinity of \$10 - \$20 billion dollars annually. Greater access to information and the use of analytics should assist Inland Revenue to identify these tax dodgers. However, information isn't free and businesses will have to wear the costs of providing additional information to Inland Revenue.

The role of taxpayers

New Zealand's tax system is built around a concept of self-assessment. Where it is ultimately determined the original self-assessment was incorrect there are a series of formal processes that must be followed to amend the assessment. Significant resources are also employed in Inland Revenue's audit function to assure compliance. Inland Revenue's evolving approach to tax compliance is shifting away from that traditional audit model and towards helping taxpayers “get it right from the start”. A key way Inland Revenue hopes to achieve this is by interacting earlier with taxpayers and to provide advice and certainty through these interactions.

Proposals outlined in the discussion document to facilitate this include:

- Expanding the scope of the binding rulings regime;
- Significantly reducing the fees for obtaining a binding ruling, particularly for SMEs; and
- Allowing for post assessment binding rulings.

The proposals will also empower taxpayers with a wider ability to self-correct errors – currently taxpayers can only self-correct errors under \$500 (soon to be increased to \$1,000). The Government is proposing to increase this amount to the lower of \$10,000 and 2% of their taxable income or output tax for the relevant period. This is a really positive step and should minimise compliance costs for a number of taxpayers, particularly SMEs. That said, the amount is still too small to be meaningful for larger organisations.

Submissions can be made on the discussion document until 24 February 2017. If you have any questions regarding the discussion document, or would like to make a submission, please contact your usual Deloitte tax advisor.



Proposals to exclude services provided to non-residents in connection with land from being GST zero-rated are causing uncertainty

By Andrea Scatchard

Any mention of GST in the press in recent months has most likely been concerned with the so called Netflix tax, the imposition of a GST obligation on certain non-resident suppliers of remote and primarily digital services. While the theory behind these changes may be fascinating to tax professionals and academics, the changes themselves have little practical relevance to most businesses in New Zealand. Indeed it is really only at a personal level that individuals have been generally affected, when their Netflix, Spotify or other similar bill has increased in price.

What is less well known to the general public is that in conjunction with these changes there are proposals to reduce the ability to zero-rate services relating to land, where these services are provided to non-resident customers by New Zealand suppliers.

While services supplied to non-residents who do not physically receive those services in New Zealand are often zero-rated, the current GST legislation excludes from zero-rating services which are “directly in connection with” land in New Zealand. As a general rule, services must physically change the land in question in order to be considered directly in connection with that land. This is a well-established and understood test which

The Commentary on the Bill and the Regulatory Impact Statement both refer to services provided by solicitors, real estate agents and architects as the types of services which are intended to be covered by the proposals

has been the subject of judicial decision, giving rise to a line between zero-rated and standard rated transactions which is generally clearly understood by taxpayers.

The Taxation (Annual Rates for 2016-17, Closely Held Companies, and Remedial Matters) Bill proposes to further exclude from zero-rating services which are in connection with land, or an improvement to land, located in New Zealand, where those services are intended to enable or assist a change in the physical condition, ownership or legal status of the land or improvement.

If we put aside the question of whether this is conceptually an appropriate extension of GST in New Zealand, and accept that

the change will happen, the immediate concern is how should taxpayers interpret the phrase “intended to enable or assist a change in the physical condition, ownership or legal status of the land or improvement”? No guidance is given in the legislation.

The Commentary on the Bill and the Regulatory Impact Statement both refer to services provided by solicitors, real estate agents and architects as the types of services which are intended to be covered by the proposals. These types of services are explained as being “services that form an integral part of a process of physically changing the land, but do not do so themselves”, and there is logic in the argument that these services enable or



assist a change in ownership of the land in question.

However there is a much broader range of services that could potentially be affected by the changes. Consider the ancillary services that a land buyer or seller may require as part of a land transaction – advertising services, valuation reports, council LIM reports and property inspection services to name just a few. There is no clarity at all about whether these types of services will be affected by the changes. Inland Revenue officials have indicated that a Tax Information Bulletin will provide clarification through a detailed analysis of the changes, but this will necessarily only be issued after enactment of the Bill.

The Bill is currently awaiting its second reading, and with Parliament not sitting again until 7 February it is expected to be well into March before the Bill receives Royal assent. The changes are intended to take effect from 1 April 2017, which leaves little time for the Inland Revenue guidance to be issued, for taxpayers to digest its contents and determine whether their specific supplies are affected, to seek professional advice if necessary and make any system or procedural changes that may be required, all before 1 April 2017.

The process is unnecessarily rushed, and in the absence of early clear guidance on the application of the rules, taxpayers risk adopting a GST treatment which may turn out to be incorrect, with the associated penalty and interest risk if it turns out they got that treatment wrong.

If your business needs guidance through these changes, please contact one of our indirect tax specialists.



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Reforms for Non Resident Withholding Tax and Approved Issuer Levy

By Emma Marr

Proposals to amend the non-resident withholding tax (**NRWT**) and approved issuer levy (**AIL**) rules are a step closer to enactment, as the May 2016 Bill, which included extensive reforms to the rules, was reported back to Parliament in late 2016. Further details on the proposals can be found in our [May 2016 Tax Alert article](#).

As we noted when the Bill was introduced, these proposals are particularly complex. Taxpayers with overseas borrowing, whether related party or not, should be getting in touch with their Deloitte tax advisor to ensure they are prepared for the reforms when they come in to force (either on the date of enactment, which is expected to be in the next couple of months, or from the start of the next income year after enactment).

Three main aspects of the reforms are discussed below. Limitations on the offshore and onshore branch exemptions are also incorporated in the Bill. Officials accepted a number of submissions suggesting drafting changes to these rules.

Removing timing mismatches

The Bill introduces new rules aimed at removing the ability for associated taxpayers to benefit from a mismatch between when income tax deductions are available for interest expenditure and when the associated NRWT liability arises. Currently the liability to pay NRWT on an amount of interest may arise later than the deduction for that interest payment. Under the proposed new rules, which introduce the concept of non-resident financial arrangement income (**NRFAI**), the ability to defer an NRWT liability on a related party debt will be limited and should more closely align with the income

tax deduction (calculated under the financial arrangement, or FA rules) available to the borrower for that interest.

The NRFAI rules introduce a deferral calculation performed from the end of the second year of a FA. The calculation compares interest deductions available on that FA up to the end of the year immediately prior to the year the calculation is being performed with interest payments made on the FA in the years up to the end of the year of calculation, plus any interest payments made after the balance date but before the NRWT is due (being within the third month following balance date). This approach recognises that interest may often be accrued up to year end then paid shortly thereafter, and does not intend to alter that type of arrangement – more significant deferrals are targeted. If total interest payments divided by total deductions is less than 90%, NRFAI arises and NRWT will be payable.

In a simple example, say a loan was taken out in late 2018 with a non-resident related party, after the enactment of the Bill. The borrower has a 31 March balance date. At the end of the second income year following the creation of the loan (the 2020 income year) the New Zealand borrower must compare the interest deductions available on the loan for the 2019 year (the year immediately before 2020) with the interest payments made in the 2019 and 2020 income years plus any that might have been paid up to 20 June 2020 (the due date of the NRWT on the NRFAI if any is due). If the interest payments made exceed 90% of the interest deductions



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available then no NRFAI arises and NRWT will not be payable. However if the interest payments made are less than 90% then the shortfall to the 90% amount is deemed NRFAI and is liable to NRWT.

The Bill introduces a de minimis level of total expenditure under all related party debts of the borrower and any companies in the same group of companies in the prior year of \$40,000. In this case no NRFAI can arise.



A number of submissions were made on the Bill, ranging from the popular submission that the reforms shouldn't go ahead at all, to more detailed submissions on how the wording of the proposed legislation could be improved. Some comments in the Official's Report, as well as changes made to the legislation as a result of these submissions include:

- Clarifying that the new NRWT rules are only intended to apply to arrangements that provide funding, not arrangements such as interest rate or foreign exchange swaps, or collateral held as security on a derivative.
- Clarifying and improving the terminology used in the new rules by referring to a "borrower" and a "lender" rather than "Person A" and "Person B".
- Undertaking to clarify a number of aspects of the new rules by publishing examples in a *Tax Information Bulletin* after the legislation is passed. (It is always preferable that legislation can be understood on its own without extra explanation, but it appears these particular rules will not be).

Submissions that the new rules are overly complex were not addressed by Officials in the Report. Further, alternative suggestions to the proposals made by submitters, such as a targeted anti-avoidance rule or denying interest deductions until NRWT is paid were rejected by Officials (partially, and somewhat ironically, on the basis that they would be too complex).

Although taxpayers may not need to adjust their current practices following the enactment of the new rules, they will still need to understand them, perform the required calculations, and document the outcome of the calculations in order to support their tax position.

The deferral calculation can only create NRFAI after the end of the second year of a financial arrangement. In the first year the deferral calculation is deemed to be over 90%. The new rules will apply to existing arrangements on and after the first day of the borrower's income year that starts after the date of enactment. For all other arrangements (i.e. new FAs) the rules will apply from the date of enactment.

Tightening AIL criteria by widening definition of 'related parties'

The Bill also tightens the criteria that must be met in order to pay AIL (at a rate of 2%) rather than NRWT (generally 10% or 15%). AIL cannot be paid on loans between related parties and the changes address the concern that parties are structuring around the rules to pay AIL instead of NRWT. The Bill widens the definition of situations that are between related parties, to target back-to-back loans and multi-party lending arrangements interposing a third party to mask what would otherwise be an associated party loan. The AIL rules will also introduce the concept of non-residents "acting together", who will now be related parties (a similar concept exists in the thin capitalisation rules).

The reported-back Bill makes some changes to these proposed reforms.

- The circumstances in which parties will be treated as creating a back-to-back loan are narrowed and the test now requires that the arrangement has the 'purpose or effect' of creating FA expenditure without any corresponding NRWT liability.
- Rules creating an "as agent" tax liability for the direct lender in a back-to-back loan arrangement (i.e. the bank) have been amended to allow lenders to reduce the likelihood that they would have any obligation to pay NRWT on behalf of a borrower.
- Other drafting changes are recommended, including moving the definition of a 'non-resident owning body' from the thin capitalisation rules to the general definition section of the legislation.

Reforms to the AIL rules will apply from the date of enactment of the Bill.

New AIL registration criteria abandoned

The major change to the NRWT/AIL proposals in the reported-back Bill is that strict new limitations on when a security can be registered for AIL have been scrapped. This is a welcome development, as the proposals were very restrictive and would have effectively closed the door to AIL to all but a few New Zealand borrowers.

For further information on these complex rules, please contact our usual Deloitte tax advisor.

A snapshot of recent tax developments



Guidance on seismic assessment costs now finalised

Inland Revenue has finalised Questions We've Been Asked 16/08 – Income tax – deductibility of the costs of obtaining a detailed seismic assessment of a building ("QBWA"). The QBWA considers whether expenditure incurred in obtaining a detailed seismic assessment ("DSA") of a building is deductible. The Commissioner concludes that DSA costs are revenue and therefore deductible in most circumstances. The exception is where DSA costs are incurred as part of an existing capital project, in which case they are capital and non-deductible.

Changes to filing GST online

Inland Revenue's improved My GST online service is available from 7 February 2017. Users of the updated system will be able to:

- File GST returns through myIR accounts;
- Access GST account information, including statements and notices;
- See when GST returns and payments are due;
- Include attachments to support GST returns; and

- Request the transfer of GST refunds to another GST account.

In addition to this, the Tax Administration (Direct Credit of GST Refunds) Order 2016 states that from the same date, GST may be refunded by direct credit under section 184A of the Tax Administration Act 1994 to a bank account nominated by the taxpayer. This means GST refunds can now be paid electronically.

CRS: Draft AEIO guidance released

In preparation for the implementation of the OECD's Common Reporting Standard ("CRS") for the Automatic Exchange of Financial Account Information in Tax Matters, Inland Revenue has released a 189-page draft guidance document. The draft guidance seeks to help financial institutions prepare for their obligations as early as possible and outlines how they will be affected and their CRS responsibilities. Following the enactment of the relevant legislation, a finalised guidance document will be prepared which will take into account public submissions on this draft.

Inland Revenue is inviting feedback or questions by 28 February 2017.

Inland Revenue's internal approach to managing changes or perceived changes to interpretation or practice

On 12 January 2017, Inland Revenue published its internal approach for dealing with changes to (or perceived changes to) its tax and social policy technical interpretation or practice of administering tax legislation. The broad approach has four steps.

1. Identify a potential change or perceived change situation.
2. Establish whether the position being proposed is actually a change from the Commissioner's earlier position or could be seen as a change.
3. Determine how to apply that "new" position if there is a change, or perceived change, in position.
4. Determine how (when and in what format) to communicate the Commissioner's approach to the matter internally and externally.

Generally, where the change results in a position less favourable to taxpayers, the position will be applied prospectively. If unfavourable to taxpayers, the Commissioner may apply the change retrospectively under section 113 of the Tax Administration Act 1994. Prior settlements and time-barred periods are unaffected by subsequent changes in position in either direction.

Inland Revenue finalise piece on the derivation of professional services income

On 20 December 2016, Inland Revenue finalised IS 16/06: When is income from professional services derived ("IS 16/06"). For tax purposes, there are two main methods for determining when an amount of income has been derived: cash basis or accrual basis. While there is no general

rule of law requiring particular professions to account for income using one method or the other, Inland Revenue prescribes a number of factors (based on case law) that should be considered when determining which method is appropriate for a particular business or profession.

Income tax treatment of unclaimed amounts of \$100 or less

On 31 January 2017, Inland Revenue released Public Rulings BR Pub 17/01 Income Tax – Treatment of unclaimed amounts of \$100 or less and BR 17/02 Income tax – Treatment of unclaimed amounts of \$100 or less – amounts held on trust (“Public Rulings”). The Public Rulings, effective from the 2017/2018 income year, provide guidance on when amounts of unclaimed money under section 4(1) of the Unclaimed Money Act 1971 of less than \$100 are derived as income when received in the course of business (not capital in nature).

Draft rulings released on the income tax treatment of the alteration of rights attached to shares

On 6 November 2016, Inland Revenue released two draft rulings relating to the income tax treatment of the alteration of rights attached to shares and the disposition of these shares under the personal property provisions (i.e. section CB 4 of the Income Tax Act 2007). The rulings clarify that altering rights attached to shares does not involve the disposal of shares.

Judith Collins appointed as Minister of Revenue

On 18 December 2016, Prime Minister Bill English announced the new Cabinet line-up and that Judith Collins has been appointed as the Minister of Revenue (replacing Michael Woodhouse).

BEPS update

A number of BEPS-related documents have been released, including the following.

- An updated version of the BEPS Action 4 report, which includes further guidance on the design and operation of the group ratio rule and issues specific to the banking and insurance sectors.
- A discussion draft on the follow-up work on the interaction between the treaty provisions of the report on BEPS Action 6 and the treaty entitlement of non-CIV funds
- Key details of jurisdictions’ domestic legal frameworks for CbC reporting (related to BEPS Action 13).
- Additional interpretive guidance on the CbC reporting standard (related to BEPS Action 13).

Commissioner’s interim operational position on calculating PAYE on non-resident seasonal workers’ holiday pay

Inland Revenue has released the Commissioner’s interim operational position on calculating PAYE on non-resident seasonal workers’ holiday pay. Under the position, a non-resident seasonal worker should be subject to the “NSW” tax code and attract a PAYE withholding rate of 10.5% on their New Zealand-sourced employment income.

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