## Connecting you to the topical tax issues

Tax Alert

May 2018

# New Zealand GST on low value imported goods announced

By Robyn Walker

**Discussion Document Released**

Non-resident retailers selling to New Zealand consumers will be required to register for and charge New Zealand GST.

Following the introduction of an offshore vendor registration for non-resident suppliers of "remote" services in 2016, it is now proposed to have a similar system for suppliers of low value goods to consumers in New Zealand from **1 October 2019**. The new rules would apply to offshore suppliers who make supplies (or expect to make supplies) of goods to New Zealand end consumers of NZ$60,000 or more in a 12-month period. Electronic marketplaces and re-deliverers will also have a requirement to register and comply with the new rules.

## In this issue:

Low value goods will be defined as imports with a customs value of NZ$400 or less (excluding GST). Tariffs and cost recovery charges will no longer apply to supplies covered by the new rules (alcohol and tobacco are excluded from these rules).

Under the current GST rules, all sales by non-residents of goods on which the total amount of GST and duty is less than NZ$60 per shipment are not subject to GST at the border and no GST is due on the sale. Due to varying rates of duty on goods, there is no single value on which GST does not apply, in some cases it is under NZ$400, and in other cases only goods under around NZ$230 are not subject to GST currently. The new rules will do away with this distinction and simply focus on whether the value of each good purchased is NZ$400 or less.

The Government Discussion Document is calling for submissions on the proposed rules, primarily focused on ensuring the proposals are workable and do not cause excessive compliance costs. Submissions on the discussion document can be made until **29 June 2018**.

### How will a supplier know if a customer is a New Zealand consumer?

Suppliers will need to charge GST if the destination of the goods is a delivery address in New Zealand.

Offshore suppliers will not be required to return GST on supplies to New Zealand GST registered businesses, nor will they be required to provide tax invoices. There will be an optional rule allowing offshore suppliers to zero-rate supplies to New Zealand GST registered businesses. This approach would allow any GST incurred by the offshore supplier to be claimed back (for example costs of attending trade fairs in New Zealand).

Offshore suppliers will be able to presume that a New Zealand resident customer is not a GST registered business unless the customer has provided their GST registration number, New Zealand Business Number or otherwise notified the supplier of their GST registered status.

If offshore suppliers are making supplies of types of goods that are typically consumed only by businesses, it may be possible to seek agreement from Inland Revenue that it can be presumed all customers are GST-registered businesses. This rule already exists for the existing remote services rules.

### Non-resident marketplaces

When certain conditions are satisfied, an operator of an online marketplace may be required to register and return GST on supplies made through the marketplace, instead of the underlying supplier.

It is proposed that a marketplace would be required to register when customers would normally consider the marketplace to be the supplier, and this is reflected in the contractual arrangements between the parties; for example, if the marketplace authorises the charge to the customer, authorises delivery to the customer, or sets any of the terms and conditions of the transaction.

### Re-deliverers

Catering to the needs of New Zealand consumers who want to purchase from retailers who won't ship to New Zealand, there are now a range of businesses who create local delivery addresses and then ship the goods to New Zealand. There are also personal shopping services available.

These businesses will be liable to register for GST and will need to collect the 15% GST on the value of the goods as well as their services (regardless of whether this includes international transport).

The sting in the tail for customers using re-delivery services is that they are could end being double taxed with New Zealand GST being added to a supply which may have also had a domestic sales tax applied due to the local delivery address being supplied to the supplier.

### Supplies above NZ$400

Where the value of an individual good exceeds NZ$400 then the current rules will continue to apply, and rather than the supplier charging GST, GST (and any applicable duty) will be collected at the New

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**NZ$60,000 is equivalent to:** AU$56,000; US$42,300; £30,800; €35,000, CNY268,100

**NZ$400 is equivalent to:** AU$374; US$282; £205; €233; CNY1787

Zealand border, with the purchaser unable to collect their goods until the tax is paid.

If multiple goods are purchased in one transaction, with the total transaction value exceeding NZ$400, then GST should be charged on all individual goods costing less than NZ$400. For example, if 6 items costing NZ$200 each are purchased (NZ$1200 total), GST of NZ$180 should be charged by the offshore supplier. The purchaser will likely need to show evidence to New Zealand Customs that GST had already been charged on the consignment.

## Compliance requirements

Offshore suppliers who are required to register under these rules will be able to apply for a simplified "pay-only" registration basis, or alternatively may undertake a full registration allowing them to claim back any New Zealand GST incurred in making New Zealand sales.

Offshore suppliers who are already GST registered under the remote services rules do not need to separately re-register for these new proposed rules.

GST returns and payments will be due quarterly (March, June, September, and December).

## Key issues for suppliers

Suppliers who sell low value goods to consumers in New Zealand should start thinking about how the new rules could impact their business.

A range of issues will need to be considered and addressed before the rules take effect including:

- Can total sales be easily tracked by jurisdiction?
- Will the level of supplies to New Zealand end consumers exceed the registration threshold?
- What type of supplier are you and what specific rules will apply – actual supplier, online marketplace operator, or re-delivery service?
- What modifications would you need to make to your website or business processes in order to determine whether New Zealand GST should apply?
  - Determining the delivery address of the customer
  - Determining whether the customer is an end consumer or a GST registered business
  - Determining the NZD value of the transaction
  - Being able to remove any local sales tax and replacing it with 15% GST
  - Including freight charges when calculating GST
  - How will returned or replaced goods need to be treated for GST purposes?
  - Do invoicing processes need to change
- Based on the level of expected supplies, what reporting period and compliance obligations will apply?
- Does the business wish to continue shipping to New Zealand or effectively outsource the compliance to a marketplace or re-delivery businesses?

For more information please contact a Deloitte tax specialist.

# Buyer beware: ring fencing may be here

By Hiran Patel and Brendan Ng

On 29 March 2018 Inland Revenue released an officials' issues paper Ring-fencing rental losses (the "issues paper") (available here) outlining proposals to introduce loss ring-fencing on residential properties held by "speculators and investors". The Government intends for these proposals to 'level the playing field' to make the tax system fairer, particularly for personal home buyers and individuals looking to buy their first home. While at first glance these proposals are aimed at property held by "speculators and investors", they will in reality affect everyone that owns residential rental property.

These ring-fencing proposals come off the back of the recent extension to the bright-line test for residential property (effective from 29 March 2018), from two years to five years, and are further weapons in the Government's arsenal for its crackdown on property speculation. For more details on the change to the bright-line test and how it will affect you and your properties, please see here, and for more details on the ring-fencing of rental losses, read on.

### What do the ring-fencing proposals mean for me?

It is proposed that you will no longer be able to offset tax losses from residential properties against your other income (such as salary or wages, or business income) to reduce your overall income tax liability. You will however be able to use your losses on a "portfolio basis" if you own multiple rental properties. This means any losses from residential properties can be offset against income you earn from your residential property portfolio (but only your residential property portfolio). This means that you will need to track the profit or loss you make on each of your rental properties, excluding your main home, and only apply any of these losses to:

- Future residential rental income across your portfolio; or
- Taxable income on the sale of any residential land.

Any remaining losses would stay ring-fenced to be used in the future against this type of income.

Note that the rules only apply to residential land, being land with a dwelling on it (or for which there are plans to build a dwelling on it) and bare land that may have a dwelling built on it under the relevant local rules. Residential land does not include farmland or land predominantly used as business premises but it does include overseas land. The definition of "residential land" will be the same as what is used for the purposes of the bright-line test.

If these new rules are imposed, it will be intriguing to see if behaviours are changed and in particular whether there will be a tendency in future to invest in commercial property (or other types of investment that provides a deduction against your income), given it is not captured by these rules.

### Are there any exemptions?

The rules are not proposed to apply to:

- A person's main home (i.e. the home you are predominantly living in and with which you have the greatest connection);
- A property subject to the mixed-use asset rules; or
- Land held on revenue account by a land-related business.

The mixed-use asset exemption means that if you own a bach / holiday home that is sometimes rented out and sometimes used privately, this will not fall under the rules.

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Special rules will be put in place to ensure that trusts, companies, partnerships and look-through company structures cannot be used to get around the ring-fencing rules

Land held by land-related businesses will also not be captured by the rule. A land-related business is one that is involved in development of land, division of land, building, or land dealing. The question of whether you fall into the category of a land-related business is another new consideration.

It is also worthwhile noting that special rules will be put in place to ensure that trusts, companies, partnerships and look-through company structures cannot be used to get around the ring-fencing rules.

### When do these rules apply from?

These loss ring-fencing rules are still in proposal form – this means that they may still change, for better or worse! The issues paper notes that it is proposed to apply the new rules from the start of the 2019-20 income year, however, the actual implementation of this is still up in the air.

Inland Revenue would like feedback on whether the rules apply in full from the outset, or whether they should be phased in over two or three years. For example in a 2-year phasing scenario, 50% of residential investment losses could be used to offset other income in 2019-20, and in 2020-21 no offsetting would be allowed against other income (only against residential rental property income).

### What are the consequences of these proposals?

The issue being addressed here is the supposed advantage (and perceived unfairness) that investors/speculators get by being able to use their losses from rental properties to subsidise their mortgage (through reduced tax on their other income sources), thereby enabling them to outbid owner-occupiers for properties.

Whether these proposals will address this issue remains to be seen. It has been noted in the past that previous ring-fencing regimes have proven not to be as watertight as they are intended to be, and that the lack of tax attributable to rental investments is not only limited to properties funded by debt. However, what we do know is that these proposals will add more compliance costs and you will now need to carefully track losses and profits from your rental properties to ensure that these are only used as allowed. You will also need to separately track any rental losses carried forward.

This will be an issue for companies and trusts where any residential rental properties held are incidental to their business. It is not currently clear how the rules will apply where residential accommodation is provided to employees (particularly if provided for no rent or below market value, i.e. there is no income). It is also not explicitly stated in the issues paper that the rules only apply to residential land owned by the taxpayer (i.e. could it apply to employers who have leased residential premises for employees).

A further issue is raised around investors with just one property (i.e. the mum and dad investors), who then end up selling on capital account. In this situation there may be losses that end up being trapped in respect of this property, with the only option to absorb the losses being to purchase another rental property that generates income – however no concession is allowed for this in the proposals as they currently stand.

Further, with these proposed new rules in play, will we see landlords less prepared to spend money on their properties (to avoid losses) to the potential detriment of their tenants?

### So how can I have my say on these proposals?

If the operation of these proposed rules will affect you, the submission close date of **11 May 2018** should be firmly locked in your diary. The proposals are only in draft form and any feedback can help to iron out any issues you may have to make the proposals workable, and potentially reduce compliance costs that will arise from having to ring-fence losses from rental properties.

If you are preparing your own submission (which can be as short and concise as you like), these can be sent to Inland Revenue at policy.webmaster@ird.govt.nz. Please contact your Deloitte tax advisor if you would like more information on this.

# Australia's GST on low value goods - what you need to know

By Sarah Kennedy and Raquel Prieto

Just like New Zealand, Australia now applies GST to digital products and services imported by consumers. In addition to this, GST will apply to low value goods imported by consumers into Australia from 1 July 2018.

To put this into perspective, if an Australian consumer downloads an e-book, this download is currently subject to GST. As of July 2018, if the same person buys the hard copy of the same book, GST will also apply.

### Who should know about these rules?

Businesses who export goods to Australia are the main people who should consider these rules. Anyone who buys goods online which will be delivered to Australia will also be affected - think of the birthday and Christmas presents of New Zealand goodies that you buy online and get delivered directly to friends and relatives living in Australia.

Understanding the pros and cons of the Australian regime will give you a head start on what your potential submission areas might be for the NZ low value goods discussion document that was issued on Tuesday.

### Imports of low value goods are affected, but what will exactly change?

Currently only goods above A$1,000 are taxed at the Australian border (with the exception of alcohol and tobacco). Australian GST on importations over A$1,000 is assessed at the border and paid by the importer prior to release. This will remain the same under the new rules.

As of July 2018 Australian GST will also apply at the point of sale to physical goods with a customs value of under A$1,000 imported by consumers into Australia if the vendor's total supplies exceed the A$75,000 registration threshold.

The Australian Tax Office ("ATO") is predicting that around 150 New Zealand companies will make supplies in excess of the annual A$75,000 threshold and need to register for GST in Australia. Broadly the three types of registrants will be exporters, electronic distribution platforms ("EDPs") and re-deliverers.

EDPs and re-deliverers are deemed to be suppliers for the purposes of these rules and are required to return the GST on these sales. Complying with the new legislation is proving to be tricky for EDPs meaning that some EDPs have publicly announced that they are considering turning off the ability for Australians using their site to purchase from overseas. Time will tell whether these new rules actually impact on Australian's ability to purchase goods from such sites.

### New Zealand suppliers importing goods into Australia

If your annual supplies to Australian consumers exceed A$75,000 you will need to:

- Register for GST before 1 July 2018 under the standard or simplified registration method
- Charge GST on sales of low value imported goods to consumers (unless they are GST-free supplies such as certain fresh food or input taxed supplies)
- Lodge returns and pay GST to the ATO.

If the only reason for registering in Australia is the new rules, you can apply for a simplified registration, and file quarterly GST

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returns. The ATO has a 24 hour turnaround time for simplified registrations. The catch with simple registration is that this is a payment only system, so no GST credits can be claimed and you are not able to issue tax invoices to purchasers (as simple registrants have an ATO reference number rather than an ABN). Instead, suppliers can issue low value goods receipts containing their ATO reference number, which are not required to be in Australian dollars.

The alternative option is to register under the standard rules which allows you to issue tax invoices and claim GST input credits. Registration is a more complex process with detailed information being required. The ATO processes standard registrations within 28 days of the provision of full information so if this is the option you wish to pursue, we recommend that you get your application underway now.

### Complexity in the rules

Although it's quite straightforward to determine if you need to register, we have found that getting your point of sale, invoicing and accounting systems to apply the new rules is not as simple. We discuss a few examples of this complexity below:

- Have you checked that none of your supplies are GST free or input taxed supplies under the Australian rules? No GST should be charged on these supplies.
- How are you separating business customers from consumers? Does your system require business customers to provide their ABN number, GST registration status and confirmation that the goods will be used in their business?
- How will you make the pricing clear on your website, will Australian customers see prices inclusive of Australian GST?
- How will consignments be dealt with? If low value items are consigned together in one parcel worth over A$1,000 duties will be paid at the border. You will have unhappy customers if the charge at the border means that they are double taxed.
- Changing website settings may not be enough, do you have customers who call New Zealand stores to arrange for delivery? How will staff process these sales in the point of sale system to ensure that the customer is charged Australian GST? What documents will be provided to the customer using this process (simplified sales receipt or tax invoice in AUD?).
- Will customs documents be completed correctly? It's common for imports to show $0 postage and add the cost of the postage to the cost of the goods, as until now it hasn't been necessary to get the split right on the customs documents. Continuing to do this could mean that goods under $1,000 are incorrectly pushed over the low value threshold resulting in double tax.

# Research & development tax incentive

By Robyn Walker

## Details of tax incentive released

From April 2019 businesses may be eligible for a tax incentive for qualifying R&D expenditure. Now is your chance to have your say on the design of the regime and what should qualify.

On 19 April the New Zealand Government released a discussion paper entitled "Fuelling innovation to transform our economy – a discussion document on a Research and Development Tax Incentive for New Zealand", download it here. The release was a joint affair between the Ministry of Business, Innovation and Employment, Inland Revenue and Callaghan Innovation and seeks public feedback on proposals for implementing a research and development tax incentive to encourage businesses to invest more into R&D.

The key proposals are as follows:

- A 12.5% non-refundable tax credit on eligible expenditure (up to a maximum of $120 million of R&D expenditure each year / $15 million tax benefit) will be available to businesses doing R&D in New Zealand, if they spend a minimum of $100,000 on eligible expenditure within one year. We set out further details of what may be eligible at the end of this article.
- This credit will be available for eligible expenditure incurred from 1 April 2019.
- A business' imputation credit account will be credited by an amount equal to the tax credit, so that shareholders receive a benefit from the tax credit when dividends are distributed.
- The discussion paper suggests two options for incentivising R&D spending above the $120 million cap, being:
  - A ministerial discretion to waive the cap for genuine claims; or
  - To require pre-registration for large claims.

The Government's goal for the R&D tax incentive is to increase R&D expenditure to 2% of GDP by 2027, to create a diverse, sustainable and productive economy. The discussion paper notes that across the OECD, almost all countries have a tax credit as part of their support for R&D, and this tax incentive will be part of wider government support for New Zealand research, science and innovation.

### What is research and development?

R&D will be defined as:

Core activities: those conducted using scientific methods that are performed for the purposes of acquiring new knowledge or creating new or improved materials, products, devices, processes, or services; and that are intended to advance science or technology through the resolution of scientific or technological uncertainty.

Support activities: those that are wholly or mainly for the purpose of, required for, and integral to, the performing of the activities referred to above as 'core activities'.

For those with long memories, the tax incentive has largely been modelled on the R&D tax credit regime that existed for the 2008 income year, however there are

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some modifications to ensure the incentive is appropriately targeted, easily accessible and lessons learnt from 2008 and other international regimes are incorporated.

### What expenditure may be eligible?

The discussion paper sets out two potential approaches for what will be considered eligible expenditure. The first is a simple direct R&D labour costs approach – the focus being on employment of staff performing R&D (this approach may allow a higher tax incentive to be available given it is a much narrower set of eligible costs). The second approach is to include a broader range of direct and indirect costs.

Under this second approach:

- Eligible costs will include salary and wages / payments to contractors directly and actively engaged in core R&D activity; depreciation on tangible property used in conducting R&D, employee training, recruitment, relocation and travel incurred directly as a result of R&D activities, materials incorporated into prototype products and plant, items consumed and the net cost of items processed or transferred in the R&D process and payments to a person for outsourced R&D services.
- There is a proposed allocation of overhead costs under this approach (either based on apportionment or as a percentage of the direct labour costs).
- Some expenditure will be specifically excluded, including interest expenditure, donations / grant funding, depreciation attributable to the time an asset is not used in R&D and expenditure that relates to R&D activities for which the entity conducting the activity has received or could reasonably be expected to receive consideration.

For more potential exclusions (and eligible costs) see the discussion paper.

### Areas for further work

The discussion paper highlights two significant areas where officials will be undertaking further work: software and businesses in tax losses.

Software R&D has become increasingly important – accounting for approximately 40-50 percent of the value of Callaghan Growth grants in the last three years. Officials are considering if there needs to be a variation to the standard definition of R&D to ensure it adequately captures R&D software activity. Special treatment for some activities, such as testing and internal software development, is also being considered.

The proposed R&D tax credit is a non-refundable credit so will not provide value to businesses in tax losses. The discussion document notes that many R&D intensive businesses may be in tax losses in the early years. Currently these businesses can benefit from the Callaghan Growth grants.

Further work will be undertaken with the intention that a modified version of the rules will be available for such businesses from 1 April 2020. In the meantime, Callaghan Growth grants will continue to be available, along with the existing R&D loss cash out scheme, which will remain in place for at least the 2019-2020 income year.

The discussion paper poses a range of questions for businesses to consider. Submissions received will help ensure the final design of the rules is creating the right incentives and will help towards the goal of increasing New Zealand's R&D expenditure to 2% of GDP. Consultation on the proposals is open until 1 June 2018.

Please speak to your usual Deloitte tax advisor for further information about these proposals.

# Employee Share Schemes – It's time to act

By Jayesh Dahya and Patrick McCalman

Changes to the tax treatment of employee share schemes have now become law. It is important for employers who offer these schemes and for employees who are enrolled in them to understand the way the rules will affect them, and how the transitional rules work. The Taxation (Annual Rates for 2017-18, Employment and Investment Income, and Remedial Matters) Act 2018 (the "Act") received Royal Assent on 29 March 2018.

We wrote about these changes in our Tax Alert of May 2017, and the rules haven't changed significantly since then.

## Application Dates

As employee share schemes are long-term arrangements that may have vesting periods of three years or more, there are transitional rules that will preserve the existing treatment for certain employee share schemes.

The new employee share scheme rules do not apply to:

- Shares granted or acquired before 12 May 2016.
- Shares granted before 29 September 2018 (six months after enactment of the new rules) provided the shares were not granted with a purpose of avoiding the application of the new law; and the share scheme's taxing date under the new law is before 1 April 2022.

## Now is the time to act

It is now time for employers with established schemes to consider how their existing schemes operate under the new rules and make decisions on the future of these schemes.

Some things to reflect on include:

- Can we make a further issue / award of shares given the six-month transitional rule?
- Can we simplify our scheme to become a more traditional option scheme given the new rules effectively tax all employee share schemes on the same basis as options.
- The tax accounting treatment for those that report in accordance with NZ IFRS - as employee share benefits (including options) will be deductible to the employer under the new rules.

Given the greater alignment of the tax treatment of a number of existing schemes with the tax treatment of options, we believe that there will be a number of schemes which could benefit from simplifying their structures.

## Overview of the new rules

The following is an overview of the new rules. For more detail refer to our May 2017 Tax Alert. The new rules apply to benefits received under an "employee share scheme".

This covers all arrangements involving the provision of shares in a company to past, present or future employees (or

their associates) if the arrangement is in connection with a person's employment or service. This covers types of arrangements such as loans to buy shares, bonuses, put and call options and transfers to employee trusts. There are some exceptions to this.

### Calculating the taxable benefit

The taxable benefit is broadly the difference between the market value of the shares at the "share scheme taxing date" less the amount paid for them by the employee.

The Inland Revenue has previously issued guidance on methods that can be used to value the shares received under an employee share scheme in CS 17/01 - valuation of employee share schemes There has been no change to this.

Despite submissions seeking an allowance for 'black out periods' where employees are restricted from disposing of shares no allowances have been made on the basis that schemes can be designed so that the shares vest outside the period and that blackout periods are generally short.

### Deductions for employers

Employers will no longer need to structure their employee share arrangements to obtain a deduction for the cost of the shares, for example by acquiring shares on market or by arranging for the purchase of shares from another group entity.

Employers will be allowed a deduction from 29 September 2018 ( six months after enactment of the new rules) for:

- Benefits provided under an employee share scheme that is equal to the amount calculated on the "share scheme taxing date" (i.e. the amount of the benefit that is taxable to the employee).
- Costs associated with the administration and managing the scheme, subject to the usual capital/revenue tests.

Employers who report under NZ IFRS will also need to review the shares or options on issue and consider whether a deferred tax asset will need to be recognised for financial reporting purposes. This will pose some challenges, as it will be necessary to identify the share tranches that are grandfathered, the options that are likely to be exercised before 29 September 2018 (not deductible) and options that will be exercised after this date (deductible).

### Exempt Schemes

There are no significant changes to the proposals regarding exempt schemes.

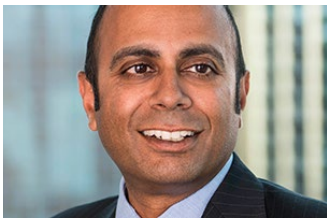
From 29 March 2018, an employer can provide to their employees up to $5,000 worth of shares to their employees per annum at a discount of up to $2,000 per annum. The benefit is not taxable to the employee. However, no deductions will be available to employers other than for the costs associated with the administration and running of the scheme.

Broadly to be eligible as an exempt scheme:

- 90% or more of full-time permanent employees must be eligible to participate in the scheme. If part-time (or seasonal) employees are also eligible to participate all part-time employees (or seasonal employees) must be eligible to participate on the same basis
- If the scheme requires an employee to buy a minimum amount of shares before they can participate, the minimum amount payable can be no more than $1,000 per annum.
- If the employee is required to pay for the shares, an interest free loan must be made available to the employee or there must be an ability for the employee to be able to purchase the shares by way of regular instalments.
- Any minimum period of service required before an employee can participate cannot exceed three years for full time employees.
- Generally, shares have to be held for three years (either by the employee or by a trustee of a trust on behalf of the employee)

It is no longer necessary for employers to obtain Inland Revenue approval to be treated as an exempt scheme. Employers will now need to notify the Inland Revenue of the existence of an exempt scheme using form IR1211 and by 31 May of each year notify the Inland Revenue on form IR1212 details of the grants made to the employees. Existing schemes that have previously been approved by the Inland Revenue will also need to complete form IR1212.

If you have any questions or comments, please contact your usual Deloitte advisor.



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# Are you ready to file your final FBT return?

By Christel Townley & Blake Hawes

As we have crossed the line of 31 March for another year inevitably the topic of tax enters our minds and equally as important, so does Fringe Benefit Tax (FBT). The 2018 fourth quarter Fringe Benefit Tax return or Annual Fringe Benefit Tax return for the year ended 31 March 2018 is due by 31 May 2018, so the time is nigh to turn our attention to the usual trip-ups in the FBT rules and any changes in these rules that have come up in the last year.

### Audits and Reviews: All the more reason to get it right

Inland Revenue has indicated that they are increasing their focus on indirect taxes, specifically FBT, and we have seen them undertaking more audits in this area to find common FBT errors, particularly in SMEs. Over the course of the last year changes have been made to legislation and further interpretation statements have been issued around current legislation that will affect almost all entities preparing FBT returns.

### FBT or PAYE?

Recently we have found a number of instances where employers have not correctly understood whether parts of an employee's compensation should be taxed through payroll, or should be subject to FBT. The general rule is that if the employer has the contractual obligation to pay the benefit then FBT applies, whereas if the employee has the contractual obligation to pay for the benefit (and the employer pays it) this should be taxed through payroll.

Examples of this included reimbursing employees for the cost of a health and wellbeing benefit or home telephone where there is a private benefit to the employee. In both of these examples, clients thought these benefits were subject to FBT but exempt under the de minimis threshold. However they should have been subject to PAYE due to a private benefit arising, as the contractual obligation for these expenses was with the employee. Now would be a good time to evaluate how you provide benefits to your employees and whether they are actually fringe benefits or required to be taxed through payroll.

### Life Insurance

From 1 April 2017 the FBT treatment of life insurance premiums was standardised to ensure that they are all treated as 'specified insurance premiums". Such premiums are explicitly included as a fringe benefit, so must be included in any employer's FBT return if they are paying life insurance policies for their employees.

This removes any ambiguity around whether certain life insurance policies are held not for the benefit of the employee but instead for the benefit of third parties and/or the employer themselves, in which case historically they might not have been subject to FBT.

### Motor Vehicles

As motor vehicles are the most commonly provided fringe benefit, Inland Revenue are increasingly focussing their attention on this area. Inland Revenue released an Interpretation Statement (IS 17/07) in August 2017 regarding the FBT treatment of motor vehicles, aiming to clarify and consolidate the Inland Revenue's operational positions in a number of areas. With this in mind, we would recommend the below issues are considered leading up to the 31 May deadline:

- **Work-related Vehicles** – First and foremost it is important to note that just because the vehicle displays the company's logo does not mean it is automatically fits into the definition

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Inland Revenue has indicated that they are increasing their focus on indirect taxes, specifically FBT, and we have seen them undertaking more audits in this area to find common FBT errors, particularly in SMEs

of a "work related vehicle". There are important restrictions on what a work related vehicle actually is, and it is very easy to fall out of those limits, for example if employees can use it for private purposes.

- **Taking the car home** – It is commonly thought that if an employee takes a car from work to home that no private use of the car has arisen, but this will very rarely be the case, and the onus is on the employer to show that the car is not available for private use.

- **Business travel and the airport carpark** – There are reasonably strict rules around whether a car that has been left at the airport while an employee is on business travel is still "available for private use", and subject to FBT. Fortunately some common sense has prevailed and Inland Revenue has confirmed a vehicle is not available for private use if the employee has been required to take a flight away from home for business reasons. However care still needs to be taken to correctly count the days it is available for private use as there are some subtle differences to when they are travelling on business with the vehicle.

- **Evidence for FBT returns** – The onus of proof for FBT self-assessments falls entirely with the employer. Inland Revenue's FBT Guide contains further detail regarding the evidence required, however the following list is a good starting place;

  - Knowing the motor vehicle (make, model, year of manufacture & registration number)
  - Support for the tax value (fixed asset register) or cost (receipt or lease documentation) of each vehicle
  - Documentation of all exempt days from private use
  - Copies of private use restrictions if in place
  - Workpapers evidencing the calculations of the fringe benefit value obtained including any amounts contributed by the employee.

If you have any questions about the detail of these rules, contact your usual Deloitte tax advisor.

## The relationship between FBT and the entertainment expenditure rules

There can be some confusion over whether the entertainment rules or the FBT rules apply when entertainment is provided to employees.

The simple answer is that in the first instance the entertainment rules override the FBT rules, therefore if you have entertainment expenditure that is caught by the specific entertainment provisions no fringe benefit is deemed to arise on this entertainment regardless of whether employees are present or not. There are some exceptions to this if the employee can choose when to receive or use the benefit, or if the employee doesn't receive the benefit in the course of or as a consequence of their employment.

## Some other important things to remember

- **Applying the de-minimis exemption for unclassified benefits**: If unclassified benefits fall below a threshold ($300 per quarter per employee or $22,500 per employer over the last 4 quarters for all employees) no FBT is payable on those benefits. This exemption threshold includes all associated entities and is a rolling quarterly calculation.

- **Washing up errors in Q4**: Despite the temptation to correct prior quarter errors in a "wash-up" calculation in the final quarter FBT return, this can only be done in a later quarter where the total adjustment to the FBT return does not exceed $1,000. Anything above this threshold should be corrected through a voluntary disclosure.

- **Annual filing threshold**: If you want to file your FBT return annually (if your total gross PAYE and ESCT contributions for the previous year were less than $1,000,000) you need to file an election with Inland Revenue by 30 June for the year you want to change to annual filing (or the end of the first quarter that fringe benefits arise). If an election has not been made yet for 2018, even a small employer will still be required to prepare quarterly returns.

- **To attribute or not, that is the question**: Employers who choose to pay FBT at the standard rate of 49.25% per quarter rather than the multi-rate of 43% can still switch to a full year attribution calculation based on FBT rates linked to the total value of cash remuneration and fringe benefits per employer in the final quarter. This can save material amounts of tax, so is well worth considering.

- **Is it GST on FBT or FBT on GST?** Don't forget to include a GST adjustment on your FBT return if the benefit is subject to GST. Note this doesn't then go on your GST return.

## Conclusion

If you require assistance with your final quarter or annual FBT calculations or wish to explore the benefits of an FBT health check further, please contact your usual Deloitte tax advisor.

## Free FBT seminar

With the FBT season upon us, now is the perfect time to up-skill on recent FBT developments, legislative changes, Inland Revenue focus areas and FBT errors that crop up regularly. We have been running FBT updates around the country in May, and details of seminars yet to come are below. RSVP to reserve your space.

**Auckland**: When: Thursday 17 May, registration 2.45pm, session runs 3pm to 4.30pm. Where: Level 18 Deloitte Building, 80 Queen Street, Auckland Central. RSVP: Lynsey Maguire lymaguire@deloitte.co.nz

**Wellington** (two sessions available): When: Monday 21 May, 3.30pm to 4.30pm or Tuesday 22 May, 9am to 10am. Where: Level 1 Old Bank Chambers, 98 Customhouse Quay, Wellington. RSVP: Meghan Coomber mcoomber@deloitte.co.nz

# How non-residents can get an IRD number without a bank account

By Emma Marr

Now that the rules around non-residents applying for IRD numbers have been relaxed (see here for more detail), Inland Revenue have released more guidance on the information they will require in order to grant such applications.

In future, Inland Revenue will be able to provide a non-resident with an IRD number if they are satisfied with the identity and background of the taxpayer.

Updated guidance on the Inland Revenue website provides that non-resident companies that do not have a New Zealand bank account will be able to obtain an IRD number by providing:

- Certified copy of the Certificate of incorporation
- Certified passport photo page of an executive office holder or director
- Certified proof of residential address of an executive office holder or director
- Certified bank account details if the company is resident in a country New Zealand has a double tax agreement (DTA) or Automatic Exchange of Information agreement (AEOI) with.
- Stock exchange listing if listed
- Names, addresses, tax identification numbers (TIN) of all directors
- Names, addresses, TIN numbers of all shareholders if the company has 5 or fewer shareholders.

The first three items were already required under the old rules, so the new requirement is to provide certified bank account details from the applicants home country. However, Inland Revenue hasn't clarified how a company resident in a country that doesn't have a DTA or AEOI with New Zealand will prove their identity.

Unincorporated entities such as trusts or joint ventures must provide:

- Certified copy of the certificate of registration, copy of trust deed or agreement (as applies)
- Certified Passport photo page of an executive office holder, trustee, partner, executor or owner
- Certified bank account details if the entity is resident of a country with which New Zealand has a DTA or AEOI.
- Proof of residential address of an executive office holder, trustee, partner, executor or owner
- Names, addresses, TIN numbers of executive office holders, trustees, partners, executors or owners

Again, the new requirement is for certified bank account details. In all cases documents need to be certified by a person or entity authorised to certify them under the laws of the relevant country of residence. Examples may include a government, judicial or regulatory body, a lawyer, or a notary public. A certified translation will need to be provided for any documentation that is not in English.

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Inland Revenue do caveat this guidance by saying that there may be situations where Inland Revenue may require more information than outlined above, and will look at these situations individually. Unfortunately they do not give any indication as to what situations this may include, so, as with all new policy, we will no doubt get more clarity as the new rules are tested by real-life examples.

In future, Inland Revenue will be able to provide a non-resident with an IRD number if they are satisfied with the identity and background of the taxpayer

# Post-BEPS transfer pricing legislation refresh requires taxpayer action

By Bart de Gouw and Julian Bryant

In August 2017 the New Zealand Government announced a comprehensive package of tax measures impacting multinationals, which were motivated by base erosion and profit shifting (BEPS) concerns. These proposals are now contained in the Taxation (Neutralising Base Erosion and Profit Shifting) Bill, which is before parliament and expected to be enacted by 30 June 2018.

Within these proposals are significant changes to New Zealand transfer pricing legislation, including modifications to the rules for establishing and defending arm's length amounts for cross-border related party transactions, and a prescribed approach to the pricing of related party debt. Combined with related proposals to expand Inland Revenue's audit powers, and similar developments by tax authorities in other jurisdictions, there is a heightened importance in focussing on transfer pricing issues in the current environment.

We set out below considerations and actions for taxpayers to undertake prior to and immediately following the enactment of the Bill into legislation.

As there is a lot of complexity in the rules including specific exceptions in certain cases, now is the time to be considering potential impacts and whether any action is required

### Limitations to interest deductibility on cross-border associated party debt

As set out in our earlier Tax Alert article (available here), the Bill introduces significant changes to the methods for determining the appropriate interest rate on in-bound associated party loans, which may impact a taxpayer's ability to claim a deduction for interest costs. Specific rules can apply to determine the credit rating of a New Zealand entity (typically one notch below an ultimate parent's credit rating) and to remove "exotic" features of a loan (e.g. terms greater than 5 years).

In advance of the proposed interest limitation rules (set to apply to income years commencing on or after **1 July 2018**) taxpayers should assess the financial impact of the changes on their inbound related party debt in order to plan tax payments and financing arrangements.

The rules will have the most significant impact on taxpayers with loans exceeding NZD $10 million where there is considered be a high "BEPS risk", which will typically occur when any of the following factors are present:

- A high leverage ratio, i.e. a debt percentage exceeding 40%.
- The lender is located in a low tax rate jurisdiction, i.e. where there is a tax rate of less than 15%.

As there is a lot of complexity in the rules including specific exceptions in certain cases, now is the time to be considering potential impacts and whether any action is required.

If you consider you may be impacted by the proposed interest limitation rules, then please reach out to your usual Deloitte advisor or the Deloitte transfer pricing team directly. We have developed an impact assessment tool which may assist in determining potential impacts of these proposed rules.

### Other changes to the transfer pricing rules

The Bill also includes significant modifications to the rules for the calculation of arm's length amounts for non-debt cross-border transactions. Primary amongst the changes is the adoption of the revised 2017 OECD Transfer Pricing Guidelines ("OECD Guidelines") into domestic legislation. The OECD Guidelines reflect global trends towards greater transparency and adopting a substance over form approach.

In relation to transfer pricing arrangements, the revised transfer pricing rules require a determination of arm's length conditions through "accurately delineating" an arrangement, using the approach set out in Chapter 1 of the OECD Guidelines. This is a substance-based approach which requires detailed consideration of the relevant facts and circumstances and often requires, in addition to a review of contractual form, a consideration of which personnel are responsible for performing important decision-making and risk controlling functions. The revised transfer pricing rules also allow Inland Revenue to reconstruct or disregard transactions in cases where the arrangements would not be entered into by third parties operating at arm's length.

With the heightened focus on substance and conduct, it is important for taxpayers to reflect on whether the pricing methodology they adopt in respect of their intercompany transactions is appropriate and reflects the functionality of the relevant businesses. Particular challenges can arise where key management personnel are based in a different location to staff or important assets (including intangible property).

It is also important to reflect on whether appropriate and up to date supporting documentation has been prepared demonstrating that appropriate analysis has been carried out. The OECD Guidelines provide guidance in relation to matters that need to be considered. For example, where there are significant risks impacting the business, it is important to identify which personnel are responsible for specific risk management functions, including decisions in relation to taking on, responding to, and mitigating risks, and who is responsible for financially bearing those risks; and where there are transactions involving

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In August 2017 the New Zealand Government announced a comprehensive package of tax measures impacting multinationals, which were motivated by base erosion and profit shifting (BEPS) concerns.

intangible assets, it is important to identify (as one element) which personnel are responsible for key decisions in relation to the development, enhancement, maintenance, protection and exploitation of the intangibles.

OECD Guidelines requires taxpayers to set out the relevant details in a two-tier documentation format including a group master file (which could be produced by group headquarters in another jurisdiction) and a New Zealand local file, which should include the range of information listed in Chapter 5 of the OECD Guidelines. While the group master file will only need to be prepared in New Zealand for New Zealand owned MNEs, in our experience this two tier documentation requires significantly more work than a one tier/one sided analysis. Inland Revenue has endorsed the two tier approach and has provided no express de-minimis threshold in respect of the preparation of documentation. How these rules will be applied in practice is still uncertain.

Preparing contemporaneous documentation is generally more cost-effective and efficient than dealing with queries from a tax authority down the track. Lack of documentation or inconsistent intercompany agreements also risks Inland Revenue establishing its own view and assumptions in respect of the nature of a taxpayer's business, which could result in lengthy arguments to correct the position. Under the proposed changes to Inland Revenue's audit powers, the onus of proof for demonstrating that a transfer pricing position aligns with arm's length conditions is shifted from Inland Revenue to the taxpayer, and the time bar for transfer pricing matters will extend from four years to seven years. This shifting of the onus of proof will greatly increase the importance of preparing annual documentation on a contemporaneous basis.

We consider that the key actions for taxpayers to take now include the following:

- Consider whether New Zealand entities have, or are likely to have, in-bound associated party debt exceeding NZD $10 million at any time during the year. If so, we recommend considering the impact of the proposed rules as described above.
- Review intercompany agreements and consider whether they accurately represent the substantive economic and commercial relationship between group entities, and whether third parties at arm's length would enter into such arrangements.
- Review supporting documentation prepared for New Zealand entities and consider whether the documentation is in the prescribed form with appropriate detail on the relevant businesses and relationships.

If you would like to discuss with us the most effective way of ensuring that your cross-border transactions are appropriately supported under the new transfer pricing rules, please contact us.

# A snapshot of recent developments


### SPS 18/02 Requests to change a balance date

SPS18/02 sets out the Commissioner's practice for considering requests for the Commissioner's approval to change a balance date for income tax purposes and applies from 1 April 2018, updating and replacing SPS 08/04.

### Calculating home office expenses - square metre rate for dual use of premises

Taxpayers who use premises for both business and private purposes can claim a deduction for some of the expenditure incurred in the business use of the premises. One method available for calculating these costs is set out in section DB 18AA(5) of the Income Tax Act 2007, which (from 1 April 2017) provides a new method for calculating a deduction for premises used for both business and private purposes –the square metre rate method. The Commissioner has published the square metre rate of $41.10 for the 2017-18 income year. Using information obtained from Statistics New Zealand, the Commissioner has calculated the average annual cost of utilities for the average sized New Zealand household (gas/electricity, telephone/mobile/internet services, and house/contents insurance) and divided this sum by the average square metre size of a New Zealand house.

### Draft SPS on effective date of GST registrations

Draft standard practice statement ED0206 sets out the Commissioner of Inland Revenue's (CIR) practice with regard to the effective date of GST registrations. It covers both required GST registrations and voluntary GST registrations. In particular, it explains the factors that the CIR will consider to determine whether a retrospective voluntary GST registration would be approved.

### Depreciation rate for skin therapy machines

The CIR has been asked to consider what depreciation rate should apply for skin therapy machines used for beauty treatments (draft determination ED0205). The Commissioner proposes to add into the "Medical and Medical Laboratory" and "Shops" industry categories, a new asset class, estimated useful life, and general diminishing value and straight-line depreciation rates listed below:

| Asset class | EUL | DV rate | SL rate |
|---|---|---|---|
| IPL, Laser, Ultrasound or RF emitting skin treatment or depilation equipment. | 8 | 25 | 17.5 |

Submissions on these proposed rates can be made until 18 May 2018.

### 'Business' section on myIR is live

The changes that Inland Revenue has made to the new Business (previously GST) section of myIR are now live. Remember this includes a new way to link and delink clients, and the ability to file, pay and amend fringe benefit tax and gaming machine duty, as well as GST. Handy information on how to navigate the new 'Business' section of myIR can be found here.

### IRD number online application change

There have been a number of changes to the online IRD number application. The application has been renamed to "Non Individual Digital Registration", and it includes applications for GST, PAYE, RWT and an IRD number. It is also more comprehensive with more questions asked than was previously the case.

## Have your say on taxing short-term accommodation

Inland Revenue are calling for input on the tax implications of home owners renting out a room or their house through peer-to-peer platforms (such as Airbnb, VRBO and Homestay). Inland Revenue are currently scoping out issues and want to know which GST or income tax questions, issues, or examples taxpayers think they should be addressing in this project? This is your chance to tell Inland Revenue what the important issues are for taxpayers so they can incorporate those into their planning. You can have your say here. Submissions can be anonymous. We welcome this as a pro-active step in identifying where Inland Revenue should best focus their efforts to serve their customers.

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