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# THE TAXATION IMPLICATIONS OF COMPANY LAW REFORM

A DISCUSSION DOCUMENT

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December 1993



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### **DRAFT LEGISLATION**



# PART ONE



# **CHAPTER 1: OVERVIEW**

## **1.1 Purpose of the Discussion Document**

The Companies Bill was introduced into Parliament in 1990. After consideration by the Justice and Law Reform Select Committee the Bill was reported back to Parliament on 15 December 1992. The resulting Act, the Companies Act 1993, was enacted by Parliament in September 1993, and is scheduled to come into effect on 1 July 1994, together with other ancillary measures forming the company law reform package.

This discussion document assesses the implications of company law changes for income tax rules in the various Revenue Acts, in particular the Income Tax Act 1976.

The purpose of this document is to put the Government's perspective on the issues before the taxpaying community as part of the process of undertaking widespread consultation on tax policy changes. The Government seeks to ensure that the reasons for tax policy changes are well understood and that, before they become law, tax policy changes are properly worked through with those in the private sector who will operate under them.

## **1.2 Submissions**

Submissions are invited on the various proposals. They should be addressed to:

The Director  
Legislative Affairs  
Inland Revenue Department  
P O Box 2198  
WELLINGTON

Submissions should be made by 21 February 1994. They should contain a brief summary of their major points and recommendations.

Following a full and thorough consideration of submissions by the Government, legislation to amend the various Revenue Acts to accommodate the new companies regime will be introduced into Parliament. The legislation will be considered by the Finance and Expenditure Select Committee of the House of Representatives. There will be a full opportunity for interested parties to make submissions on the legislation during the Select Committee process.

## 1.3 Background

The major income tax implications of recent company law reforms relate to:

- provisions in company law that allow a company to purchase its own shares;
- company amalgamations and their treatment for tax purposes;
- tax accounting procedures for existing companies when they register under the new companies regime;
- the implications of the repeal of the notions of "par value" and "nominal capital", and "share premium";
- miscellaneous changes to the Income Tax Act where existing concepts and terminology will be redundant or are to be modified by the new companies regime. (For example, the new Companies Act does not retain the current distinction between public and private companies.)

## 1.4 Objective and Scope of this Review

The objective of this review is to revise those aspects of taxation law that require amendment because of the linkages between company and taxation law. The review is not a complete revision of company taxation.

The Government desires to see taxation law integrate well with revised company law rules. While there is no desire to see taxation provisions inhibit the willingness of companies to take advantage of any increased flexibility that company law changes may confer, the need to maintain the integrity of the tax base must be given due weight. It is unrealistic to assume that because company law changes may increase the ability of companies to restructure or return funds to shareholders, tax imposts on such activities should be removed. Tax rules must be designed to achieve an appropriate balance between the competing considerations of maximising commercial activity and maintaining robust and fair taxation rules. Furthermore, the Government seeks rules that provide certainty and that impose as few as possible compliance costs on taxpayers in their day to day operations.

Existing tax rules which govern company distributions have also been reviewed. There are significant weaknesses in existing rules designed to prevent companies substituting tax-free distributions of subscribed capital for taxable distributions when shares are redeemed or cancelled by an on-going company. The current anti-dividend substitution rules are set out in section 4A(1)(c)(ii) of the Income Tax Act. Weaknesses include:

- The uncertain nature of existing rules. There is considerable uncertainty about the circumstances in which existing anti-dividend substitution rules apply and the exact meaning of the words used in the provisions. Consequently, the rules are difficult to apply in practice.
- Inadequate marshalling rules. Existing rules provide opportunities for companies to attribute the entire amount of a distribution to tax-free reserves even though taxable reserves remain in the company. This effectively allows tax-free reserves to be distributed first.

These weaknesses would be aggravated by the greater ease with which shareholders will be able to access the capital of a company under the new Companies Act.

In addition, existing rules aimed at preventing reserves that are taxable on distribution from being converted into tax-free reserves through share for share transactions are not completely effective. These rules include the restrictive definition of "qualifying share premium".

In order to address the weaknesses of the existing rules, this discussion document proposes new rules that:

- define clearly when distributions made by way of share repurchases, cancellations or redemptions are deemed to be dividends;
- modify the averaging formula that defines the portion of a distribution that is tax-free on the repurchase or redemption of shares, or liquidation of a company;
- define additions to subscribed capital where shares are issued either:
  - directly or indirectly in consideration for the acquisition of shares in another company; or
  - in circumstances where the subscription for that issue is funded by the payment of tax-free inter-corporate dividends by the issuing company.

The background to these proposals is described in more detail later in this report.

## 1.5 Outline of the Document

This document is set out in two parts. Part One comprises five chapters and details the major tax implications of company law changes and proposed tax policy responses. Part Two contains draft legislation and explanatory notes to the legislation.

An overview of the significant implications of proposed changes to companies legislation on current tax rules is outlined below. The issues are discussed in more depth in succeeding chapters.

### ***1.5.1 Share Repurchases and Related Issues (Chapter 2)***

From a tax perspective, proposed changes to company law will have their most significant impact on the tax treatment of company distributions. A key change is that companies will be able to purchase their own shares. Sections 58 to 67 of the new Companies Act provide that a company may purchase its own shares subject to:

- the company's constitution containing a power to repurchase;
- the solvency test;
- the repurchase being fair and reasonable to the company and its shareholders;
- no material information being withheld from shareholders;
- shareholders receiving advance advice of the repurchase (with an exception for small repurchases made on the stock exchange).

Repurchases can be initiated by the company only if the repurchase is made on:

- a **pro rata** basis, that is, an offer is made to all shareholders to acquire a proportion of the shares that would, if accepted, leave unaffected relative voting and distribution rights (section 60(1)(a) of the new Companies Act); or
- a **selective** basis, that is, an offer is made selectively to one or more shareholders to acquire shares (section 60(1)(b) of the new Companies Act); or
- a **stock exchange**, so giving all shareholders the same opportunity to sell some or all of their shares (sections 63 and 65 of the new Companies Act).

In all cases, shares are cancelled upon repurchase.

A company may repurchase on the stock exchange, without prior notice to its shareholders, up to 5 percent of its shares in any 12-month period. However, it must advise its shareholders of any such repurchase within 10 working days of the repurchase occurring.

A share repurchase may also be initiated by a shareholder under the buy-out of minority shareholder provisions in section 110 of the new Companies Act. A shareholder can require the company to repurchase his or her shares if:

- The shareholder casts all his or her votes against a resolution (passed by other shareholders) to:
  - adopt or revoke the company's constitution;
  - alter the company's constitution to impose or remove a restriction on the activities of the company;
  - approve a major transaction (defined in section 129 of the new Companies Act);
  - approve an amalgamation; or
- The shareholder does not sign a shareholders' resolution made in accordance with section 122 of the new Companies Act. Such a resolution must be signed by at least 75 percent of the company's shareholders representing at least 75 percent of votes entitled to be cast on that resolution.

A company may arrange for the shares it is required to repurchase to be acquired by another party.

The basic issues with respect to the tax treatment of share repurchases discussed in Chapter 2 are:

- determining the reserves from which tax-free distributions resulting from share repurchases can be funded (referred to as "tax-free reserves");
- determining when distributions by way of repurchases can be attributed to tax-free reserves;
- the mechanism for taxing the dividend component of share repurchases.

At present companies are able to cancel their own shares, subject to High Court approval, or, in the case of redeemable preference shares, redeem their own shares. However, the new Companies Act provides greater scope for companies to provide a cash return to shareholders in a form other than an ordinary dividend. This follows from the relaxation of the constraints on share repurchases or cancellations and the removal of the current company law requirement to distinguish between reserves that consist of subscribed capital and other reserves.

### ***1.5.2 Amalgamations (Chapter 3)***

The new Companies Act provides that two or more companies may amalgamate and continue as one company, which may be one of the amalgamating companies or a new company. Broadly, the procedure to amalgamate requires

the consent of the boards and shareholders of each amalgamating company; there is no court involvement. The consent by shareholders must be by way of special resolution and the amalgamated company must satisfy the solvency test immediately after amalgamation.

A short-form amalgamation procedure is provided under section 222 of the new Companies Act for a wholly-owned subsidiary that amalgamates with a parent or two wholly-owned subsidiaries that amalgamate. Under the short-form procedure, an amalgamation may be approved solely by the boards of each amalgamating company agreeing to the amalgamation, provided that the solvency test is still met.

Following approvals, an amalgamation proposal is registered with the Registrar of Companies, who thereupon issues an amalgamation certificate. The certificate specifies the effective date of amalgamation.

The new Companies Act provides that all assets and liabilities of the amalgamating companies are vested in the amalgamated company. However, shareholders of amalgamating companies must agree to the terms of the amalgamation, and shares and rights of shareholders in amalgamating companies are not necessarily converted into shares and rights in the amalgamated company. Where one amalgamating company holds shares in another amalgamating company, those shares must be cancelled for no payment when amalgamation becomes effective.

Under current tax law, there are full tax consequences on the transfer of assets from the amalgamating company to the amalgamated company, and on the exchange of shares in the amalgamating companies for shares in the amalgamated company, where those are held on revenue account. Tax losses and imputation credits are generally extinguished. These consequences follow from an amalgamation being treated in substantially the same manner as a liquidation.

Under the new rules proposed in Chapter 3, amalgamating companies would be able to utilise tax-free asset transfer rules based on the existing consolidation regime. The tax losses and imputation credits of the amalgamating companies will be able to be retained, subject to shareholder continuity and commonality tests being met. Dispositions of shares occurring under an amalgamation would continue to be assessable to revenue account shareholders.

### ***1.5.3 Tax Accounting Issues (Chapter 4)***

#### *Treatment of Reserves*

Company law reform will remove the concepts of "par value", "nominal capital" and "share premium" on which existing tax law relies. As a result, it is proposed that tax rules be amended to focus on subscribed capital (consisting of the sum of what is now paid-up capital and qualifying share premium). When existing



companies register under the new companies regime, it will be necessary to convert reserve accounts for tax purposes into a form appropriate to the new regime. The treatment in this context of paid-up capital, including bonus issues, share premium and capital redemption reserves, is covered in Chapter 4.

Also considered in Chapter 4 is the carry over into the amended dividend definition applying after the enactment of company law reform of an equivalent of the concept of "qualifying share premium". Existing rules limit the range of share premium eligible for tax-free distribution to "qualifying share premium". This limitation is aimed at preventing companies from creating, via share swaps, share premium reserves on take-overs or mergers from which tax-free distributions can be made.

Tax accounting issues relating to amalgamation are also addressed, as is the extent to which subscribed capital can be derived directly or indirectly from exempt inter-corporate dividends.

#### *Recovery of Excess Distributions*

The new Companies Act provides in section 56 for a company to recover distributions made to shareholders where such distributions breach the solvency test. The recovery of distributions from shareholders is likely to be a rare event, since repayment by the shareholder would not be required if the unauthorised dividend was received in good faith, and it would be unfair to require repayment having regard to the altered circumstances of the shareholder. The discussion document outlines how current income tax rules will need to be amended in order to cater for situations where taxable distributions are later returned to a company.

#### **1.5.4 Miscellaneous Issues (Chapter 5)**

In addition to the issues outlined above, there are also a number of consequential changes to the Income Tax Act resulting from terminology changes in company law. A number of the existing definitions, largely relating to defining a shareholder's interest in a company, rely on the concepts of nominal and paid-up capital that, as previously noted, will have no relevance under the new companies regime.

Also, the removal of the private/public company distinction means that changes will be necessary to those provisions of the Income Tax Act that rely on the definition of "private" and "public" companies.



# CHAPTER 2: SHARE REPURCHASES AND RELATED ISSUES

## 2.1 Background

The new Companies Act treats share repurchases as a distribution. When making a distribution under the new Companies Act a company is subject only to restrictions in the company's constitution and to satisfying the solvency test in section 4 of the Act. The term "distribution" is defined widely in section 2 of the Act to mean:

*"(a) the direct or indirect transfer of money or property, other than the company's own shares, to or for the benefit of [a] shareholder; or*

*(b) the incurring of a debt to or for the benefit of [a] shareholder;*

*in relation to shares held by that shareholder, and whether by means of a purchase of property, the redemption or other acquisition of shares, a distribution of indebtedness, or by some other means."*

There is no longer a restriction as to the fund or reserve out of which a distribution can be made. A distribution can now be made out of capital. The definition of a distribution recognises that, regardless of its form, a distribution by a company reduces the cushion of reserves available to creditors. The new Companies Act distinguishes between distributions in the form of "dividends" and other distributions, such as share repurchases and certain redemptions, because the administrative rules governing the payment of dividends differ in detail from those that govern other forms of distribution. However, the economic equivalence of all forms of distribution made by an on-going company is recognised so that all distributions, whatever their form, are subject to the same solvency test.

## 2.2 General Considerations

Share repurchases as provided for in the new Companies Act are not contemplated under existing tax rules. The closest existing analogy to a share repurchase is a share cancellation. Both reduce the capital of the company. Until such time as a company is registered under the new Companies Act, if it wishes to reduce its capital it will only be able to cancel shares. Accordingly, the treatment applied to cancellations should, as far as possible, parallel the tax treatment of repurchases.

The Valabh Committee considered the appropriate treatment of share repurchases in its two reports on *The Taxation of Distributions From Companies*, released in November 1990 and July 1991. The Committee proposed a

mechanism by which the dividend component of share repurchases could be subject to tax. A number of submissions to that Committee argued that, except in certain circumstances, a repurchase should be treated in the same way as a sale of shares to a third party. That is, no tax consequences should arise if the shares repurchased were on capital account. Furthermore, submissions argued that to tax the dividend component of a share repurchase would mean that it would never be prudent for a company to repurchase its shares because it would have to pay a premium on the market price. This was seen as undermining the objectives of proposed company law reform.

The Valabh Committee considered these objections but maintained its earlier view that there is little difference in principle between the distribution of retained earnings as an ordinary dividend and the distribution of retained earnings by way of a share repurchase by a company. The effect on the company's retained earnings and shareholders' total wealth is the same in each situation. It logically follows that the overall tax consequences of each type of distribution should be identical. If this were not the case there would be an incentive for companies to characterise dividends as share repurchases (Valabh Committee (1991) p33).

The Valabh Committee also rejected the argument that treating share repurchases and other distributions in a consistent manner would undermine company law reform. As the Committee noted, this is no more true than to say that taxation of ordinary dividends undermines company law provisions allowing the payment of such dividends (ibid, p33).

The Government agrees with the Valabh Committee's general conclusions. There are three key questions to consider, however:

- What part of the repurchase proceeds should be tax-free in the hands of the shareholder? In particular, should distributions funded from capital profits be tax-free when made through repurchases?
- What ordering rule is to be used to determine the portion of the amount paid on the repurchase of shares that is tax-free?
- What is the most appropriate mechanism for taxing the dividend component of amounts distributed through a repurchase?

These issues are discussed below.

## 2.3 Current Rules For Taxing Share Cancellations

### 2.3.1 The Current Rules

Under current income tax law:

- A payment made to shareholders on cancellation of a share during the life of a company is taxable unless it represents a return of capital.
- Cancellation payments funded from a company's capital gains are taxable (except on a full liquidation). This is consistent with the rules for dividends generally. Dividends funded from capital gains are taxable.
- Rules apply to determine the contributed capital amount and qualifying share premium amount per share. This is the amount that can be returned tax-free. Where the company is being liquidated, capital profits can also be distributed tax-free. The formulae for determining these tax-free components are outlined in Annex 2.1.
- Rules also apply to determine when a distribution is in substitution for a dividend, in which case the full amount is taxable. These rules are contained in section 4A(1)(c)(ii) of the Income Tax Act.

Dividends are easily distinguished conceptually from a return of subscribed capital from a company to its shareholders. They are normally seen as a distribution of the profits of the enterprise to its owners. In a perfectly operating company tax system, imputation credits equivalent to full company tax would be attached to dividends. By contrast, a return of subscribed capital would be expected to be an unusual one-off event reflecting a distinct feature of a company at any point in time. To the extent that a company distribution to a shareholder consists merely of a return of the shareholder's investment, the distribution should not constitute a taxable dividend. While it is conceptually clear, there are difficulties in applying this "in principle" distinction in the operating commercial environment.

First, the funds actually held by the company are not necessarily equal to the amount an individual shareholder has invested. Many shares are likely to have been purchased on the secondary market at a price different from their issue price. With bonds, this issue is dealt with by taxing as income any gain made by the holder on the bond. However, the same treatment applied to shares would result in the taxation of gains on shares held on capital account. The approach adopted for shares therefore is to treat as a return of capital the amount invested in a company with respect to those shares by the original shareholder. Under existing law this amount is paid-up capital for tax purposes. When company law reforms become effective, it will be subscribed capital. The concept of subscribed capital is considered in more detail in Chapter 4.

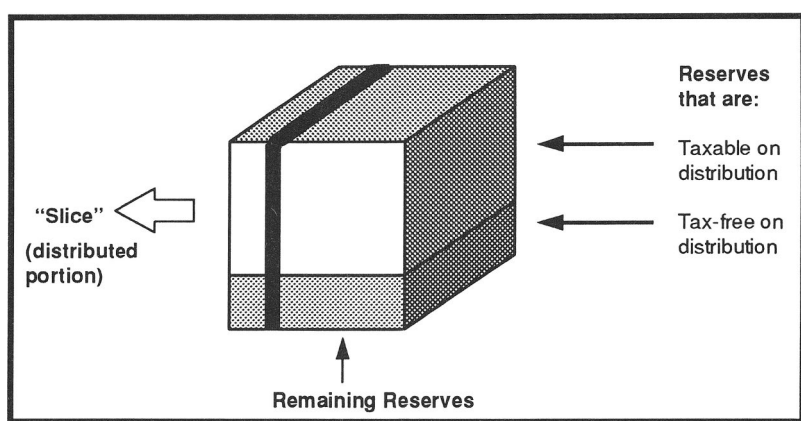
Second, it is not uncommon for companies to issue bonus shares in lieu of dividends, or periodically seek new capital by offering new shares to existing shareholders. As the issue price of the new shares usually varies from the price of the initial shares, shares of the same class represent differing levels of investment in the company. Companies do not necessarily keep records tracing the issue price of specific shares. Thus, tax rules apply an averaging formula to compute the amount of capital attributable to shares in a class.

Third, allowing companies to determine the source of the distribution without constraint (other than in the course of a liquidation) would seriously undermine the dividend tax base since it would allow companies to substitute distributions funded from tax-free sources for taxable distributions of retained earnings.

Consequently, the current rules identify the order in which the funds are sourced. Any amount over and above paid-up capital is deemed to be a distribution of revenue reserves and is taxed. Where the market price is paid for the share, the current rule results in a distribution arising from a share cancellation being deemed to come from both taxable and tax-free sources. This is referred to as the "slice rule". The Government considers the slice rule to be the most appropriate approach to determining the portion of the distribution that is tax-free.

Broadly, the aim of the slice rule is to base the non-taxable and taxable components of the share repurchase proceeds on the ratio between capital and the taxable reserves of the company.

Given the variation in accounting treatments, it is inappropriate to specify for tax purposes reserves that are taxable on distribution. Existing tax rules specifically define tax-free distributions. Distributions in excess of those nominated as being tax-free are taxable. Consistent with this approach, taxable reserves are the difference between the tax-free reserves and the market value of the company's shares. Existing rules on the full liquidation of a company reflect this treatment. Under those rules, all the proceeds of a distribution on a full liquidation (representing the market value of the company's underlying assets at that time) are taxable except for those specifically deemed to be tax-free.



Since any dollar distributed cannot be specifically identified as coming from either tax-free or taxable reserves, the slice rule has the advantage of being "even-handed" by assuming the distribution comes from both sources in proportion to their contribution to total market value.

### ***2.3.2 Problems With Existing Rules***

The existing rules that govern share cancellations have two key problems which give rise to a need to strengthen those rules so that they achieve their intent.

First, while the slice rule applies if the market price is paid for the share, the rules allow a company to pay less than market price. As a result, the entire distribution can be made tax-free by the company paying only the contributed capital per share. Shareholders are not penalised provided their respective interests in the company remain unchanged. Existing rules in practice therefore provide scope for subscribed capital to be distributed ahead of taxable reserves. For tax base maintenance reasons, the Government considers that it is appropriate that the slice rule apply in these circumstances.

Second, the test that determines when a cancellation is in substitution for a dividend is very difficult to apply because it is highly subjective. The test relies on identifying the distribution as being made "regularly, systematically or explicitly" in lieu of a dividend, which is very difficult for the Commissioner to determine. First, there may be some argument that "systematic" does not include a one-off cancellation. A more fundamental problem is that the test requires the Commissioner of Inland Revenue to determine what a company would distribute as an ordinary dividend in any particular year in the absence of an ability to cancel or repurchase shares. This has proved difficult to apply in practice, and in the case of a newly established company, or a company with a one-off gain, the test is particularly hard to administer. Since companies are expected to repurchase shares more frequently than they currently cancel shares, this weakness represents significant potential for dividend tax base erosion.

## **2.4 Proposed Changes**

### ***2.4.1 Distributions Funded by Way of Capital Profits***

#### *General Proposal*

The Government, in determining what proportion of a distribution should be taxed as a dividend, has considered the appropriate treatment of distributions funded from capital profits. As noted above, under existing rules, distributions funded from capital profits are tax-free only when a company is fully liquidated. The Valabh Committee proposed that distributions funded from capital profits also be tax-free when effected by way of a share repurchase or redemption (Valabh Committee (1991), p37). The recommendation related only to non-qualifying

companies. The qualifying company regime, aimed at small incorporated businesses, already provides that distributions funded from capital profits are tax-free when distributed to shareholders.

The arguments advanced by the Committee in favour of relaxing the existing rules and allowing distributions funded from capital profits to be tax-free on a repurchase or redemption of shares were that:

- There is no "in-principle" distinction between an amount distributed by way of a repurchase and distributions on the full liquidation of a company (when distributions from capital profits are tax-free).
- Rules aimed at preventing companies substituting tax-free repurchases for taxable dividends should be sufficient to protect the dividend tax base if the existing restriction is relaxed.

There are some arguments for not relaxing the rules. Under the new Companies Act, repurchases and dividends are subject to broadly similar rules, such as the solvency test, while rules applying on a full liquidation differ significantly. Also, the proposal to allow distributions sourced from capital profits to be tax-free creates an opportunity for on-going companies to provide a tax-free return to their shareholders by way of share repurchases not currently available. This could undermine the dividend tax base. Existing anti-dividend substitution rules are considered inadequate in this regard. The proposal also involves some increase in compliance and administration costs. Implementing it would require rules to attribute distributed capital profits to shares of a company (other than fixed rate shares) repurchased by a continuing company. For their part, companies would need to have adequate records that identify realised capital profits and losses, as well as any past distributions from those sources.

After careful consideration of this issue, the Government has determined on balance to support the Valabh Committee's recommendation that distributions by way of share cancellations or repurchases that are funded from realised capital profits be tax-free, so long as the distribution is of sufficient size to clearly not be in substitution for a dividend. For the reasons outlined above, the Government considers that such a change should be conditional upon the implementation of more robust rules to prevent the substitution of tax-free distributions for the payment of taxable dividends. These rules are discussed further below. Since the new rules will apply to share cancellations, they will affect companies registered under the Companies Act 1955 as well as the new Companies Act.

This change would not apply to fixed rate shares. Distributions upon the redemption or repurchase of fixed rate shares, other than those funded by subscribed capital, would continue to be taxable.



### *Determining the Capital Gain Amount*

As noted above, it is necessary to apply rules to attribute realised capital profits to shares repurchased. Otherwise, there would be little constraint on a company targeting tax-free distributions funded from this source to particular shareholders, such as high-marginal rate taxpayers. The capital gain attributable to shares on a repurchase or redemption would be calculated by simply averaging the total realised capital gain reserves over the number of shares of all classes, other than fixed rate shares, on issue prior to the repurchase or cancellation. Capital gain reserves would be the sum of all realised capital gains, less capital losses and distributions previously funded from such reserves, since the creation of the company.

#### **2.4.2 New Anti-Dividend Substitution Rule**

In light of the weaknesses in the current law, the Government proposes to amend the legislation to achieve two objectives. The objectives are:

- to ensure that the slice rule applies even where less than the market price is paid for the share;
- to incorporate a more robust and effective anti-dividend substitution rule.

#### **2.4.3 Reinforcing the "Slice Rule"**

##### *General Approach*

A company making a share repurchase or redemption, or a distribution on liquidation, would continue to be able to determine the amount that is attributed to tax-free reserves on a similar basis to the current section 4A(1)(c) of the Income Tax Act, but with a key modification.

It is proposed to amend the section to ensure that the tax-free and dividend components of the distribution better reflect the composition of the company's value. As noted earlier, currently companies can make a pro rata cancellation that is entirely tax-free by cancelling shares for their par value despite the market price being many times that amount. Such a strategy could also be possible with off-market repurchases but unlikely with on-market repurchases as shareholders would not sell their shares on-market for less than the market value.

Under the proposed change, where the market value or more is paid for a share, the subscribed capital and capital gain amount in relation to the share could be returned in full. Where less than the market value is paid, those amounts would be reduced as follows:

$$\frac{\text{price paid}}{\text{market price}} \times (\text{subscribed capital amount} + \text{capital gain amount})$$

Section 4A of the Income Tax Act currently refers to the "returned capital amount". This term will be replaced by the term "subscribed capital amount", a concept that will reflect the capital position and shares on issue at any point in time, taking into account all previous capital subscriptions and reductions. The current formula refers to all shares and capital ever issued.

*Example*

Assume a company has 100 shares, all of one class, with subscribed capital of \$0.50 per share. The market value of the company is \$100.00 and its realised capital gain reserves are \$20 (or \$0.20 per share). The company repurchases 70 percent of the shares for \$0.70 each through off-market repurchases. The tax-free component per share would be \$0.49, that is:

$$\frac{\text{price paid}}{\text{market price}} \times \text{tax-free amount} = \frac{\$0.70}{\$1.00} \times (\$0.50 + \$0.20) = \$0.49$$

*Determination of Market Value*

It is envisaged that the Commissioner would exercise a discretion as to how market value would be calculated in the case of repurchases, having already the power to determine the market value of shares in several other contexts. At the request of the Government, the Commissioner has considered ways to reduce compliance costs involved in determining the market value, and is conscious of the need to approve or confirm market values of shares to enable the proposed measures to operate in a satisfactory manner. For example, in the case of non-listed companies it is envisaged that detailed valuations will not be required but that a written valuation by an independent competent valuer will suffice in most cases. This should reduce compliance costs. Submissions as to how to further reduce compliance costs consistent with the general objective would be welcomed.

**2.4.4 Brightline Tests**

*The New Test*

Under the slice rule, amounts distributed by way of share repurchases and redemptions would continue to be tax-free to the extent that they are considered to be returns of subscribed capital or realised capital gains. However, it is proposed to include in section 4A(1)(c) of the Income Tax Act two new tests that would allow this treatment only in circumstances where a "qualifying capital reduction" or a material reduction in a shareholder's interest (a "qualifying

disproportionate reduction") occurs. These tests establish levels referred to as "brightlines". The tests are designed to give a clear, objective determination of when a distribution is a qualifying capital reduction or a qualifying disproportionate reduction as opposed to a deemed dividend. If the tests are not satisfied, the distributions would be taxable in full to the shareholder as dividends.

The tests will apply to repurchases other than "on-market repurchases". The slice rule would automatically apply to on-market repurchases, with the company rather than the shareholder being responsible for meeting the tax imposition (refer to section 2.5 for further details). On-market repurchases would be defined as repurchases where:

- The company acquires the repurchased shares through a broker in a recognised exchange (as defined in section 8B of the Income Tax Act for the purpose of determining interests in companies).
- The seller, as a result, is unaware of the identity of the purchaser at the time the offer to acquire is accepted.

The brightline tests specify that amounts distributed by way of repurchases, redemptions and cancellations (other than on-market repurchases) would be considered to be in lieu of taxable dividends, and would therefore be fully taxable as dividends, in the following circumstances:

- where a repurchase offer is made on a pro rata basis under the terms of the companies legislation and the amount ultimately distributed represents less than 15 percent of the market value of the repurchasing company's shares at the time the company first notified shareholders of the intended offer. To be pro rata the offer must apply to all shares of the company other than fixed rate shares (defined in the proposed section 4A(3) of the Income Tax Act);
- where a repurchase offer is made on a non pro rata basis, a shareholder's proportionate interest in the company after the repurchase or cancellation is more than 85 percent of the shareholder's pre-repurchase/cancellation interest. The shareholder's interest would include the interests of certain persons associated with the shareholder. This test would be applied to the aggregate of all shares in a company, other than fixed rate shares.

Sections 8A to 8D of the Income Tax Act, which measure voting and market value interests, would be used as the basis for establishing a shareholder's underlying interest in a company.

The tests of when a distribution is in lieu of a dividend have been designed to enable companies, for reasons such as downsizing of operations, to fund one-off distributions to all shareholders (or to selected shareholders in the case of disproportionate reductions) partly from tax-free reserves of the company.

The brightlines have been set at levels where it is clear a company would be returning capital rather than paying a dividend. The 15 percent of market value level represents approximately three times typical dividend yields. This represents a reasonable level for a robust anti-dividend substitution rule.

#### *Commissioner's Residual Discretion*

The Commissioner's discretion currently in the law will be rewritten as a backstop measure for use only when taxpayer behaviour defeats the purpose of the new rules.

Where there is either a qualifying disproportionate reduction or a qualifying capital reduction, the distribution will be considered to be in lieu of a dividend only if the Commissioner is of the opinion that the repurchase was made under an arrangement to acquire, redeem or otherwise cancel shares in lieu of the payment of a dividend. The factors to be considered by the Commissioner in this regard are outlined in the legislation.

A circumstance in which this residual discretion for the Commissioner should apply is where a company (likely to be a closely-held company) accumulates earnings until they represent 15 percent or more of the market value of the company. The company then makes a distribution, ostensibly as a result of a downsizing operation, but without reducing any of its core business. Similarly, successive disproportionate reductions that leave the respective interests of shareholders largely unchanged would also run foul of this rule.

#### *Repurchase by Related Company*

It is necessary to include rules to prevent a repurchase being characterised as a sale of shares to a third party by using, for example, related sibling companies or trusts to acquire shares. While it is considered that section 99(5) of the Income Tax Act is likely to catch such repurchases, it would be difficult to apply the section in relation to on-market repurchases, since it is not practical to deem a dividend to have been derived by the vendor. Accordingly, to cover the case of repurchases occurring on-market in the circumstances outlined above (or similar circumstances), a new section 4(12) will be inserted. This in effect provides for a debit to the Imputation Credit Account (ICA) of the company that issued the shares in respect of the dividend component of the repurchase. There would be no tax consequences for the vendor. Under section 4A(1)(cb) the amount paid to the vendor would be excluded from the dividend definition.

#### *Treatment of Fixed Rate Shares*

Fixed rate shares would be excluded from the brightline tests. They are more akin to debt instruments and usually do not carry an entitlement to the reserves of the company. This means that only subscribed capital in respect of such shares would be returned tax-free. The only exception would be when there is a

plan or arrangement to redeem fixed rate shares in lieu of the payment of a dividend on other shares in which case the distribution would be fully taxed as a dividend. An anti-avoidance rule to deal with this situation is included in the draft legislation.

## **2.5 Mechanism for Taxing the Dividend Component of Share Repurchases**

### ***2.5.1 Introduction***

How the dividend component of a share repurchase will be subject to tax will vary according to a number of factors, including:

- whether the repurchasing company is a resident or a non-resident company;
- whether the repurchase occurs on-market or off-market. Since it will not generally be possible for repurchasing companies to identify vendor shareholders at the time shares are acquired through the sharemarket, on-market share repurchases are likely to be from selected shareholders. Pro rata share repurchases will generally be confined to off-market transactions;
- whether the shareholder from whom shares are repurchased is a company, a non-corporate shareholder, a resident or is taxable on gains from the sale of shares.

Each of the above combinations results in different considerations that should be taken into account in determining how best to tax the dividend component of share repurchases. The proposals are discussed in more detail below, and are summarised in general terms in Annex 2.2.

### ***2.5.2 Off-Market Purchases by Resident Non-Qualifying and Qualifying Companies***

#### *Background*

The Valabh Committee made the following recommendations on the appropriate general mechanism for accounting for tax on the dividend component of a share repurchase:

- A company buying back its shares should be subject to fringe benefit tax (FBT) on the dividend component of the repurchase where that occurred on- or off-market.

- The company should be able to debit its imputation credit account (ICA) in satisfaction of the FBT liability.
- If insufficient ICA credits exist to satisfy FBT, then FBT should be actually paid with no credit to the ICA for that payment.
- All vendor shareholders should be exempt from tax on the dividend component of the repurchase price.

The Committee made its recommendations when non-cash dividends were subject to FBT and prior to the removal of the inter-corporate dividend exemption. This latter change means that where a company repurchases from a resident corporate vendor, the dividend component will be taxable. Where this occurs there is some argument that applying the Valabh Committee approach unaltered would operate harshly in relation to repurchases from corporate shareholders. In order to address this concern in respect of off-market repurchases, it is proposed that where shares are purchased by a qualifying or non-qualifying company off-market, the normal dividend distribution rules apply.

#### *Repurchase from Resident Non-Corporate Shareholder*

Where a company repurchases shares from a resident individual, the shareholder will be taxable on the dividend component of the sale proceeds.

Imputation credits may be attached by the company in accordance with ordinary rules, and the dividend will generally be subject to the resident withholding tax regime. This treatment is illustrated in Annex 2.3.

#### *Repurchase from a Resident Corporate Shareholder*

A corporate shareholder would be taxed in the same way as an individual on the repurchase of shares. A credit will arise to the vendor's imputation credit account equal to the amount of any imputation credit, or resident withholding tax credit, attached to the dividend component of the sale proceeds. In this way, the appropriate amount of tax would be levied on dividend income.

#### *Repurchase from a Vendor who Holds Shares on Revenue Account*

The interaction between taxing the dividend component of a share repurchase and taxing gains or losses on shares on revenue account has not been fully evaluated. Any changes that may be proposed as a result of further evaluation will be discussed with interested parties during the consultation period.

The proposal is that a vendor shareholder who holds shares on revenue account would be assessed on profits arising from the sale of the shares. The vendor would also be assessed on the dividend income arising from the repurchase. To ensure that both the dividend and the gain on share sales are not subject to tax, it is proposed that only the dividend component (excluding imputation credits)

and the excess profit over the dividend, if any, should be assessable. Where a loss had been made on sale, it could be offset against dividend income.

#### *Repurchase from a Non-Resident Shareholder*

The purchasing company would be required to deduct from the purchase price non-resident withholding tax on the dividend component of that repurchase price.

#### *Repurchase from Tax Exempt Shareholder*

Where the vendor shareholder is tax exempt, the dividend would be exempt and therefore not subject to RWT. However, imputation credits must be allocated to the dividend in accordance with the imputation rules.

### **2.5.3 On-Market Repurchase by a Resident Non-Qualifying Company**

#### *Background*

Where a company purchases on-market from a shareholder of the company, the normal dividend rules will be inappropriate because:

- The shareholder will be unaware of the identity of the purchaser.
- At the time of the acquisition, the purchaser will not know the identity of the vendor.
- Where shares (representing less than 5 percent of the company) are held by a nominee the purchaser may never know the identity of the beneficial owner of the shares.

The Valabh Committee's recommended approach to taxing the dividend component of a repurchase, outlined above, assumed a link between dividends and FBT. The regime that applied at that time levied FBT on non-cash dividends. This is no longer the case. In view of this, and because a situation in which a company would prefer to pay FBT rather than debit its ICA is unlikely to arise, it is proposed that the legislation simply provide for a debit to arise to the ICA of a company to cover tax due where shares are repurchased on-market.

#### *Repurchase from Resident Non-Corporate*

Where a company repurchases shares from a resident non-corporate, the company would debit its ICA in respect of the dividend component of the repurchase price.

The amount of the debit would be calculated in the same way as resident withholding tax on non-cash dividends. Where the purchasing company has insufficient credits in its ICA to absorb the debit at the time of purchase, it would

make a payment of tax sufficient to square the account by 31 March (without penalty) or 20 June. In almost all circumstances, this payment would offset a future provisional tax liability. The vendor would not be taxed on the dividend component.

### *Repurchase from Resident Companies*

Where a company repurchases on-market from a resident corporate shareholder, the repurchasing company will debit its ICA in payment of tax on the dividend component of the repurchase. Although the shareholder would not be taxed on the dividend component, that amount may be taxed again if it is distributed to shareholders of the vendor.

One mechanism by which this problem could be eliminated is to permit a credit to arise in the ICA of the vendor company. A corporate shareholder who sells shares to the company in which it holds shares would receive the same price for the shares as would have been the case had the shares been sold to a third party. In the former case, however, the shareholder would also receive imputation credits. The corporate shareholder who sells to the company should not be in a better position than one who sells to a third party. When the company sells its shares to a third party, it receives no such credit. Accordingly, allowing a credit to arise is inappropriate.

The other possible solution to this problem is to exempt from the ICA debit mechanism dividends on shares repurchased from corporate shareholders. There are two concerns about such an exemption from the ICA debit mechanism:

- Where shares are owned by a nominee company, the status of the beneficial owner should determine whether tax is payable. If the beneficial owner is a non-corporate, tax should be levied. However, companies will not typically know whether a corporate shareholder is a nominee, or the character of the beneficial owner.
- Because the repurchasing company has an advantage if shares are acquired from a corporate, there is some incentive to arrange for shares to be purchased by a corporate prior to sale to the company.

For these reasons, it is proposed that where shares are repurchased from a corporate, the repurchasing company would be liable for tax on the dividend component of the proceeds by way of a debit to its ICA. It should be noted that companies may be able to avoid these difficulties by repurchasing shares off-market. In that case, ordinary dividend rules would apply with imputation credits able to be attached to the dividend component of any share repurchase.



### *Repurchase from Tax-Exempt Entities*

To make the share repurchase rules as simple as possible, no special rules for on-market repurchases from tax-exempt entities are proposed. Such repurchases would be treated in the same way as acquisitions from resident taxable entities. A debit to the ICA of the repurchasing company would arise in respect of the dividend component.

### *Repurchase from a Non-Resident Shareholder*

It is proposed that a debit (calculated as outlined above for residents) arise in the ICA of a company that repurchases its shares on-market from a non-resident. There would be therefore no need to distinguish between non-resident and resident vendors.

An alternative approach would be to treat the dividend component as an ordinary non-cash dividend for non-resident withholding tax (NRWT) purposes. This means that no deduction of NRWT would be made from the sale proceeds. Instead, the repurchasing company would pay an amount of NRWT equivalent to the amount that would have been deducted under general rules. This mechanism would be more appropriate than a deduction of NRWT because it ensures that the vendor is in the same position as a vendor selling to a third party. However, this approach assumes that a repurchasing company is able to identify the vendor as a non-resident shareholder. Where shares are held by a nominee company, it would seem that such identification is impossible.

Accordingly, the approach proposed of debiting the ICA of the repurchasing company is simpler and is preferred. In addition, where a company has sufficient credits in its ICA, it may prefer to debit the ICA rather than pay NRWT.

### *Repurchase from a Vendor who Holds Shares on Revenue Account*

Where a share trader sells on-market, the share trader will be liable for tax on any profit on sale of the shares. In addition, a debit will arise to the ICA of the repurchasing company in relation to the dividend component of the sale proceeds. However, as the vendor will not be able to identify the purchaser and the repurchasing company will not know whether the shares are held on revenue account, this appears unavoidable. Obviously, the problem would be reduced if shares are repurchased off-market, although this may not always be possible.

## **2.5.4 Repurchase by Non-Resident Companies**

### *Off-market*

The Valabh Committee considered that, while changes in our company law would have no impact on non-resident companies that repurchase shares, our tax law should address the consequence of a share repurchase permitted by

other jurisdictions. Their proposal was that the rules should be consistent with the rules that apply to resident company share repurchases.

Adopting this approach, the ordinary dividend rules should apply to off-market repurchases by non-resident companies from resident shareholders. The Government agrees with this approach.

If the resident shareholder is an individual, the dividend component would be assessed to the shareholder. Where the shareholder is a corporate, foreign dividend withholding payment may be payable on the dividend.

### *On-market*

Placing a liability for tax on a foreign corporate repurchasing shares on-market poses jurisdictional and administrative problems. Therefore, it is considered that no tax liability should be imposed where shares are repurchased by non-resident companies on-market.

## **2.6 Treasury Stock Option**

During the course of developing the company law reforms, consideration was given to whether companies should be able to retain shares that they repurchased. This "treasury stock option" would enable companies to resell repurchased shares rather than be required to cancel them. However, this option was not included in the Companies Act.

The Valabh Committee had made proposals on how a treasury stock option might work from a tax perspective, but in the context of company law providing for treasury stock. In the absence of company law providing for a treasury stock option, it would be very difficult to provide a workable treasury stock option in the tax legislation. For this reason the Government has decided against including a treasury stock option in the tax legislation.

## **2.7 Summary of Proposals**

The principal proposals outlined in this chapter are that:

- a Distributions funded from realised capital profits will be tax-free when made through qualifying share repurchases or redemptions.
- b Amounts distributed to shareholders on the repurchase, redemption, or other cancellation of shares that occur through off-market repurchases be fully taxable as dividends:
  - i where the offer to repurchase or cancel is pro rata and the amount ultimately distributed represents less than 15 percent of the market

value of the shares of the company (i.e. it is not a *qualifying capital reduction*); or

- ii where the offer to repurchase or cancel is not made on a pro rata basis, a shareholder's proportionate interest in the company after the repurchase or cancellation is more than 85 percent of the shareholder's interest prior to repurchase or cancellation (i.e. it is not a *qualifying disproportionate reduction*).
- c Where there is a qualifying capital reduction or a qualifying disproportionate reduction, the "slice rule" would apply to determine the dividend component of the distribution except where the Commissioner applied the residual discretion to deem the full distribution to be in lieu of a dividend.
- d Where the slice rule applies the tax-free component of an amount distributed on a repurchase or cancellation is the sum of:
- (i) the subscribed capital amount (broadly, the subscribed capital per share repurchased or cancelled); and
  - (ii) the capital gain amount per share (broadly, the total realised capital profits of the company divided by the total number of shares on issue, other than fixed rate shares).
- e Where less than the market value is paid for a share that is repurchased or cancelled, the subscribed capital amount and the capital gain amount attributable to the share will be reduced so that the tax-free component of the distribution is the amount of subscribed capital and capital gain over the market value of the share.
- f Where a company purchases its shares off-market, the dividend component of the purchase is taxable to the vendor of the shares.
- g Where a company purchases its shares on-market, the company is liable for the tax on the dividend component of the purchase price. This is met by way of a debit to its imputation credit account which is calculated in the same way as resident withholding tax on a non-cash dividend. The vendor is exempt from tax on the dividend component.

## ANNEX 2.1

### ***Current Rules For Calculating Paid-Up Capital, Qualifying Share Premium and Excess Return Amount***

Section 4A of the Income Tax Act sets out a number of exclusions from the term "dividends". Principal among those exclusions are amounts funded from subscribed capital (being paid-up capital and qualifying share premium) distributed when shares are cancelled or redeemed, and amounts funded from capital gains distributed on the liquidation of a company.

Hence, a dividend for tax purposes is a benefit which is derived by virtue of a shareholder's ownership interest in a company, excluding the return of the original investment and, in the case of a liquidation, capital gain amounts. Under section 4A those excluded amounts are calculated as follows:

#### *Distributions Attributable to Paid-Up Capital*

Under the section, the amount per share returnable tax-free as paid-up capital is computed as:

$$\begin{array}{r} a \\ - \\ b \end{array}$$

where:

- a is the total amount of capital paid up prior to the redemption of the shares of the class being redeemed or cancelled; and
- b is the total number of shares of the class that have ever been issued by the company prior to the redemption that are still on issue.

#### *Distributions Attributable to Qualifying Share Premium*

Qualifying share premium amounts returnable tax-free are computed according to a similar averaging formula to that outlined in the previous paragraph. However, the amount of tax-free share premium is the actual amount debited to the company's share premium account in respect of the redemption if this is smaller than the amount computed under the averaging rule.

#### *Distributions Attributable to Other Tax-Free Sources on a Liquidation*

Distributions funded from certain realised and unrealised capital gains are also non-taxable when distributed on the liquidation of a company. These residual

non-taxable amounts are allocated to distributions on a pro rata basis according to total distributions made on a liquidation, other than distributions of subscribed capital. Broadly, the residual amounts distributable tax-free to a shareholder on liquidation are computed as:

$$\frac{a \times b}{c}$$

where:

- a is the amount of realised and unrealised capital gains available for distribution to shareholders;
- b is the distributions received **by the shareholder** on the liquidation, other than distributions of paid-up capital and share premium; and
- c is the total amount of distributions payable to **all shareholders** on liquidation, except distributions of paid-up capital and qualifying share premium.

Where a distribution exceeds the total amount that can be attributed to tax-free sources, the excess is taxable as a dividend.

The first two formulae operate on a class by class basis for each class of shares redeemed or cancelled. Shares are considered to be of the same class for tax purposes if:

- the shares carry the same rights to exercise voting power and the same rights to distributions; or
- the same amount has been subscribed in respect of each share, the company elects to treat such shares as being of the same class, and the company can distinguish between such shares and other shares.

## ANNEX 2.2

### MECHANISMS FOR TAXING THE DIVIDEND COMPONENT

Shareholder	REPURCHASING COMPANIES				
	Resident Non-Qualifying Company		Resident Qualifying Company	Non-Resident Company	
	<i>On-Market selective only</i>	<i>Off-Market pro rata or selective</i>	<i>Off-Market pro rata or selective</i>	<i>On Market</i>	<i>Off-Market</i>
<i>Resident Non-Corporate</i>	Dividend exempt to recipient. Debit to ICA	Ordinary dividend treatment. ICA, RWT credits attached	Ordinary dividend treatment. ICA, RWT credits attached	No Tax	Ordinary dividend treatment
<i>Resident Corporate</i>	As above	As above	As above	No Tax	As above
<i>Resident Vendor Taxable on share gain</i>	As above plus tax on gain	As above plus tax on gain over and above dividend	As above plus tax on gain over and above dividend	No Tax	As above plus tax on gain over and above dividend
<i>Resident Tax Exempt</i>	Debit to ICA	Ordinary dividend treatment (exempt)	Ordinary dividend treatment (exempt)	No Tax	Ordinary dividend treatment
<i>Non-Residents</i>	No NRWT. Debit to ICA	Ordinary dividend NRWT deduction	Ordinary dividend NRWT deduction	No Tax	No Tax

## ANNEX 2.3

### *Examples of Mechanisms for Taxing the Dividend Component*

Example 1: Repurchase from resident shareholder

#### Off-market

Company A has reserves comprising:

\$20,000 subscribed capital  
\$10,000 realised capital gain  
\$10,000 revenue reserves

There are 2,000 shares on issue, all of the same class, held by 10 shareholders. The market value of each share is \$20.

B owns 500 shares. Company A purchases those shares for \$20 per share. B receives \$10,000. As all of B's shares are sold, the distribution is not deemed to be in lieu of a dividend and the slice rule applies. The subscribed capital and capital gains attributable to the repurchased shares will be tax-free and are calculated in the following way:

#### Subscribed capital

$$\begin{array}{r} \$20,000 \\ \hline 2,000 \end{array} = \$10.00 \text{ per share}$$

#### Capital gains

$$\begin{array}{r} \$10,000 \\ \hline 2,000 \end{array} = \$5.00 \text{ per share}$$

The balance, being the dividend component, is therefore \$5 per share (\$2,500 in total). The company attaches the maximum imputation credits to the dividend (\$1,231.34) which is the benchmark ratio for the year. As the dividend is fully imputed, no RWT is deducted. B returns \$3,731.34 as assessable income and claims \$1,231.34 as a credit of tax. (If B was a resident company it would also credit its ICA with \$1,231.34, being the imputation credit attached to the dividend).

Where the repurchasing company is distributing tax-paid income (and assuming that the company is able to fully impute the dividend) no premium above market price need be paid to attract shareholders to sell to the company. However, where the company does or cannot fully impute the dividend component, the cost to the company of the repurchase may be greater than the market value of the shares. This is because, where there is a market for the shares, the shareholder will look for an after-tax return that is not less than what the shares could be sold for on-market.

In practice, however, it is difficult to understand why a company would prefer to pay a premium on the market value and deduct resident withholding tax rather than make a payment of tax (which it could use to offset a future tax liability) and fully impute the dividend to the shareholder.

### On-market

If the shares were repurchased on-market the slice rule would automatically apply. The dividend component would also be \$5 per share. A debit would arise to company A's imputation credit account as follows:

$$\frac{0.33}{0.67} \times \$2,500 = \$1,231.34$$

### Example 2: Off-market repurchase from vendor who is taxable on share profits

Assume in the above example that B is a trader who purchased the shares for \$15 each (and subsequently sold them to the company for \$20). B receives taxable income of \$5 per share, totalling \$2,500 for 500 shares. In addition, (assuming the company is paying the distribution from tax-paid profits) B will receive a fully credited gross dividend of \$3,731.34, comprising a dividend component of \$2,500 and imputation credits of \$1,231.34. This transaction has therefore been taxed twice - once as a dividend and then again as a profit on sale. To avoid this double taxation, B would be assessed only on the dividend component of the share repurchase.

If B had purchased the shares for \$5 per share so that the profit on the transaction was \$7,500, \$5,000 (\$7,500 - \$2,500) would be taxable as a profit on sale.



## **CHAPTER 3: AMALGAMATIONS**

### **3.1 Introduction**

This chapter considers the tax implications of the amalgamation provisions of the new Companies Act.

### **3.2 The Amalgamation Provisions of the New Companies Act**

Under the amalgamation provisions of the new Companies Act, the procedures governing the amalgamation of two or more companies into one company have been simplified in comparison with those applicable under existing company law. Under the new Companies Act, the amalgamation of two or more companies generally requires the following:

- approval from the board of directors;
- a resolution of the board of directors that the amalgamation will be in the best interests of the company;
- a resolution of the board of directors that the amalgamated company will satisfy the solvency test immediately after the amalgamation;
- advice to all secured creditors of the amalgamation proposal;
- shareholders' approval by special resolution; and
- registration of the proposal with the Registrar of Companies.

The amalgamation takes effect on the date specified in the amalgamation certificate issued by the Registrar of Companies.

Under the new amalgamation procedures court involvement is no longer required unless sought. In addition, an even simpler amalgamation process is provided for the amalgamation of wholly-owned companies. A "short-form" amalgamation procedure is provided under section 222 of the new Companies Act for a wholly-owned subsidiary amalgamating with a parent, or for two wholly-owned subsidiaries that amalgamate. Under the short-form procedure, an amalgamation may be approved solely by the boards of each amalgamating company agreeing to the amalgamation, provided the solvency test is still met.

Under the new Companies Act, the amalgamating companies continue as one company, which may be a continuation of one of the amalgamating companies or a new company. All assets and liabilities of the amalgamating companies are vested in the amalgamated company. Amalgamating companies can agree to

the terms of their amalgamation. Thus, if the terms of the amalgamation so provide, some shareholders in the amalgamating companies may be issued shares in the amalgamated company, while other shareholders in the amalgamating companies may be bought out for cash and debentures. Where one amalgamating company holds shares in another amalgamating company, those shares must be cancelled for no payment when the amalgamation becomes effective.

### **3.3 Tax Treatment of Revenue Account Shareholders in an Amalgamation**

#### ***3.3.1 Current Treatment***

Under current tax rules, the realisation of a gain or loss upon the disposal of a parcel of shares by a revenue account shareholder is a taxable event. Therefore, revenue account shareholders making a gain or loss on any shares swapped for other shares as part of an amalgamation face the same tax consequences as if they had sold the shares for cash.

#### ***3.3.2 Rollover Relief***

Ideally, taxes should not influence taxpayer preferences between different investment choices. However, any tax incurred on realisation of an investment spanning multiple tax periods changes taxpayer behaviour to the extent that taxpayers defer the tax liability by retaining an asset longer than they otherwise would. This is known as "lock-in". Lock-in influences are unavoidable in a realisation based income tax.

The Government is aware that some taxpayers believe that shareholder lock-in in relation to company amalgamations should be addressed by the provision of some form of shareholder rollover relief, which would enable a tax liability arising as a result of a share swap to be deferred until the shares acquired in the amalgamation were sold. Providing shareholder rollover relief only changes the timing of income recognition for tax purposes. The incentive to delay realisation is not eliminated. Indeed, if the shares acquired in an amalgamation increase further in value, rollover relief would exacerbate lock-in influences. Accordingly, the existence of lock-in does not support arguments that there is a sound policy basis for providing rollover relief.

In New Zealand only gains on shares held on revenue account are taxed. In Australia, Canada, and the United Kingdom rollover relief was not available prior to the introduction of comprehensive capital gains taxes in those jurisdictions. Thus, if anything, the experience of those jurisdictions suggests that the provision of rollover relief is not appropriate for New Zealand.

Introducing rollover relief would also result in tax considerations further distorting taxpayer decision-making by creating a bias towards amalgamation over other forms of sale or reorganisation.

Finally, the relief provisions that apply to corporate restructuring in other jurisdictions are understood to be among some of the most complex tax rules of those countries. These rules are apparently subject to considerable "tax planning". Under the circumstances, it does not appear necessary or appropriate to add to the Income Tax Act another layer of complexity that will increase opportunities for tax planning.

In summary, the current treatment of shares disposed of as part of a corporate reorganisation is consistent with the general realisation-based treatment of other taxable gains. The new Companies Act does not introduce any special feature in relation to amalgamations that is sufficient to warrant a departure from current tax treatment by the introduction of tax treatment inconsistent with general tax principles for taxpayers holding shares on revenue account. Accordingly, no legislative change is proposed.

## **3.4 Tax Treatment of Asset Transfers**

### ***3.4.1 Asset Transfers in an Amalgamation***

The purpose of the amalgamation provisions in the new Companies Act is to simplify the administrative procedures that must be followed when two or more companies merge. Thus, the new amalgamation provisions are designed to minimise administrative impediments to corporate restructuring through amalgamations.

The Government favours extending to amalgamations the tax-free asset transfer treatment available to consolidated groups. Both consolidation and amalgamation can be used to achieve the same substantive restructuring. Tax rules should not influence which method (amalgamation or consolidation) taxpayers use in merging their corporate operations. In other words, the two different methods of restructuring should yield the same tax consequences.

The amalgamation of two or more companies can be viewed as a one-step procedure by which companies become wholly-owned (100 percent commonly-owned by the same shareholders) and then merge their assets into a single company. The consolidation regime can be used to achieve this result without triggering income tax consequences on the transfer of the merging companies' assets to a single company.

The Government proposes that amalgamation be dealt with by utilising the tax-free asset transfer rules of the consolidation regime.

### **3.4.2 Other Considerations**

Consistent with the consolidation regime, the amalgamated company would inherit each transferor's tax cost for the asset (as well as the transferor's other tax attributes in respect of the asset).

The Valabh Committee has recommended an asset classification system under which tax consequences would be triggered when a taxpayer moves an asset out of the tax base. Accordingly, the Government considers it would be appropriate to implement rules that would trigger tax consequences when an asset moves from revenue to capital account as a result of an asset transfer made pursuant to an amalgamation.

In addition, tax-free treatment should only apply where the amalgamated company will be resident in New Zealand. Otherwise, assets could be transferred out of the New Zealand tax base free of tax consequences, thereby permanently avoiding (rather than deferring) New Zealand tax. Under the consolidation regime, only companies that are resident in New Zealand are eligible to be members of a consolidated group.

If the amalgamated company is a qualifying company, tax-free treatment should only apply if all amalgamating companies are also qualifying companies. Otherwise amalgamating a non-qualifying company into a qualifying company would enable qualifying company election tax to be avoided.

## **3.5 Losses and Imputation Credits**

### **3.5.1 Introduction**

In the Government's view, an amalgamated company should be able to succeed to the losses and imputation credits of the amalgamating companies, subject to ensuring that the shareholder continuity rules and the limitations on loss grouping are not circumvented.

### **3.5.2 Losses - Implications of Shareholder Continuity and Loss Grouping Rules for Amalgamations**

The tax treatment of companies that amalgamate should be consistent with the tax treatment of company losses generally. An amalgamated company should inherit the losses of an amalgamating company only when shareholder continuity and commonality tests are met.

### ***3.5.3 Existing Shareholder Continuity Rules***

The purpose of the loss carry-forward rules is to ensure that, to an extent, shareholders in a company at the time it incurred tax losses are still shareholders when the company utilises those losses. This is achieved through shareholder continuity rules that determine what tax losses a company may offset against its future income.

A company may carry forward its losses and offset them against income arising in subsequent income years provided that shareholder continuity of at least 49 percent is maintained throughout the period beginning with the year in which the loss is incurred and ending with the year to which the loss is carried forward (the "continuity period"). Shareholder continuity is maintained if at least 49 percent of the shares in the company are owned by the same persons throughout the continuity period.

### ***3.5.4 Shareholder Continuity Rules and Amalgamations***

An amalgamation would not provide a means of circumventing the shareholder continuity rules with respect to the amalgamating companies provided those rules continue to apply after the amalgamation. The amalgamated company would be considered to satisfy shareholder continuity with respect to the losses of an amalgamating company if at least 49 percent of the shares in the amalgamated company and 49 percent of the shares of the amalgamating company are owned by the same persons throughout the continuity period. The amalgamated company would be considered a continuation of the loss company for the purposes of the shareholder continuity test.

Of course, if at the time of the amalgamation more than one amalgamating company had carried forward tax losses, and those companies had different shareholders during the relevant continuity periods, the amalgamated company would need to keep track of the losses of each such company separately, even where those losses were incurred for the same income year.

### ***3.5.5 Existing Loss Grouping Rules***

The purpose of the loss grouping rules is to enable the losses of loss companies to offset the income of profit companies provided a minimum commonality of ownership is achieved. The application of the commonality of ownership test is separate and different from the shareholder continuity test.

Under current loss grouping rules, the losses of one company (both current losses and those carried forward) may be offset against the income of another company only if, throughout the period beginning with the year the loss is incurred and ending with the year of offset, a group of persons concurrently owns at least 66 percent of the shares in each of the companies. This group of shareholders is not restricted to persons who were shareholders at the time the

losses were incurred. This requirement is often referred to as "shareholder commonality".

If a loss company wishes to group its losses with a profit company, and it has some losses that do not satisfy the shareholder commonality test, and other losses from subsequent years that do satisfy the shareholder commonality test, only those losses satisfying the shareholder commonality test may be used to offset the profit company's taxable income.

### **3.5.6 Loss Rules And Amalgamations**

The Government considers that an amalgamated company should be allowed to inherit the losses of any amalgamating company if:

- The shareholder continuity rules continue to be satisfied with respect to the losses of that amalgamating company after the amalgamation.
- The losses of that amalgamating company could have been grouped against income realised by all other amalgamating companies immediately prior to the amalgamation.

If the losses of more than one of the amalgamating companies are carried into the amalgamated company, the losses of each predecessor company would continue to be identified separately in order to continue to test shareholder continuity. Where the losses arose in the same income year, the amalgamated company would be able to elect the set or sets of losses against which its income could be offset. Where no election is made, losses would be offset against assessable income on a pro rata basis.

Shareholder continuity would be measured by reference to ownership interests in the amalgamated company compared to ownership interests in the predecessor amalgamating company for the continuity period. Where the amalgamated company subsequently breaches shareholder continuity, any remaining losses carried over from the amalgamating company would be forfeited in the usual way.

A more lenient approach is possible in the consolidation regime as the members of the consolidated group continue as separate legal entities. Therefore, under consolidation, where a consolidated group contains a loss company with pre-consolidation losses that cannot be grouped with any other members of the consolidated group, the losses can be carried forward and offset against the loss company's income, as long as it continues to meet the loss carry-forward shareholder continuity requirements.

However, it is not practicable to develop rules regarding amalgamations that fully replicate this, as the amalgamating companies that form an amalgamated company have no continuing legal existence separate from the amalgamated company.

### ***3.5.7 Imputation Credit Shareholder Continuity Rules***

The purpose of imputation carry forward restrictions is to ensure that the imputation credits are enjoyed by substantially the same shareholders of the company as existed at the time the imputation credits arose.

The shareholder continuity rules apply to imputation credits in the same manner as to losses, except that the shareholder continuity threshold is 66 percent. Except for consolidated groups there are no provisions for grouping imputation credits between members of commonly-owned groups.

Consequently, an amalgamated company should be allowed to succeed to imputation credits of an amalgamating company if, after the amalgamation, the shareholder continuity requirement continues to be satisfied with respect to the relevant amalgamating company up to the period those credits are distributed by the amalgamated company.

## **3.6 Conclusion**

The simplified amalgamation provisions in the new Companies Act are designed to remove unnecessary regulatory impediments to amalgamations. The provisions are not designed to create a bias towards amalgamations for their own sake.

Similarly, tax rules should not favour amalgamations over other similar forms of corporate restructuring. This means that tax rules regarding amalgamations should be more or less the same as current generally applicable rules regarding company and shareholder taxation. Tax rules relating to the amalgamation of two or more companies should be closely aligned with existing rules governing the carry forward and grouping of tax losses and the carry forward of imputation credits. Amalgamating companies should also be able to use the preferential asset transfer rules currently available to taxpayers through the consolidation regime, without needing to consolidate or group the amalgamating companies prior to amalgamation.

A tax liability would be triggered when shareholders trading on revenue account swap shares in an amalgamating company for shares in an amalgamated company. This is a continuation of existing law.

### 3.7 Summary of Proposals

It is proposed that the following income tax rules apply to company amalgamations:

- (a) Revenue account shareholders in an amalgamating company will realise assessable income or loss on the exchange of their shares in the amalgamating company for shares in the amalgamated company. This requires no change to existing tax rules.
- (b) The transfer of assets to an amalgamated company from the amalgamating companies will be tax-free, under rules similar to those that apply to consolidated groups.
- (c) An amalgamated company will be allowed to succeed to losses of a particular amalgamating company if:
  - (i) the shareholder continuity requirement with respect to that amalgamating company continues to be satisfied; and
  - (ii) immediately prior to the amalgamation, the losses of that amalgamating company could have been grouped against income of all other amalgamating companies.
- (d) An amalgamated company will be allowed to succeed to imputation credits of an amalgamating company only if the shareholder continuity requirement continues to be satisfied with respect to that amalgamating company after the amalgamation.
- (e) For the purposes of the shareholder continuity tests the losses and imputation credits of each predecessor company would continue to be separately identified by the amalgamated company. Where the losses arise in the same income year, the amalgamated company will be able to elect the set or sets of losses against which its assessable income could be offset. Where no election is made, losses would be offset against assessable income on a pro rata basis.



# CHAPTER 4: TAX ACCOUNTING ISSUES

## 4.1 Introduction

This chapter covers tax accounting questions associated with the transition between the existing and the new companies regime, as well as issues relating to company distributions made other than by way of share repurchases. The following areas, in particular, are discussed in this chapter:

- treatment of the existing capital reserves of companies registering under the new companies regime;
- revision of the current qualifying share premium rules;
- determining the subscribed capital of an amalgamated company;
- tax rules where distributions made to shareholders breach the company law solvency test and are subsequently recovered.

## 4.2 Treatment of Company Accounting Reserves for Tax Purposes

The current tax treatment of company reserves generally requires only minor changes to respond to the reform of company law. The only significant change will be the proposed revision of the current qualifying share premium rules.

### 4.2.1 Existing Capital Reserves

The new Companies Act makes no distinction between reserves arising from shareholder contributions and other reserves. However, this distinction is important for tax purposes, as reserves contributed by shareholders can be distributed tax-free. Therefore, the existing tax concepts of paid-up capital and share premium will be supplanted by the single concept of "subscribed capital".

Subscribed capital will, like paid-up capital and share premium, be available for tax-free distribution on liquidation, or on the redemption or repurchase of shares, subject to the proposed rules regarding share repurchases detailed in Chapter 2. Where shares are "partly paid" on subscription, only the amount paid on subscription is included in subscribed capital. For tax purposes, existing paid-up capital and qualifying share premium reserves will be included in subscribed capital.

The subscribed capital of new companies registering under the new Companies Act will include all sums paid to the company in return for shares in the company and the net value of subsequent taxable bonus issues.

For three years after the new Companies Act comes into force, some companies will have re-registered while others will remain under the old regime. Consequently, some companies will distinguish in their capital reserves between share premium and paid-up capital, while other companies will record only subscribed capital. Several sections of the Income Tax Act, including sections 4 and 4A, will be redrafted to accommodate both situations.

#### ***4.2.2 Capital Redemption Reserves***

The Companies Act 1955 provides that where redeemable preference shares are redeemed otherwise than from the proceeds of a fresh issue of shares, a company must transfer a sum equal to the nominal amount of the shares redeemed to a "capital redemption reserve fund", sourced from funds available for distribution as a dividend.

Capital redemption reserves are not currently treated as paid-up capital for tax purposes. This treatment will be preserved for companies registering under the new companies legislation - capital redemption reserves will not be subscribed capital for tax purposes.

#### ***4.2.3 Existing Bonus Issues***

Under the Companies Act 1955, bonus issues represent a transfer of retained earnings to paid-up capital effected by way of the creation of additional "bonus" shares which are issued to shareholders for no consideration, or in lieu of a dividend.

For tax purposes, there are currently three types of bonus issues, namely taxable, non-taxable and 10-year bonus issues. A different tax treatment applies to each of these.

Where non-taxable bonus issues are made, the bonus issue is tax-free, and the transfer to paid-up capital is ignored for tax purposes. It is proposed that amounts of paid-up capital resulting from non-taxable bonus issues will be taxable on distribution, with the exception of amounts bonus issued out of capital gain or qualifying share premium reserves and distributed during a liquidation or cancellation of shares.

In the case of taxable bonus issues, the value of the issue, less any attached imputation or RWT credits, is transferred from taxable reserves to paid-up capital at the time the issue occurs. It is proposed that on transition to the new companies regime, amounts of paid-up capital that have arisen from capitalised taxable bonus issues will be subscribed capital for tax purposes.

A 10-year bonus issue is a bonus issue made between 1 April 1982 and 1 October 1988. These bonus shares were non-taxable at the time of issue, with the capitalisation not being recognised for tax purposes until the tenth anniversary of the bonus issue. In effect, companies are permitted to make a tax-free transfer to paid-up capital 10-years after the bonus issue.

It is proposed that upon registration under the new Companies Act, amounts capitalised from 10-year bonus issues that have reached their tenth anniversary will be subscribed capital for tax purposes, while amounts capitalised in 10-year bonus issues that are less than 10 years old will not qualify as subscribed capital until the tenth anniversary of the issue. The exception to this is where the bonus issue was sourced from capital gain amounts or qualifying share premium. Other amounts capitalised by way of 10-year bonus issues would continue to be taxable if distributed before the 10-year period has elapsed.

#### **4.2.4 Future Bonus Issues**

With the elimination of company law distinctions between capital reserves and retained earnings, there is no need to maintain a tax distinction between share splits and non-taxable bonus issues. Therefore, Income Tax Act references to non-taxable bonus issues will also be applicable to share splits.

It is proposed that for taxable bonus issues other than those made in lieu of a dividend, the issuing company will be free to elect the amount transferred to subscribed capital per bonus share issued.

While the new Companies Act does not explicitly authorise bonus issues, section 42 provides a general authorisation for a company to issue shares as it sees fit. Consequently, it is not intended at this stage to develop tax rules that provide an alternative to taxable bonus issues.

It may be appropriate, however, to consider developing a mechanism that would enable companies to distribute imputation credits without creating additional shares or paying out cash. In particular, it may be appropriate to develop notional distribution rules similar to those applicable for co-operative companies, with appropriate anti-streaming rules. Submissions on this matter are welcomed.

#### ***4.2.5 Tax-Exempt Taxable Bonus Issues and Dividends***

At present, if a taxable bonus issue is exempt from tax under section 63 of the Income Tax Act (for instance, a bonus issue made between members of a consolidated group) a tax-free transfer from that company's taxable to tax-free reserves may be achieved without any tax being paid. Similarly, a tax-free transfer from taxable reserves to subscribed capital may occur when tax-exempt dividends are paid out, and the funds are then re-subscribed in the dividend paying company. This is inconsistent with other tax rules that aim to tax, either at the time of the transfer or upon distribution to shareholders, amounts transferred from potentially taxable reserves to subscribed capital.

Accordingly, it is proposed that special rules apply to such a dividend that is either:

- used to directly or indirectly fund a subscription of capital in the company paying the dividends or in an associated company; or
- a taxable bonus issue.

The amount of the above subscription will be ineligible to be included in subscribed capital for tax purposes, to the extent that the dividend from which the subscription was sourced was:

- exempt from tax under section 63 of the Income Tax Act; and
- less than fully imputed, in which case an allocation rule will determine the portion of the dividend that is fully imputed.

For example, assume a company pays an exempt dividend of \$800, attaching imputation credits of \$200. The shareholder then subscribes \$1,500 to the company. The attached imputation credits are sufficient to fully credit \$406 of the dividend, with the remaining \$394 being uncredited. The first \$406 of the capital subscription would be subscribed capital for tax purposes, the next \$394 would not be subscribed capital, while the remaining \$700 would also be subscribed capital.

#### ***4.2.6 Qualifying Share Premium Rules***

Subscribed capital (including qualifying share premium) can be returned tax-free to shareholders, unless it is distributed in lieu of a dividend. This is in contrast to retained earnings, which are generally taxed on distribution. Therefore, in the absence of effective tax rules to the contrary, taxpayers face an incentive to recharacterise retained earnings as subscribed capital.

Under current law, qualifying share premium does not include share premium arising with respect to the issue of shares in one company for shares in another company. This limitation on qualifying share premium is designed to prevent a tax advantage resulting from share swaps on capital restructuring occurring either as part of a genuine commercial transaction or motivated entirely by tax considerations.

The current rule is somewhat arbitrary and poorly targeted, in that the application of the rule to shares issued in the exchange is determined by the relationship between the par value and issue price of the shares (the difference being the share premium), rather than the relationship between paid-up capital plus qualifying share premium and the issue price of the shares acquired in the exchange.

Accordingly, it is proposed to revise the existing qualifying share premium rule to take account of company law changes, to better reflect the tax policy underlying the current rule, and to provide a rule suitable for application to both share swaps made in the course of an amalgamation, and other share swaps. Where a transaction or series of transactions has the effect of the issuing of shares by a company in exchange for shares in another company, the subscribed capital attributable to the issued shares shall be the lesser of the subscribed capital or market value of the shares acquired in consideration for the issued shares. This would include a transaction where the acquiring company pays cash for the acquired shares, on condition that the cash is then re-subscribed in the issuing company.

This rule might be defeated by inflating the subscribed capital of the acquired company in anticipation of the share swap. Therefore it is proposed to include an anti-avoidance provision that would prevent the limitation on subscribed capital being defeated in this way.

Existing amounts of non-qualifying share premium resulting from the application of the existing qualifying share premium definition will continue to be taxable on distribution. Share premium that currently qualifies for tax-free distribution will retain that status.

### **4.3 Amalgamations**

Amalgamations would be subject to the general rules limiting subscribed capital attributable to shares issued in return for other shares.

In addition, it is proposed that the subscribed capital of any amalgamating company represented by shares held by or on behalf of any other amalgamating company immediately prior to the amalgamation would not qualify as subscribed

capital in the amalgamated company. This prevents double counting of subscribed capital, eliminates a tax planning opportunity, and is consistent with the new Companies Act. The new Companies Act requires that shares in any amalgamating company held by or on behalf of another amalgamating company be cancelled without payment or the provision of other consideration (sections 220(3) and 222(2)(b)(i) refer).

The example in Annex 4.1 demonstrates both this rule and the general subscribed capital limiting rule applicable to shares issued in exchange for other shares.

Other aspects of amalgamations are discussed in Chapter 3.

## **4.4 Excess Distributions**

### ***4.4.1 General Approach***

Under the new Companies Act, the board of a company may authorise a distribution (including a repurchase of shares) only if it is satisfied that the company will be solvent after the distribution. Where the company does not satisfy the solvency test after the distribution, the dividend may be recovered by the company from the shareholder. There are three exceptions to this right of recovery:

- where the shareholder received the distribution in good faith and without knowledge of the company's failure to satisfy the solvency test;
- where the shareholder has altered its position relying on the validity of the distribution;
- if it would be unfair to require repayment.

It is anticipated that use of the recovery provisions is likely to be a rare occurrence. However, the Income Tax Act has to be amended to provide for this.

An amendment to unwind the distribution for tax purposes is complicated by the fact that some dividends will have been fully imputed, some will have had resident withholding tax deducted and others will carry neither imputation nor RWT credits. In addition, where imputed dividends are paid to a company the attached credits will have been credited to the recipient's ICA.

It is proposed to amend section 4 of the Income Tax Act to provide that where a shareholder repays a dividend to the company pursuant to the new Companies

Act, the shareholder shall be deemed not to have received that dividend or any imputation credits attached to it. The Commissioner will reassess the shareholder's return for the year in which the dividend was received.

The company that recovered the distribution will credit its ICA as at the date of recovery for the amount of imputation credit attached to the dividend.

It is proposed that the Commissioner be required to refund any RWT or NRWT previously deducted on payment of the dividend.

#### ***4.4.2 Corporate Recipient***

A corporate recipient will have credited to its ICA any RWT or imputation credits attached to the dividend. It is proposed that an offsetting debit to the corporate shareholder's ICA arise on repayment of the dividend.

### **4.5 Summary of Proposals**

The following tax rules are proposed for companies registering under the new Companies Act:

- (a) That the following amounts be "subscribed capital" for tax purposes:
- (i) existing paid-up capital reserves, being:
    - amounts subscribed by shareholders;
    - where shares are "partly-paid" on subscription, the amount paid on subscription;
    - amounts that have arisen from taxable bonus issues;
    - amounts represented by 10-year bonus issues that have reached their tenth anniversary;
    - amounts represented by both unexpired 10-year bonus issues, and non-taxable bonus issues, that were sourced from either capital gain amounts or qualifying share premium;
  - (ii) existing qualifying share premium reserves.
- (b) In respect of future transactions, including amalgamations, having the effect of the issuing of shares by a company in exchange for shares in another company:

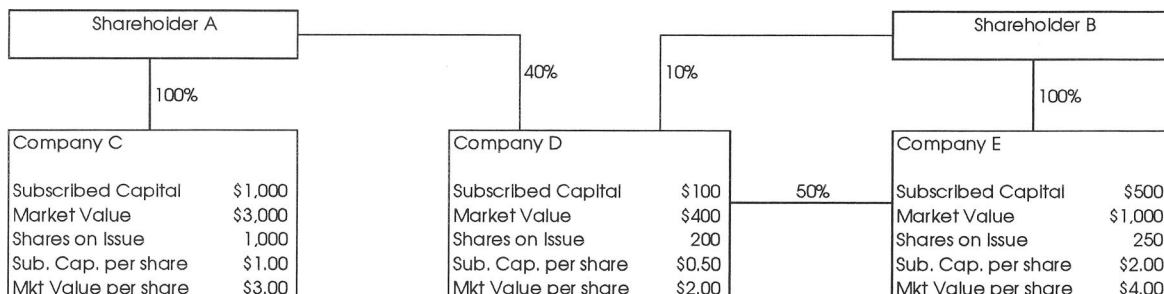
- (i) The subscribed capital of the issued shares will be the lesser of the subscribed capital or market value of the shares received in exchange for the issued shares.
  - (ii) For the purposes of paragraph (b)(i) an anti-avoidance rule would apply, so that the subscribed capital of the acquired company will not include capital resulting from subscriptions in that company made in anticipation of the share swap, to the extent that some or all of that capital is returned to the subscribing shareholders in some form other than as shares in the amalgamated company. This removes any tax advantage that would otherwise result from inflating the subscribed capital of a target company prior to acquisition.
  - (iii) Subscribed capital represented by shares held by amalgamating companies in each other would not be credited to the subscribed capital of the amalgamated company.
- (c) Subscriptions be excluded from subscribed capital for tax purposes to the extent that they are attributable to dividends that were:
- (i) exempt from tax under section 63 of the Income Tax Act; and
  - (ii) were not fully imputed (in which case an allocation rule will apply to determine the non-imputed amount).
- (d) In the case of a company recovering a distribution from shareholders:
- (i) A credit to the value of imputation credits attached to the recovered dividend would arise in the imputation credit account of the company that recovers the dividend. The ICA credit would arise on the date of dividend recovery.
  - (ii) The shareholder would be deemed not to have received that dividend, or any imputation credits attached to it, and would be reassessed accordingly.
  - (iii) The Commissioner would be required to refund any RWT or NRWT that had previously been deducted from the refunded dividend.
  - (iv) Where the recipient of the dividend was a corporate, the repaying company would debit its imputation credit account with an amount equal to the value of any resident withholding tax or imputation credits attached to the recovered dividend.



## APPLICATION OF TAX ACCOUNTING RULES TO AN AMALGAMATION

### Stage 1

Start position:



### Stage 2

A and B agree to amalgamate C Co, D Co, and E Co into a new company, F Co. F Co issues 2,000 shares in total to A and B in proportion to the market value of their direct holdings (double counting results if indirect holdings are included, as the value of an indirect shareholding is counted once as the market value of the subsidiary company, and again as a share investment forming part of the value of the shareholding company).

In return for existing holdings in C Co and D Co, A is issued shares in F Co with a market value of:

C Co's market value x A's shareholding, plus D Co's market value x A's shareholding, =  $\$3,000 \times 100\% + \$400 \times 40\% = \$3,160$

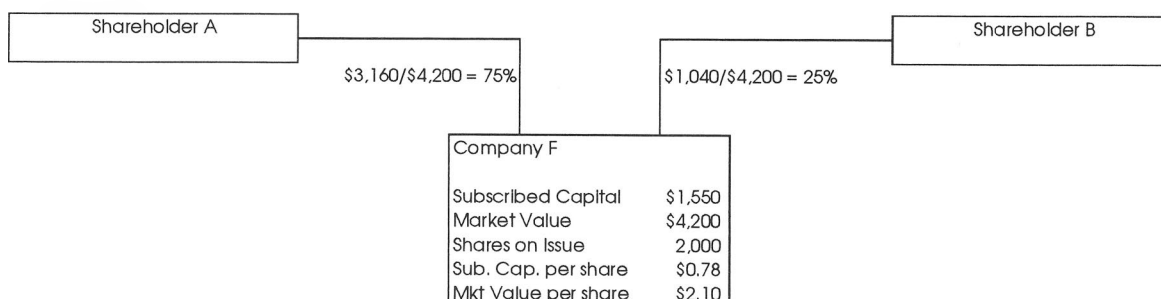
In return for existing holdings in D Co and E Co B is issued shares in F Co with a market value of:

D Co's market value x B's shareholding, plus E Co's market value x B's shareholding, =  $\$400 \times 10\% + \$1,000 \times 100\% = \$1,040$ .

The subscribed capital of F Co is the subscribed capital of C, D and E Co shares acquired by F Co in return for the F Co shares, excluding holdings by any of the amalgamating companies in each other =

Subscribed capital (C Co + D Co + E Co), less sub. cap. of D Co held by E Co =  $\$1,000 + \$100 + \$500 - (\$100 \times 50\%) = \$1,550$ .

End position:





## **CHAPTER 5: MISCELLANEOUS ISSUES**

### **5.1 Introduction**

This chapter covers aspects of company law reform with tax implications which have not already been specifically addressed:

- capital structure: abolition of nominal and par value;
- use of new measurement of company ownership rules to replace obsolete company law concepts;
- revising associated persons and company control definitions to accommodate company law changes;
- substituting the closely-held company definition for private and proprietary company definitions;
- providing for references to both the new and old Companies Acts during the transition period;
- the effect of companies having only one shareholder or one share;
- replacing memoranda and articles of association references in the Revenue Acts with the term "constitution";
- other terminology changes; and
- the Commissioner of Inland Revenue's preferred creditor status.

### **5.2 Capital Structure: Abolition of Nominal and Par Value**

The concepts of "par value" and "nominal capital" (and also as a consequence the concept of "share premium") are abolished under the new Companies Act. This will mean that the capital structure and financial accounts of a company incorporated or registered under the new Act will be significantly simplified.

Par value and nominal capital had their origin in the capital maintenance rule, which required a company to retain assets equal to its capital for creditor and shareholder protection reasons. The concept of capital maintenance is superseded under the new Act by the solvency test.

Par value was intended to provide protection for existing shareholders against stock watering (i.e. reducing the value of shares) by the issue of shares below

the value established at par. This protection, however, is not effective in circumstances where the shares are worth substantially more than par value. Section 47 of the new Act addresses the problem of stock watering by effectively requiring there to be adequate consideration paid on the issue of a company's shares. The board of directors is responsible for deciding the consideration for which a company's shares will be issued. Before issuing any shares the board must be satisfied that the consideration received for the shares is fair and reasonable to the company and to all existing shareholders. If the shares are to be issued other than for cash the board must determine the reasonable present cash value of the consideration.

Section 35 simply defines a share as personal property. This means that the new Act retains an essentially common law definition of a share. The Income Tax Act mainly relies on the common law understanding of what is and what is not a share (with the exception of section 192 and 195 debentures, which are deemed to be shares for Income Tax Act purposes).

There are various provisions in the Revenue Acts which use the terms nominal value, nominal capital or par value. As these terms are obsolete under the new Act, references to them will be replaced. These references are listed in Annex 5.1.

The terms nominal value, nominal capital and par value are mainly used in the various Revenue Acts to measure shareholders' interests in companies. It will be possible to replace these terms with the voting and market value interest concepts used in sections 8A to 8D of the Income Tax Act. Such a change of terminology can have effect from date of enactment and therefore can apply to companies incorporated under either the Companies Act 1955 or the new Companies Act.

### **5.3 Measurement of Shareholder Interests**

In addition to replacing such terms as nominal capital, nominal value and par value, the measurement of shareholder interest rules in section 8A to 8D of the Income Tax Act can also be used to replace references to issued capital, paid-up capital (where this term is not used for distribution purposes) and shares generally where those terms are used as a measurement of company ownership. Those rules are not dependent on the existing terminology of the Companies Act and can therefore be applied more generally in the Income Tax Act.

The company control definition in section 7 of the Income Tax Act and the various associated persons definitions are the main areas where the voting and market value interest concepts will be applied.

### ***5.3.1 Associated Persons and Company Control Definitions***

As noted above, it is proposed that the company control definition (section 7) and the various associated persons definitions in the Revenue Acts be amended to employ the measurement of shareholder interests rules contained in sections 8A to 8D. Under these rules shareholders' economic interests in a company will generally be measured by reference to their voting interests in that company. In certain limited circumstances, shareholders' interests may need to be determined by reference to **both** their voting interests and market value interests in the company.

Section 7 provides a standard company control definition which is used throughout the Income Tax Act (i.e. there is no multiplicity of definitions as there is with associated persons). By contrast, in addition to the general associated persons definition in section 8, there are currently four other associated persons definitions which apply only for the purposes of certain provisions in the Income Tax Act. They appear in:

- section 67 - tax treatment of profits and gains from land transactions;
- section 166 - notional interest on loans made to employees under an employee share repurchase scheme;
- section 214E - associated persons definition for the petroleum mining regime (sections 214D to 214N). (This definition is also used for section 74 purposes, where in the case of timber sold to an associated person of the seller the seller's deduction for the cost of the timber is limited to the amount of the profit or gain derived by the seller);
- section 245B - for purposes of the CFC and FIF regimes in Part IVA of the Income Tax Act. (For example, control interests held by associated persons are aggregated for the purposes of determining whether a foreign company is a CFC).

Each of these definitions also requires amendment to employ the new measurement of shareholders' interests. Similarly, it is proposed to amend the associated persons definition in section 2 of the GST Act.

The corporate and nominee look-through rules in existing section 8(2) are inadequate as they only refer to paid-up capital and not nominal capital, even though the latter is also used in section 8(1)(b) as a measure for determining whether a company and any individual are associated persons. The use of voting interest/market value interest tests in the recast section 8 will address this shortcoming.

## **5.4 Abolition of Private and Public Company Distinction**

The new Companies Act does not retain the current distinction between private and public companies, which in effect distinguishes between closely-held and widely-held companies. It is not considered necessary to have a separate regime for closely-held companies in the new Act. The flexibility typically provided by such a regime, such as less formality in management and shareholder decision-making, can be achieved under the new Act by a particular company's constitution providing that various presumptions in the new Act will not apply to that company.

Tax references to the existing Companies Act private company definition are listed in Annex 5.2.

The use of the private/public company classification in certain Income Tax Act provisions recognises the desirability of distinguishing between closely-held and widely-held companies in certain situations for tax purposes. In light of the absence of a closely/widely-held company distinction in the new Companies Act, those Income Tax Act provisions which currently refer to a private company could use the closely-held company definition contained in section 8B of the Income Tax Act. This would have the advantage of reducing the number of similar definitions.

However, there are distinctions between the definitions. While a private company can currently have between 2 and 25 shareholders, there is no associated persons rule whereby associated shareholders are treated as one person. A closely-held company, as defined in section 8B, is a company in which five or fewer shareholders (with associated shareholders such as relatives being treated as one person) have in total over 50 percent of the direct voting interests (or direct market value interests where a market value circumstance exists). After receiving submissions the Government will determine whether its goal of applying a single definition in all circumstances is the best approach.

While the closely-held company concept is embodied in various provisions in the Income Tax Act through the use of private company and proprietary company terms, there is no similar need for a widely-held company concept to replace the term "public company" outside of the shareholder continuity provisions.

The term public company is used only once in the Income Tax Act, in section 147. This reference can remain as it is defined separately from the Companies Act 1955 and relies currently on the definition of the private company. In short, a public company for section 147 purposes will generally be defined as any company which is not a closely-held company.

There is a reference to a public company, within the meaning of the Companies Act 1955, in section 35 of the Inland Revenue Department Act 1974 relating to the treatment of evidence in Taxation Review Authority proceedings. It is proposed to replace the public company references in this provision with a reference to the widely-held company definition in section 8B of the Income Tax Act.

## **5.5 Proprietary Companies**

In light of the removal of the private company references in the Income Tax Act, it is appropriate to review the proprietary company definition in section 2 of that Act. That definition also embodies a closely-held company concept of a company with a small number of associated shareholders and where ownership and management are often by the same persons. The proprietary company definition is utilised in various provisions which recognise that transactions between such companies and their shareholders (including persons associated with these shareholders) are more likely than in the case of other companies to be governed by other than arm's length considerations.

A proprietary company is defined generally as a company under the control of not more than four persons. Provisions in the Income Tax Act which use the proprietary company definition and the closely held concept that it embodies are set out in Annex 5.3. As discussed in the private company section of this chapter, the closely-held company concept is now also embodied in the appropriately named "closely-held company" definition in section 8B of the Income Tax Act.

It would be desirable if the Income Tax Act could employ a single, general closely-held company definition. Accordingly, it is proposed that the existing proprietary company references in the Income Tax Act also be replaced with the section 8B closely-held company definition.

## **5.6 Companies Act References**

Sections of the Revenue Acts which refer to the Companies Act 1955 are listed in Annex 5.4. This does not include Income Tax Act references which are used only for the purpose of defining a private company and which will therefore be omitted when private company references are removed.

Immediate replacement of all Companies Act 1955 references with Companies Act 1993 references will not be possible because during the three year transition period following the enactment of the new Companies Act there will continue to exist companies incorporated under the 1955 Act, which will not be repealed until the end of the transition period. Therefore, until the expiration of the transition period there will have to be references in the Revenue Acts to both Companies Acts.

## **5.7 One Shareholder/One Share Companies**

It is possible under the new Companies Act for a company to have only one shareholder and/or one share. Under the present law a company must have a plurality of shareholders and shares (i.e. at least two of each).

Many provisions in the Revenue Acts referring to shares or shareholders are predicated on the basis that a company must have a plurality of shares and shareholders and accordingly use words importing the plural number. The advent of one shareholder/one share companies should not, however, be problematical. Section 4 of the Acts Interpretation Act 1924, relating to the general interpretation of terms used in New Zealand statutes (unless inconsistent with the express provisions or context of an Act), provides that words and statutes importing the plural number are to include the singular number.

Consequential amendments to the Revenue Acts to take account of the possibility of one shareholder/one share companies will therefore not be necessary.

## **5.8 Company Constitutions: Abolition of Memoranda and Articles of Association**

A company's constitutional arrangements under the new Act will no longer be governed by a separate memorandum of association (containing the objects of the company and the amount of its authorised share capital) and articles of association (providing for the company's internal government). Instead, each company will have a constitution.

The absence of memorandum of association and articles of association terminology in the new Companies Act will involve little change to the Revenue Acts as they already typically use the generic term "constitution". For example, the term is employed in section 394B(2)(c) and the measurement of company ownership provisions in sections 8A to 8D. The few references to "memorandum of association" and "articles of association" in the Revenue Acts (listed in Annex 5.5) can be immediately replaced with the analogous term constitution.

## **5.9 Other Terminology Changes**

### ***5.9.1 Change from Allotment/Allotted to Issue/Issued***

The new Companies Act refers to shares being issued by a company and the issued shares. This is a change from the language used in the current



Companies Act, which refers to the allotment of shares by a company and the allotted shares.

The Income Tax Act currently uses both types of terms (i.e. allotment/allotted and issue/issued) in relation to shares. It would therefore be sensible for reasons of conformity with the new Companies legislation and the standardisation of terms within the Income Tax Act itself to change the allotment/allotted references in the Income Tax Act to the terms "issue" or "issued". In those sections where allotment/allotted is used in tandem with issue/issued, the allotment/allotted references merely need to be omitted. The Income Tax Act sections which currently use allotment/allotted terminology are listed in Annex 5.6.

As the allotment/allotted and issue/issued references, in relation to shares, have exactly the same meaning, it will be possible to change these terms from the date of enactment of the taxation legislation.

### **5.9.2 Change from Wound Up/Winding Up to Liquidated/Liquidation**

The rules for ending the life of a company have been greatly simplified in the new Act. Partly because of this simplification the following terms used in the Companies Act 1955 - "winding up", "voluntary winding up", "dissolution", and "striking off" - have been able to be dispensed with and replaced simply with the concepts of liquidation and removal from the register in the Companies Act 1993.

The term "liquidation" describes the process under which a company's assets are liquidated. The removal from the register of companies (equivalent to dissolution under the Companies Act 1955) is the final step on the liquidation of a company. Removal from the register can also constitute the entire process of ending a company's life in its own right (i.e. a prior liquidation process may not be necessary).

It should be noted that where the grounds for the removal from the register are that the Registrar is satisfied that the company is defunct, or the director or shareholders of an insolvent company have applied for it to be removed, notice must be given to the Commissioner of Inland Revenue. This notice allows the Commissioner to object to a company being removed from the register where there is outstanding tax owing by the company.

The Income Tax Act currently uses the terms winding up or wound up to describe the process of ending a company's life. Winding up is defined in section 2 of the Income Tax Act as including the final dissolution of a company. In order to achieve conformity with the new terminology in the new Companies Act relating to the termination of a company's existence the current Revenue Act references to the terms winding up or wound up (listed in Annex 5.7)

should be changed to liquidation or liquidated. This change can apply from the date of enactment. The term liquidation should be defined in section 2 of the Income Tax Act as including the removal of a company from the register of companies under the new Companies Act or a dissolution under the Companies Act 1955. The reference to dissolution under the Companies Act 1955 can be deleted at the end of the three-year transition period. As with the term liquidation, winding up refers to the process by which a company's life is ended. Dissolution is the final step in the winding up of a company.

## 5.10 Commissioner's Status as Preferred Creditor

Section 312 of the new Companies Act provides that a liquidator, after meeting the claims of secured creditors (other than the claims of debenture holders under any floating charge), must pay out of the assets of the company the preferential claims set out in the Seventh Schedule of the new Act.

Clause 2(d) of the Seventh Schedule refers to amounts deducted by the company from the wages or salary of an employee in order to satisfy obligations of the employee. The total sum to which priority can be given under section 2(d) is limited by section 6 of the seventh schedule to \$6,000 in the case of any one employee. This section is widely drafted and could include PAYE liability. The Commissioner would, however, rely on his specific priority under clause 5 in respect of this liability.

Clause 2(e) of the Seventh Schedule includes any amounts relating to child support which are required to be deducted from an employee's wages or salary by a company and paid to the Commissioner of Inland Revenue in accordance with the Child Support Act 1991.

Clause 5 of the Seventh Schedule gives the Commissioner of Inland Revenue preferred creditor status in respect of:

- GST;
- source deduction payments under Part XI of the Income Tax Act (this specifically includes PAYE obligations **without** any limit as to the amount to which priority is given);
- non-resident withholding tax deductions;
- resident withholding tax deductions.

Clause 9 of the Seventh Schedule provides that after a liquidator's or receiver's expenses are met all other preferential claims rank equally and if a company's assets are insufficient to meet them the debts abate and are paid in equal proportions.

Clause 9 also provides that preferential debts are paid in priority to the claims of holders of debentures under any floating charge. If the assets available for payment of general creditors are insufficient to satisfy preferential debts, then the shortfall can be taken from assets which are subject to a floating charge.

The existing preferential creditor status of the Commissioner is unchanged by Clause 5 of the Seventh Schedule, which specifically states the nature and extent of the Commissioner's priority. The Commissioner's preferred creditor status is not specifically referred to in section 308 of the Companies Act 1955 (the equivalent provision to section 312); instead, this status is "imported" by specific provisions in the GST Act (section 42) and the Income Tax Act (section 365(2)(b)). It is proposed to amend these preferred creditor provisions in the Revenue Acts so that they contain cross-references to the Seventh Schedule to the new Companies Act.

## 5.11 Summary of Proposals

The proposals in this chapter are that:

- (a) The current references in the Revenue Acts to nominal capital, nominal value, par value, issued capital, paid-up capital and shares generally - where those terms are used to measure shareholders' interests in companies - be replaced with the concepts of voting interest and market value interest contained in the measurement of company ownership rules in sections 8A - 8D of the Income Tax Act.
- (b) The Income Tax Act employ a single, general closely-held company definition (outside the qualifying company regime) which would be substituted for the current private company and proprietary company references in the Income Tax Act.
- (c) The public company reference in section 35 of the Inland Revenue Department Act 1974 be replaced with a reference to the widely-held company definition in section 8B of the Income Tax Act.
- (d) Other existing company law references in the Inland Revenue Acts identified in Annexes 5.4 to 5.7 be amended to align the Revenue Acts with the new definitions and concepts used in the Companies Act 1993.

## **ANNEX 5.1**

### **NOMINAL VALUE, NOMINAL CAPITAL AND PAR VALUE REFERENCES**

#### **Nominal Value**

##### ***Income Tax Act***

- Section 7(4) - defining when two companies consist substantially of the same shareholders.
- Section 8(1)(b) - defining when a company and an individual are associated persons.
- Section 67(2)(b) - profits or gains from land transactions.
- Section 150(1)(d) - contributions to employees' superannuation schemes.
- Section 166(2)(b) - notional interest on loans made to employees under employee share purchase schemes.
- Section 194(5) - deduction for dividends paid on specified preference shares issued before 23 October 1986.
- Section 195(2) - interest on debentures issued in substitution for shares.
- Section 214E(1) - petroleum mining operations regime associated persons definition.

#### **Stamp and Cheque Duties Act**

- Section 22B(4)(c) - conveyance duty exemption for first farm purchase.

#### **Estate and Gift Duties Act**

- Section 75(1)(b),(c) - gift duty exemption for certain payments by employers.

## **Nominal Capital**

### ***Income Tax Act***

- Section 7(2), (5) - defining when a company is under the control of any person.
- Section 245C(4)(b) - calculation of control interest.
- Section 245D(2)(b) - calculation of income interest.
- Section 245E(1) - variations in control or income interests.

## **Par Value**

### ***Income Tax Act***

- Section 194(1)(e), (f) - deduction for dividends paid on specified preference shares issued before 23 October 1986.

## ANNEX 5.2

### PRIVATE COMPANY REFERENCES

#### Income Tax Act

- Section 2 - definitions of terms "major shareholder" and "expenditure on account of an employee".
- Section 4A(10) - exclusions from term "dividends".
- Section 6(2),(3) - meaning of term "source deduction payment".
- Section 106(1)(j) - private and domestic expenditure.
- Section 147(1) - deduction for cash donations by certain companies (while amending this section the opportunity should be taken to delete the public authority and local authority references in subsection (1) as these entities are no longer excluded from the company definition in section 2 of the Income Tax Act).
- Section 194(1) - deduction for dividends paid on specified preference shares issued before 23 October 1986.
- Section 336N(1) - definition of "shareholder-employee" for purposes of FBT regime.
- Section 336TB(1) - election to pay fringe benefit tax on an annual basis.
- Section 362(2) - tax deductions to be credited against tax assessed.
- Section 374B(1)(g) - determination of assessable income for family support purposes.
- Section 374E(1)(c) - Guaranteed minimum family income.

## **Inland Revenue Department Act**

- Section 35(4) - evidence in Taxation Review Authority proceedings (as discussed in Chapter 5, this private company reference will no longer be necessary when the reference to "public company" in this provision is changed to "widely-held company").

## **Estate and Gift Duties Act**

- Section 22 - valuation of shares.

## ANNEX 5.3

### INCOME TAX ACT APPLICATION OF PROPRIETARY COMPANY DEFINITION

- Section 2 - definition of term "expenditure on account of an employee". This is only relevant to any payment made by a proprietary company before 1 April 1989 in respect of expenditure incurred by an employee.
- Section 4(1)(k) - Certain proprietary company expenditure will constitute a dividend where the benefit of that expenditure is enjoyed by a shareholder of the company.
- Section 4(9) - If shareholders repay any expenditure which has been treated as a dividend under section 4(1)(k) the Commissioner, in certain circumstances, can amend the assessment by reversing the dividend and refunding any tax paid in excess.
- Section 4(12) - This provision exempts certain deemed dividends arising under section 4(1)(l) between 1 April 1992 and 31 March 1993.
- Section 7(3) - The provision for determining who has control of a company provides that, in relation to a proprietary company, where there is a group of persons, not exceeding four in number, who, for example, hold more than 50 percent of the company's shares, the company will be deemed to be under the control of those persons for the purposes of the section 2 proprietary company definition. It will be irrelevant that there may be another group of persons who could also be deemed to have control of the company under any of the other tests used to determine control of a company in section 7(2) such as paid-up capital, voting power or entitlement to profits.
- Section 97(1) - This provision allows the Commissioner to re-allocate for tax purposes excessive remuneration paid by certain taxpayers to relatives. The reference to a proprietary company in this provision is exclusionary in nature only and has the result that the provision does not apply to a proprietary company making a payment of excessive remuneration.
- Section 151(2) - A proprietary company is denied a deduction for any pension paid to a former employee who is or was a shareholder in the company unless the Commissioner is satisfied that the former employee was a bona fide employee of the company and the size of the pension was similar to that which would have been arranged on an arm's length basis.



- Section 190 - The Commissioner in certain cases may limit the deduction available for remuneration paid to any shareholder, director, or one of their relatives, by a proprietary company to the extent that the Commissioner considers such remuneration to be excessive. The amount of remuneration considered by the Commissioner to be excessive is deemed to be a dividend paid by the company to the recipient.

## ANNEX 5.4

### COMPANIES ACT 1955 REFERENCES

#### Income Tax Act

- Section 2 - Definitions of the terms "director" and "winding up".
- Section 4(1)(b)(ii) - Meaning of term "dividends".
- Section 64F(1)(c)(ii) - Income and expenditure treatment where financial arrangement redeemed.
- Section 78(2)(b) - Amounts remitted to be taken into account in computing income.
- Section 188(6)(c)(ii) - Carrying forward of losses.
- Section 211B(10)(b) - Special partnerships.
- Section 214D - Interpretation of petroleum mining provisions.
- Section 245J(12) - Branch equivalent income calculation.
- Section 276(1) - Liability of directors and shareholders for tax payable by company left with insufficient assets.
- Section 327Q(3) - Recovery of resident withholding tax deductions.
- Section 365(2)(b), (3) - Recovery of tax deductions from employers.
- Section 367(1)(c) - Unpaid tax deductions to constitute charge on employer's property.
- Section 400(1) - Deduction of tax from payment due to defaulters. (No Companies Act reference will remain in section 400(1) following the deletion of redundant paragraphs (a) and (b) of the definition of "bank" in this provision.)

## **GST Act**

- Section 42(2)(b) - Recovery of tax.
- Section 43(1) - Deduction of tax from payment due to defaulters (for the same reason as for section 400 of the Income Tax Act, the Companies Act reference in this provision can be removed).
- Section 55(8) - Group of companies.

## **Stamp and Cheque Duties Act**

- Section 7(h),(k) - Meaning of expression "instrument of conveyance" extended.
- Section 15(3) - Rate of conveyance duty.

## **Estate and Gift Duties Act**

- Section 6(2)(i) - Situation of property for the purpose of determining the dutiable estate.

## **ANNEX 5.5**

### **MEMORANDUM AND ARTICLES OF ASSOCIATION REFERENCES**

#### **Income Tax Act**

- Section 61(34) - Definition of non-profit body for purposes of limited income tax exemption.

#### **GST Act**

- Section 2 - Definition of term "non-profit body".

#### **Stamp and Cheque Duties Act**

- Section 2 - Definition of term "shares in a flat or office owning company".
- Section 44 - Valuation of shares.

#### **Estate and Gift Duties Act**

- Section 22 - Valuation of shares.

## **ANNEX 5.6**

### **ALLOTMENT REFERENCES**

#### **Income Tax Act**

- Section 3(1)(a),(2) - Definition of term "bonus issues".
- Section 7(4) - Defining when two companies consist substantially of the same shareholders.
- Section 8(1)(b) - Defining when a company and an individual are associated persons.
- Section 67(2)(b) - Profits or gains from land transactions.
- Section 150(1)(d),(e) - Contributions to employees' superannuation schemes.
- Section 166(2)(b) - Notional interest on loans made to employees under employee share purchase scheme.
- Section 194(1)(f) - Deduction for dividends paid on specified preference shares issued before 23 October 1986.
- Section 204M(3) - Non-resident life insurer may elect to be treated as resident life insurer.
- Section 214E(1)(b) - Petroleum mining operation regime associated persons definition.
- Section 218(3),(10) - Profits or gains from sale of mining shares by companies.
- Section 226(1) - Definition of term "disposition of property" in the interpretation section in the trust regime.
- Section 393F(3) - Period of grace for certain new qualifying company regime elections.
- Section 393O(2) - Revocation of loss attributing qualifying company elections and new elections.

- Section 394A(1) - Definition of term "paid" in the interpretation provision of the imputation regime.

### **Stamp and Cheque Duties Act**

- Section 2 - Definition of term "instrument of nomination of shares".
- Section 7(h),(k) - Meaning of expression "instrument of conveyance" extended.
- Section 47(1)(b) - Valuation of consideration.
- Section 90(1) - Offence to issue certain shares unless pursuant to duly stamped instrument of nomination.

### **Estate and Gift Duties Act**

- Section 2(2) - Definition of term "disposition of property".

# ANNEX 5.7

## WINDING UP REFERENCES

### Income Tax Act

- Section 2 - Definition of terms "proprietary company" and "winding up".
- Section 4A(1)(c),(h),(3),(4),(10) - Exclusion from term "dividends".
- Section 8B - Definition of term "shareholder decision-making rights" in interpretation section for measurement of voting and market value interests provisions.
- Section 12(1)(f) - Commissioner's power to demand special returns and make special assessments.
- Section 65A - Transitional provision for certain superannuation contributions (this section would appear to be spent and therefore could probably be repealed outright).
- Section 183(1),(2) - Refund from income equalisation reserve account of company on winding up.
- Section 195(2) - Interest on debentures issued in the substitution for shares.
- Section 197(2) - Distribution of trading stock to shareholders.
- Section 197G(5) - Primary producer co-operative companies.
- Section 197H(7) - Co-operative dairy, milk marketing, and pig marketing companies.
- Section 218(9) - Profits or gains from sale of mining shares by companies.
- Section 226(10A) - Interpretation section in trust regime.
- Section 234(3) - Interpretation section in Maori Authority provisions.
- Section 245A(1) - Definition of term "accounting period" in interpretation section for international regime.

- Section 245C(4)(e) - Calculation of control interest in controlled foreign company regime.
- Section 245D(2)(e) - Calculation of income interest in controlled foreign company regime.
- Section 276(8),(10)(a),(b) - Liability of directors and shareholders for tax payable by company left with insufficient assets.
- Section 309(2)(a) - Interpretation section in non-resident withholding tax regime.
- Section 327P(6) - Record retention requirements for resident withholding tax regime.
- Section 393K(2) - Taxation on election to become qualifying company.
- Section 393N(b)(ii) - Loss attributing qualifying companies definition.
- Section 394M(4) - Limits on refunds of tax.
- Section 394ZZF(5) - Dividend withholding payment regime.
- Section 428(4) - Retention of business records requirements.
- Section 428A(2) - Record retention requirements where return information is transmitted electronically.

## **GST Act**

- Section 75(4) - Record retention requirements.



# PART TWO



## **EXPLANATORY NOTES TO THE DRAFT LEGISLATION**

The following notes provide an explanation of the proposed amendments to the Income Tax Act. In the interests of brevity, the commentary is confined to amendments that are considered to be significant and complex and that are not described in detail in the discussion document. The commentary should be regarded as a guide only, and it does not, for interpretation purposes, override the actual words used in the legislation.

### **Section 3(1)**

The definition of "bonus issue" will be amended to reflect the absence of a company law concept of capitalisation.

The definition of "non-taxable bonus issue" will be retained, but will in future be synonymous with a share split.

The term "ten year bonus issue" will be repealed. Amounts bonus issued between 31 March 1982 and 1 October 1988 which have served their time or which are paid up after 20 August 1985 and sourced from capital gain amounts and qualifying share premium are credited to subscribed capital (see item *i(i)* of "Transitional capital amount" in section 4A(3)).

### **Section 3(2)**

Section 3(2) will be repealed as "subscribed capital" is not reduced where losses are written off. The provision is therefore unnecessary.

### **Section 3(3)**

Section 3(3) will also be repealed. The replacement subsection provides a mechanism for determining for tax purposes how much is converted to subscribed capital by a taxable bonus issue (other than a bonus issue in lieu). This is required because there is no longer a distinction between the types of reserves for company law purposes and therefore no external reference point for determining the amount bonus issued. The amount credited to subscribed capital is the amount which the company elects is bonus issued (by notifying the Commissioner). The amount of dividend arising on a taxable bonus issue is the amount per share that the company so elects (section 4(6)). The provision only applies to New Zealand resident companies.

### **Section 4(1) and (3)**

It appears that there is no reason for the specific inclusion of "specified payments" in section 4(1)(a). "Specified payments" are defined in sections 4(3)

and 4A(2) as (in effect) share premium. Distributions of share premium in cash appear to be covered in the general category "all sums in money" in paragraph (a). The proposed deletion of this term does not reflect any change in policy in relation to distributions of share premium.

### **Section 4(1)(g)**

This paragraph has been redrafted to make it clear that amounts paid to shareholders on the acquisition by a company of its shares are included in the dividend definition (to the extent that they are not excluded under section 4A).

### **Section 4(7A)**

New subsection (7A) reverses the tax effect of a distribution which is subsequently recovered by an insolvent company. The provision operates on the assumption that the net dividend (that is, the dividend less any resident withholding tax or non-resident withholding tax) will be recovered from the shareholder. The RWT or NRWT will be refunded by the Commissioner directly to the company.

### **Section 4(12)**

The Government is concerned that companies, rather than purchase their own shares, will arrange for related companies to acquire those shares in order to avoid the dividend consequences that attach to the repurchase of shares. Such arrangements are likely to be caught by section 99(5). However, section 99(5) does not adequately deal with the tax consequences of an on-market repurchase.

Accordingly, section 4(12) will clarify how section 99(5) will apply in such circumstances. Where a company arranges for a related company to purchase shares in substitution for an on-market buy back, section 4(12) in effect provides that a debit will arise to the imputation credit account of the company that issued the shares.

### **Section 4(15)**

Section 4(15) will be amended to provide that where a person holds shares on revenue account, and sells those shares off-market to the company, the shareholder is taxed on the profit on sale only to the extent it exceeds the dividend (exclusive of imputation credits) arising on the sale.

## **Section 4A(1)(c)**

The new section 4A(1)(c) excludes from the dividend definition, if the conditions set out in subparagraphs (i) to (iv) are satisfied, amounts returned to shareholders when a company repurchases, redeems or cancels its shares (other than on liquidation) up to the amount of subscribed capital and realised capital gain per share.

### ***Subparagraph(i)***

This subparagraph contains the "brightline tests" discussed in section 2.4.4 of the discussion document.

### ***Subparagraph (ii)***

The brightline tests do not apply to fixed rate shares. The subscribed capital will be tax-free on redemption of such a share (assuming the anti-dividend substitution provisions in subparagraphs (ii) and (iii) do not apply).

### ***Subparagraph (iii)***

This subparagraph contains a redraft of the current anti-dividend substitution provision.

### ***Subparagraph (iv)***

This provision contains the "slice rule" described in sections 2.3.1 and 2.4.3 of the discussion document.

## **Section 4A(1)(ca)**

This paragraph excludes from the dividend definition amounts returned to shareholders when the company's shares are redeemed or cancelled upon its liquidation. The exclusion is limited to the aggregate of the subscribed capital per share and realised and unrealised capital gains per share.

## **Section 4A(1)(cb)**

This paragraph excludes from the dividend definition amounts returned to shareholders when a company repurchases its shares on the stock market. Such amounts are treated as dividends only for the purposes of:

- requiring that a debit arises to the repurchasing company's imputation credit account in relation to the dividend component of a distribution;

- enabling section 99(5) to apply (in the circumstances where it can apply) where there is an on-market acquisition;
- the recovery of dividend provisions in section 4(7A).

### **Section 4A(1)(h)**

Paragraph (h) will be repealed because losses written off will not affect a company's "subscribed capital amount" (defined in new section 4A(3)).

### **Section 4A(3)**

A new section 4A(3) will replace the current provision. It will contain definitions of new terms to be used in section 4A as well as amended definitions of terms currently in use. The terms used are in relation to a single share.

#### ***"Excess return amount"***

This formula is used in section 4A(1)(c) and (ca). It distinguishes between realised capital gains (item d) that may be distributed tax free on a cancellation or repurchase of shares, and unrealised capital gains (item e) which are available for tax free distribution only on liquidation.

The formula spreads such gains across all shares of the company, other than fixed rate shares.

Paragraph (ii) of the present item e has been broadened to align that paragraph with section 4A(11).

#### ***"Fixed rate share"***

Fixed rate shares are essentially shares in respect of which the rate of dividends paid is not commensurate with the company's profits. The definition in this subsection is similar to the definition of that term in sections 8B and 63(2D). It has a further requirement that there be no shareholder decision-making rights available to the holder of the shares except in very limited circumstances.

#### ***"Fully credited"***

This term is used in the definition of "subscribed capital amount" (item f(iv)) and discussed in section 4.2.5 of the discussion document.

The calculation of the subscribed capital amount of a share excludes:

- taxable bonus issues made to shareholders who are exempt from tax under section 63; and
- consideration received by a company on the issue of shares which is attributable to the payment by the company of a dividend exempt to those shareholders.

The exclusion applies except to the extent to which the taxable bonus issue or the dividend is fully credited.

"Fully credited" in relation to a dividend thus refers to that proportion of a dividend which is credited with imputation or withholding payment credits at the maximum imputation ratio.

### ***"Ineligible capital amount"***

This concept is the "anti-avoidance" provision referred to in section 4.2.6 of the discussion document. The term is used in the definition of subscribed capital amount (item f(vi)). It is intended to prevent the inflation of the subscribed capital of an acquired company in anticipation of a share swap.

### ***"Subscribed capital amount"***

The *subscribed capital amount* is a new concept which refers in essence to consideration received by a company on the issue of its shares. Its relevance is in determining the amount that can be distributed tax-free to shareholders under section 4A(1)(c) and (ca) described above. The predecessors of the subscribed capital amount are the current "returned capital amount" and "returned share premium amount" which effectively compute the subscribed capital per share based on an overall average of shares ever issued of the same class.

It is considered that the current returned capital amount computation will be deficient in the context of the "slice rule" in that where less than market value is paid for a share the rule restricts the amount of subscribed capital that may be returned to shareholders. Accordingly, there is a need for a new concept of subscribed capital which is based on a "moving average". The "moving average" formula will in effect calculate subscribed capital attributable to shares on issue at any particular time.

Subscribed capital amount is thus the aggregate of:-

- for a company that was in existence before the application date, its "transitional capital amount" (see below); and
- consideration received by a company on the issue (after the application date) of shares of the same class as the share being cancelled (subject to certain exclusions);

less

- subscribed capital amounts which have previously been returned to shareholders on the cancellation of shares of that class on or after the application date and which have been treated as tax-free distributions under section 4A(1)(c).

The result of the above calculation is divided by the number of shares of the same class on issue immediately prior to the relevant cancellation.

It is important to note (see item f(vi) in the calculation) that the amounts making up the consideration received by a company on the issue of its shares do not include consideration in the form of shares in another company acquired by the company to the extent to which the value of those shares exceeds the subscribed capital amounts (after deducting the *ineligible capital amounts*) in respect of such shares. Thus, if (for example) a company ("A Co") issues shares to a shareholder of another company ("B Co") in exchange for shares in B Co the subscribed capital amount of A Co increases only by the subscribed capital amount attributable to the shares acquired in B Co (calculated after deducting the ineligible capital amount).

### ***"Transitional capital amount"***

This term is only relevant to companies formed before the application date. As noted above, the calculation of the subscribed capital amount based on a moving average will require knowledge of amounts of subscribed capital paid up on shares of a class currently on issue. It was thought that it may be time consuming for companies to identify amounts of paid up capital returned to shareholders on shares previously cancelled.

Therefore, the simplest solution was to include in the subscribed capital amount calculation, a "transitional" amount which would relieve companies from having to identify those amounts. The transitional capital amount is thus simply an amount calculated by multiplying the outstanding shares in each class by the returned capital and share premium amounts determined under the current averaging formula.

## **Section 191WD**

### ***Corporate Amalgamations***

Some corporate amalgamations qualify for particular taxation treatment under this section. The taxation treatment minimises administrative impediments to corporate restructuring through amalgamations by permitting, for example, tax-free asset transfers on amalgamation and preservation of accumulated losses



and imputation credits for use by the amalgamated company. The provision also details the tax consequences for non-qualifying amalgamations.

### **Section 191WD(1)**

This subsection contains a number of definitions relevant to the operation of section 191WD. It limits the particular taxation treatment to "qualifying amalgamations" occurring under the 1955 and 1993 Companies Acts. Each amalgamating company must be an "eligible company" (essentially resident in New Zealand and not exempt from income tax). Amalgamations between qualifying and non-qualifying companies are not qualifying amalgamations.

### **Section 191WD(2)**

Amalgamating companies have up to 63 days from the date documentation evidencing the amalgamation is given to the Company Registrar for registration purposes to give notice of the amalgamation in writing to the Commissioner of Inland Revenue.

### **Section 191WD(3)**

This subsection explains how to calculate the subscribed capital amount of shares issued in the amalgamated company. It has the same effect as item f(vi) in the definition of subscribed capital amount (a separate provision is included here as the term ineligible capital amount referred to in that item relates only to the acquisition of shares).

Except as discussed in relation to subsection (4), generally the subscribed capital amount of the amalgamating company becomes subscribed capital of the amalgamated company. However, a portion of the amalgamating company's subscribed capital may be ineligible to be attributed in this way. This restriction is intended to prevent an amalgamating company increasing the level of its subscribed capital in anticipation of amalgamation with another company, in order to inflate the amount which may be credited to subscribed capital of the amalgamated company. This provision is only triggered to the extent a shareholder in the amalgamating company receives cash or other liquid property for shares converted.

### **Section 191WD(4)**

The effect of this subsection is to subtract the subscribed capital of shares held by an amalgamating company and cancelled upon an amalgamation from the subscribed capital of the amalgamated company. The subscribed capital attributable to the cancelled shares therefore does not form part of the subscribed capital of the amalgamated company.

### **Section 191WD(5)**

The transfer of assets out of an amalgamating company may affect the market value of the shares held by an amalgamating company in that company. The cancellation of the shares and the issue of new shares in the amalgamated company in effect result merely in the gain or loss being transferred to the amalgamated company. Accordingly, this provision prevents that gain or loss from being taken into account by deeming the amalgamating shareholder company to have disposed of the shares at their opening book value (for shares purchased in prior years ) and at cost ( for newly acquired shares ).

### **Section 191WD(6)**

This provision ensures the continuity of the liabilities and rights of an amalgamating company that ceases to exist after the amalgamation. For tax purposes, this ensures continuity of the amalgamating company's objection rights, loss election rights and rights to refunds.

### **Section 191WD(7)**

Income received by the amalgamated company for the provision of services by an amalgamating company is treated as assessable in the recipient's hands if the income would have been assessable to the amalgamating company that provided the services.

### **Section 191WD(8)**

Taxation consequences apply on the transfer of assets in a non-qualifying amalgamation. There is a deemed disposal at market value.

### **Section 191WD(9)**

This subsection contains several provisions relating to the tax treatment of the asset transfers that occur from an amalgamating company to an amalgamated company.

First, it provides for the tax-free transfer of assets other than trading stock at the time of amalgamation. In determining the assessable income that may arise later to the amalgamated company in respect of these assets, the consolidation provisions in section 191N(1) to (4) apply with some modifications.

Second, the transfer of trading stock of the amalgamating company to trading stock of the amalgamated company is treated as a deemed disposal at opening book value (for trading stock on hand) and at cost ( for new acquisitions ). This

prevents movements in the opening and closing values to the date of amalgamation being taken into account by the amalgamating company.

Third, it provides for tax to be payable where an asset is converted from revenue account to capital account on amalgamation. This provision ensures the tax-free treatment of asset transfers is not used to convert assets without taxation consequences.

### **Section 191WD(10)**

This subsection provides for a deemed consideration for the base price calculation required on the transfer of a financial arrangement (of which the amalgamating company is the issuer) to an amalgamated company. In certain circumstances, for example, where the same method of allocating income or expenditure is used by both the amalgamating and amalgamated companies, the deemed consideration is one that results either in a nil allocation or a fair and reasonable allocation. Where a different method of allocation is used, the market price of the financial arrangement is taken into account. This provision is identical to the treatment of financial arrangements of which the amalgamating company is the holder.

### **Section 191WD(11)**

An amalgamating company that ceases to exist may, subject to certain conditions, carry forward any accumulated loss, attributed foreign loss, foreign investment fund loss or tax credit into the amalgamated company. The amalgamated company is allowed to succeed to losses of an amalgamating company only if the shareholder continuity requirement is satisfied with respect to the amalgamating company after the amalgamation, and immediately prior to the amalgamation, offset of the losses of that amalgamating company was allowable against the income of all the other amalgamating companies.

### **Section 191WD(12)**

This subsection provides an ordering rule for the offset of losses and the tax credits referred to in subsection (11) of two or more amalgamating companies against the future income or tax liability of the amalgamated company.

### **Section 191WD(13)**

The liability of an amalgamated company to make provisional tax instalment payments after an amalgamation is based on the residual income tax of the preceding income year of each amalgamating company.

## **Section 191WD(14)**

This subsection contains several provisions relating to debits and credits of an amalgamating company in its imputation credit account, dividend withholding payment account, branch equivalent tax account and policyholder credit account.

First it provides for the pre-amalgamation debits and credits to be treated with effect from the amalgamation as debits and credits of the amalgamated company provided the continuity of shareholding has been maintained.

Second, it provides the mechanism for posting any debits or credits of an amalgamating company that arise after the amalgamation to the equivalent accounts of the amalgamated company.

Finally, it mirrors the limits applying to refunds contained in sections 394M and 394ZO of the Act.

## **Section 327C(1)**

Resident withholding tax on taxable bonus issues (except bonus issues in lieu) will be calculated under paragraph (c). For the purposes of item b of the formula, the dividend paid is the amount which the company elects to transfer to subscribed capital.

Paragraph (d) will be redrafted so that it applies only to a bonus issue in lieu.

## **Section 394E(1) and (2)**

Where a company repurchases shares on-market, a debit arises to that company's imputation credit account. The formula for calculating the amount of the debit is contained in proposed new paragraph (1)(ab). The debit arises on the date of acquisition of the shares. The slice rule automatically applies in calculating the debit amount, i.e. the brightline tests do not apply in relation to an on-market repurchase.

## **Section 394ZW (1)**

This section will be amended to remove the reference to refunds under section 394ZO. This is to accommodate a refund of dividend withholding payment arising on the recovery of a dividend distribution from a corporate shareholder by a non-resident insolvent company.

**DRAFT  
LEGISLATION**



## TAXATION IMPLICATIONS OF COMPANY LAW REFORM - DRAFT LEGISLATION

### Income Tax Act 1976

**OO. Interpretation** - Section 2 of the principal Act is hereby amended by -

(a) Inserting, after the definition of the term "charitable purpose", the following definition:

**"Closely-held company"** means, at any time, a company in respect of which at that time there are 5 or fewer persons (with persons who are associated at the time with each other being treated as one person for this purpose) -

(a) The aggregate of whose direct voting interests (as defined in section 8B of this Act) in the company exceeds 50 percent; or

(b) In any case where at the time a market value circumstance exists in respect of the company, the aggregate of whose direct market value interests (as so defined) in the company exceeds 50 percent:

(b) Omitting from paragraph (d) of the definition of the term "director", the figure "1955" and substituting the figure "1993":

(c) Repealing, from the definition of the term "expenditure on account of an employee", paragraphs (a)(i) and (d):

(d) Inserting, after the definition of the term "life insurance", the following definition -

**"Liquidation"**, in relation to a company, includes -

(a) Removal of the company from the register of companies under the Companies Act 1955 or the Companies Act 1993; and

(b) Dissolution of the company under the Companies Act 1955; and

(c) Termination of the company's existence under any other procedure of law:

(e) In the definition of the term "major shareholder", -

- (i) Omitting the words "private company (as defined in section 2 of the Companies Act 1955)" and substituting the words "closely-held company"; and
  - (ii) Omitting the word "private" from the three other places where it appears:
- (f) Repealing the definitions of the terms "proprietary company" and "winding-up".

**OO. Bonus issues** - (1) Section 3(1) of the principal Act is hereby amended by -

- (a) Repealing the definition of the term "bonus issue" and substituting the following definition -

**"Bonus issue"** means -

- (a) The issue of shares in the company; or
- (b) The giving of credit in respect of the whole or part of the amount unpaid on any shares in the company, -

where the company receives no consideration (other than an election by the shareholder not to receive money or money's worth as an alternative to the issue) for the issue or crediting, except to the extent to which, in respect of any issue or crediting on or before the 20th day of August 1985, such issue or crediting was excluded from the meaning of the term "bonus issue" in accordance with subsection (3) or subsection (4) of this section as those subsections applied from time to time before their repeal by section 31(1) of the Income Tax Amendment Act (No.5) 1988:

- (b) Omitting from the definition of the term "taxable bonus issue" the phrase "subsection (3)(a)(i)" and substituting the phrase "subsection (3)(a)":
  - (c) Repealing the definition of the term "ten year bonus issue":
- (2) Section 3 of the principal Act is hereby further amended by repealing subsection (2).
- (3) Section 3 of the principal Act is hereby further amended by repealing subsection (3) and substituting the following subsection:

"(3) Where a company which is resident in New Zealand (not being a company which, pursuant to a provision of arrangements to which effect is given by an Order in Council made under section 294 of this Act, is treated as not being resident in New Zealand for the purpose of the arrangements) proposes to make a bonus issue, other than a bonus issue in lieu, -

"(a) The company may elect, by -

- "(i) Resolving, upon the making of the bonus issue, -



"(A) That the bonus issue will be a taxable bonus issue; and

"(B) The amount (being greater than nil) which will be treated as a dividend in respect of the bonus issue; and

"(ii) Notifying the Commissioner of the election and the amount, under section 13A of this Act, -

that the bonus issue will be a taxable bonus issue (in which case the bonus issue will be treated as a dividend under section 4(1)(f) of this Act); and

"(b) If the company fails to make an election under paragraph (a) of this subsection, the bonus issue shall be deemed to be a non-taxable bonus issue."

**OO. Meaning of the term "dividends"** - (1) Section 4(1) of the principal Act is hereby amended by -

(a) Omitting from paragraph (a) the words "or that are specified payments":

(b) Repealing paragraph (ba)(ii) and substituting the following subparagraph -

"(ii) The shareholder has been released from the obligation to pay that amount by the operation of the Insolvency Act 1967, the Companies Act 1955, the Companies Act 1993 or the laws of a country or territory other than New Zealand or by any deed or agreement of composition with the shareholder's creditors; or":

(c) Omitting, from paragraph (f), the words "(as defined in subsection (3) of this section)":

(d) Repealing paragraph (g) and substituting the following paragraph -

"(g) All amounts (whether in money or money's worth) distributed in any manner and under any name from and in respect of any -

"(i) Acquisition by the company of shares in the company; or

"(ii) Redemption or other cancellation of shares in the company; or

"(iii) Other reduction in or return of share capital of the company:"

(e) Omitting from paragraph (k) the words "proprietary company" and substituting the words "closely-held company".

(2) Section 4(3) of the principal Act is hereby amended by repealing the definition of the term "specified payments".

(3) Section 4 of the principal Act is hereby further amended by repealing subsection (6) and substituting the following subsection -

"(6) The amount of the dividend arising in respect of -

- (a) A bonus issue in lieu shall be the amount of the money or money's worth offered as an alternative to the bonus issue less, in the case of a bonus issue made to a shareholder where an amount of resident withholding tax is deducted in respect of the bonus issue in accordance with Part IXA of this Act, that amount of resident withholding tax; and
- (b) Any other taxable bonus issue shall be such amount per share as the company elects when resolving upon the bonus issue."

(4) Section 4 of the principal Act is hereby further amended by inserting, after subsection (7), the following subsection -

"(7A) Where any dividend paid or provided by a company to a shareholder is subsequently recovered by the company from the shareholder under section 56 of the Companies Act 1993 (or the equivalent provision of any company legislation of a country or territory other than New Zealand), -

(a) The Commissioner shall, if notified in writing of the recovery -

- (i) Notwithstanding anything in section 25 of this Act, amend any assessment of the shareholder for income tax, any determination of loss or loss carried forward of the shareholder, any assessment of the shareholder made under Part XIIB of this Act or any assessment of the company made under Parts IX, IXA and XIIA of this Act or by virtue of section 308A(3) of this Act; and
- (ii) Notwithstanding anything in section 409 or 394ZO of this Act but otherwise subject to this Act, refund to the shareholder any income tax, dividend withholding payment (as defined in section 394ZK of this Act) or dividend withholding payment penalty tax (as defined in section 394ZZG of this Act) and to the company any non-resident withholding tax or resident withholding tax; and

(b) A credit or debit (as the case may be) shall arise, as at the date of recovery, to be recorded in the imputation credit account (as defined in section 394A of this Act) of the company or (in any case where the shareholder is an imputation credit account company (as so defined) or dividend withholding payment account company (as defined in section 394ZK of this Act)) the imputation credit account or dividend withholding payment account (as defined in section 394ZK of this Act) of the shareholder -

to such extent as is necessary in order, for the purposes of this Act, to disregard the dividend and any imputation credit (as defined in section 394A of this Act) or dividend withholding payment credit (as so defined) attached to the dividend and take into account the resultant refunds."

(5) Section 4 of the principal Act is hereby further amended by repealing subsection (12) and substituting the following subsection -

"(12) For the purposes of this Act, where any acquisition of shares in a company by a person (other than the company) is deemed, under section 99(5) of this Act, to be a dividend, the dividend shall be deemed to be an on-market acquisition (as defined in section 4A(2) of this Act) by the company if the dividend would have been an on-market acquisition had the person been the company.

(6) Section 4 of the principal Act is hereby further amended by repealing subsection (15) and substituting the following subsection -

"(15) Notwithstanding any provision of this Act, where any dividend is derived by a person -

"(a) If the dividend is from and in respect of the acquisition, redemption or other cancellation by the company of a share in the company and any profit derived by the person from the acquisition, redemption or other cancellation would be assessable income of the person under section 65(2)(a) or (e) of this Act, the profit shall be assessable income of the person under section 65(2)(a) or (e) of this Act only to the extent (if any) to which it exceeds the amount of the dividend (exclusive of any imputation credit (as defined in section 394A of this Act) or dividend withholding payment credit (as defined in section 394ZK of this Act) attached to the dividend); and

"(b) The dividend shall not be treated as assessable income of the person under any provision of this Act other than section 65(2)(j) so as to result in double taxation of the person, except where the provision expressly or by necessary implication so provides and, for the avoidance of doubt but without limiting the application of this subsection, section 198 of this Act shall be treated as a provision which expressly so provides."

**OO. Exclusion from term "dividends"** - (1) Section 4A(1) of the principal Act is hereby amended by repealing paragraph (c) and substituting the following paragraphs:

"(c) Any amount (whether in money or money's worth) returned upon the acquisition, redemption or other cancellation (in whole but not in part) by the company of any share in the company (other than upon the liquidation of the company) (referred to in this paragraph as the relevant cancellation) where -

"(i) If the share is not a fixed rate share (as defined in subsection (3) of this section), -

"(A) The relevant cancellation is as a result of a prorata offer (as so defined) where the company has a fifteen percent capital reduction (as so defined); or

"(B) The relevant cancellation is not as a result of a prorata offer but the shareholder suffers a fifteen percent interest reduction (as so defined); and

"(ii) If the share is a fixed rate share -

"(A) The share was not issued or acquired by the shareholder under an arrangement for the company to acquire, redeem or otherwise cancel fixed rate shares; and

"(B) The relevant cancellation was not made, -

in lieu of the payment of dividends on shares other than fixed rate shares, whether in whole or in part; and

"(iii) The Commissioner is satisfied that neither the whole nor any part of the relevant cancellation was made in lieu of the payment of dividends, having regard to -

"(A) The nature and amount of dividends paid by the company prior or subsequent to the relevant cancellation;

"(B) The issue, or proposed issue, of shares in the company subsequent to the relevant cancellation;

"(C) The expressed purpose or purposes of the relevant cancellation; and

"(D) Any other relevant factor; and

"(iv) To the extent to which the amount returned does not exceed the amount calculated in accordance with the following formula -

$$(a + b) \times c$$

where -

*a* is the subscribed capital amount (as defined in subsection (3) of this section); and

*b* is -

(A) In any case where the share is not a fixed rate share, the excess return amount; and

(B) In any case where the share is a fixed rate share, nil; and

*c* is -

(A) In any case where the amount returned on the relevant cancellation is less than the market value of the share at the time at which notice is first given by the company to the shareholder or, in any case where the relevant cancellation is proposed by the shareholder, by the shareholder to the company proposing the relevant cancellation, the fraction calculated by dividing the amount returned by the said market value of the share; and

(B) In any other case, 1.

"(ca) Any amount (whether in money or money's worth) returned upon the redemption or other cancellation of any share in the company upon the liquidation of the company to the extent that the amount returned does not exceed the aggregate of -

"(i) The subscribed capital amount (as defined in subsection (3) of this section); and

"(ii) The excess return amount (as so defined):

"(cb) Except for the purposes of sections 4(7A) and (12), 99(5) and 394E(1)(ab) and (2)(ab) of this Act, any amount returned upon an on-market acquisition by the company of any share in the company:"

(2) Section 4A(1) of the principal Act is hereby further amended by repealing paragraph (h).

(3) Section 4A(2) of the principal Act is hereby amended by -

(a) In the definition of the term "capital gain amount" -

(i) Omitting, from each place where the words appear, the words "winding up" and substituting the word "liquidation"; and

(ii) Omitting the phrase "subsection (1)(c)" and substituting the phrase "subsection (1)(ca)":

(b) Repealing the definition of the term "non-qualifying capital" and substituting the following definition -

**"On-market acquisition"** means an acquisition by a company of a share in the company where -

(a) The company acquires the share per medium of a broker in a recognised exchange (as defined in section 8B of this Act) or some other similar agent independent of the company; and

(b) As a result, at the time of the acquisition the shareholder is not aware that the acquirer of the share is the company:"

(c) In the definition of the term "shares of the same class", repealing paragraph (b)(ii), (iii) and (iv) and substituting the following subparagraph -

"(ii) Distributions of assets of the company on any acquisition, redemption or other cancellation by the company of its shares or other reduction in or return of share capital of the company, whether on its liquidation or otherwise:"

(d) Repealing the definition of the term "specified payments".

(4) Section 4A of the principal Act is hereby further amended by repealing subsections (3), (3A) and (4) and substituting the following subsections -

"(3) For the purposes of this subsection and paragraphs (c) and (ca) of subsection (1) of this section, in relation to a share and a company referred to in those paragraphs, -

"**Excess return amount**" means the amount calculated in accordance with the following formula -

$$\frac{d + e}{f}$$

where -

*d* is the aggregate of capital gain amounts of the company available for distribution to shareholders at the time of the acquisition, redemption or other cancellation (referred to in this definition as the relevant cancellation); and

*e* is, in any case where the relevant cancellation is upon the liquidation of the company, the total market value of capital assets of the company received by shareholders at the time of the relevant cancellation, to the extent such total market value exceeds the aggregate of -

- (i) The total cost to the company of such assets; and
- (ii) The total capital losses arising from the realisation of capital assets (other than realisations to which subsection (9) of this section applies) incurred in the income year in which the capital assets were received by the shareholders, in any subsequent income year or in any preceding income year (being a preceding income year that commences on or after the 1st day of April 1994), not being losses already taken into account under subsection (11) of this section in calculating capital gain amounts, -

and, in any other case, nil; and

*f* is the number of shares (other than fixed rate shares) in the company on issue at the time of the relevant cancellation:

"**Fixed rate share**" means a share where -

- (a) The only dividend payable (disregarding any dividend payable on issue of the share) in respect of the share is payable at a rate which is -
  - (i) A specific fixed percentage of the amount subscribed in respect of the issue of the share; or
  - (ii) A percentage of the amount subscribed in respect of the issue of the share which is determined by a fixed relationship to economic, commodity, industrial or financial indices, or to banking rates or general commercial rates of interest; or

- (iii) A percentage that would be of a kind referred to in subparagraph (i) or subparagraph (ii) of this paragraph but for any variation in the rate of dividend that may occur only -
  - (A) By a fixed relationship to a rate of income tax; or
  - (B) As may be necessary to compensate the shareholder for any default on the part of the paying company or any expenditure or loss suffered by the shareholder (or a person associated with the shareholder) in respect of the holding of the share; and
- (b) Such rate is not set with a purpose and does not have an effect of defeating the intent and application of subsection (1)(c)(i) or (ii) of this section; and
- (c) The holder of the share does not have, in respect of that share, any shareholder decision-making rights (as defined in section 8B of this Act) except to the extent of any such right which -
  - (i) Arises only in circumstances where the position of the holder of the share may be altered to the holder's detriment; and
  - (ii) Is granted to the holder of the share for the purpose of assisting that holder to prevent such alteration; and
  - (iii) At the time of issue of the share is not expected to arise:

**"Fifteen percent capital reduction"** means, in respect of any company and any prorata offer, where the aggregate amount paid to those persons who accept the offer is equal to or greater than 15 percent of the market value of all shares in the company at the time the company first notified shareholders of the offer:

**"Fifteen percent interest reduction"** means, in respect of any company and any acquisition, redemption or other cancellation (referred to in this definition as the relevant cancellation) by the company of any share of a shareholder in the company, where, as a result of the relevant cancellation (together with any other acquisitions, redemptions or other cancellations of shares (other than fixed rate shares) in the company occurring at the same time), the aggregate voting interests in the company immediately after the relevant cancellation of the shareholder and all persons associated with the shareholder (not being persons associated with the shareholder merely by virtue of being relatives of the shareholder, unless a spouse or minor child of the shareholder or a trustee for such spouse or minor child) (the counted associates being referred to in this definition as the relevant associates) do not exceed 85% of the aggregate voting interests in the company of the shareholder and the relevant associates immediately before the relevant cancellation and, in any case where at the time of the relevant cancellation a market value circumstance exists in respect of the company, the aggregate market value interests in the company of the shareholder and the relevant associates immediately after the relevant

cancellation do not exceed 85% of the aggregate market value interests of the shareholder and the relevant associates immediately before the relevant cancellation:

"**Fully credited**" means, in respect of any dividend, that part of the dividend which is calculated by multiplying the dividend (exclusive of any imputation credit (as defined in section 394A(1) of this Act) or dividend withholding payment credit (as so defined) attached to the dividend) by the lesser of 1 and the following fraction -

$$\frac{a}{b}$$

where -

*a* is the combined imputation ratio (as so defined) and dividend withholding payment ratio (as defined in section 394ZK(1) of this Act) of the dividend; and

*b* is the maximum imputation ratio specified in section 394G(1) of this Act:

"**Ineligible capital amounts**" means, in any case where a company (referred to in this definition as the acquiring company) issues shares for consideration received, directly or indirectly and whether by one or a series of transactions, in the form of shares in another company (referred to in this definition as the acquired company), subscribed capital amounts of shares in the acquired company to the extent that -

(a) Such subscribed capital amounts are attributable to shares issued -

(i) In anticipation of the acquisition by the acquiring company of the shares in the acquired company; and

(ii) In consideration for cash or other liquid property; and

(b) Such subscribed capital amounts do not exceed consideration provided or to be provided in the form of cash or other liquid property (not being shares in the acquiring company) by the acquiring company in consideration for the acquisition of shares in the acquired company:

"**Prorata offer**" means an offer by a company to all persons holding shares (other than fixed rate shares) in the company to acquire, redeem or otherwise cancel all or part only of each such person's shares (other than fixed rate shares) in the company where, if each such person were to accept the offer, the resultant acquisition, redemption or other cancellation would not alter the voting interest (or, in any case where at the time a market value circumstance exists in respect of the company, market value interest) of any person in the company:

"**Subscribed capital amount**" means the amount calculated in accordance with the following formula:



$$\frac{e + f - g}{h}$$

where -

*e* is -

- (i) In the case of any company which existed before the [application date], the transitional capital amount; and
- (ii) In any other case, nil; and

*f* is the aggregate amount of consideration received by the company on or after the [application date] and prior to the acquisition, redemption or other cancellation, in respect of the issue of all shares in the company of the same class as the share being acquired, redeemed or otherwise cancelled (referred to in this subsection as the specified class), including as consideration -

- (i) In the case of any bonus issue in lieu made on or after the [application date], the amount of money or money's worth offered as an alternative to such bonus issue; and
- (ii) In the case of any taxable bonus issue (other than a bonus issue in lieu) made on or after the [application date], the amount of the dividend arising in respect of the taxable bonus issue, -

but not including -

- (iii) Any amount in respect of any other bonus issue; or
- (iv) Any amount in respect of any taxable bonus issue (except to the extent fully credited) made to a shareholder who was exempt from income tax in respect of the bonus issue under section 63 of this Act; or
- (v) Any consideration received by the company which is primarily attributable, directly or indirectly, to the payment by the company (or by any other company associated at the time of payment with the company) of a dividend (except to the extent fully credited) to a shareholder who was -
  - (A) Exempt from income tax under section 63 of this Act; and
  - (B) Not required by section 394ZL of this Act to deduct an amount by way of dividend withholding payment, -

in respect of the dividend; or

- (vi) The amount of any consideration received by the company, directly or indirectly and whether by one or a series of transactions, in the form of shares in another company to the extent to which such consideration exceeds the aggregate subscribed capital amounts (calculated after deducting ineligible capital amounts) in respect of such shares in the other company at the date of the receipt; or
- (vii) Any amount included in calculating the transitional capital amount in respect of the company; and

*g* is the aggregate amount of subscribed capital amounts returned -

- (i) Upon the acquisition, redemption or other cancellation by the company of shares in the company of the specified class; and
- (ii) On or after the [application date] and before the relevant acquisition, redemption or other cancellation; and
- (iii) Excluded from the meaning of the term "dividends" by subsection (1)(c) or (ca) of this section; and

*h* is the aggregate number of shares of the specified class on issue immediately before the time of the acquisition, redemption or other cancellation:

**"Transitional capital amount"** means the amount calculated in accordance with the following formula -

$$\frac{i+j}{k} \times l$$

where -

*i* is the aggregate amount of capital paid up before the [application date] in respect of shares of the specified class (whenever issued), not being -

- (i) An amount paid up by a bonus issue made after the 31st day of March 1982 and before the 1st day of October 1988, except where -
  - (A) The date of the acquisition, redemption or other cancellation falls more than ten years after the date of the bonus issue; or
  - (B) The amount was paid-up by way of application of any capital gain amount or amount of qualifying share premium; or
- (ii) An amount paid up by a bonus issue (other than a taxable bonus issue) made on or after the 1st day of October 1988, except where the amount was paid-up by way of

application of any capital gain amount or amount of qualifying share premium; and

- j* is the aggregate amount of qualifying share premium paid to the company before the [application date] in respect of shares of the specified class (whenever issued), not being an amount subsequently (before the [application date]) applied to pay up capital on shares in the company; and
- k* is the number of shares in the specified class ever issued before the close of the [day preceding the application date]; and
- l* is the number of shares in the specified class on issue at the close of the [day preceding the application date].

"(4) For the purposes of subsection (1)(c) and (ca) of this section, in determining the amount not included within the term "dividends" on any acquisition, redemption or other cancellation by the company of a share in the company (whether upon liquidation of the company or otherwise), where any consideration paid to the company (in money or money's worth) in respect of the issue of shares in the company is denominated and payable in a currency other than New Zealand currency, the consideration paid to the company shall be deemed to be equal to the consideration paid in the currency other than New Zealand currency converted into New Zealand currency as if that consideration had been paid on the date of the acquisition, redemption or other cancellation.

(5) Section 4A(6) of the principal Act is hereby amended by omitting the phrase "subsection (1)(c)" and substituting the phrase "subsection (1)(ca)".

(6) Section 4A(7) of the principal Act is hereby amended by omitting the phrase "subsection (1)(c)" and substituting the phrase "subsection (1)(ca)".

(7) Section 4A(8)(a)(ii) of the principal Act is hereby amended by omitting the word "made" and substituting the word "realised".

(8) Section 4A(10) of the principal Act is hereby amended by -

- (a) Omitting the words "private company within the meaning of the Companies Act 1955" and substituting the words "closely-held company":
- (b) Omitting the words "winding up" and substituting the word "liquidation".

(9) Section 4A(11) of the principal Act is hereby amended by -

- (a) Omitting the phrase "subsection (1)(c)" and substituting the phrase "subsection (1)(c) and (ca)":
- (b) Omitting the words "a profit or gain which is not included in the assessable income of the company for any income year" and substituting the words "capital gain amounts".

**OO. Meaning of term source deduction payment** - Section 6 of the principal Act is hereby amended by omitting, from each place where it appears, the word "private" and substituting in each place the words "closely-held".

**OO. Defining when a company is under the control of any persons** - Section 7 of the principal Act is hereby repealed and the following section inserted -

**"7. Defining when company is under control of any persons** - (1) For the purposes of this Act, a company shall be deemed to be under the control at any time of the persons -

"(a) The aggregate of whose direct voting interests (as defined in section 8B of this Act) in the company at the time exceeds 50 percent; or

"(b) In any case where at the time a market value circumstance exists in respect of the company, the aggregate of whose direct market value interests (as so defined) in the company at the time exceeds 50 percent; or

"(c) Who have at the time control of the company by any other means whatsoever.

"(2) For the purposes of this section, where any person (referred to in this subsection as the nominee) holds any rights at any time on behalf of or to the order of another person, the rights shall be deemed to be held at the time by the other person as well as by the nominee, as if the nominee, the other person and all other such nominees of the other person were at the time a single person."

**OO. Defining when 2 persons are associated persons** - Section 8 of the principal Act is hereby repealed and the following section substituted -

**"8. Defining when 2 persons are associated persons** - (1) For the purposes of this Act, unless the context otherwise requires, at any time associated persons or persons associated with each other are -

"(a) 2 companies where at the time there is a group of persons -

"(i) The aggregate of whose voting interests in each company is equal to or exceeds 50 percent; or

"(ii) In any case where at the time a market value circumstance exists in respect of either company, the aggregate of whose market value interests in each company is equal to or exceeds 50 percent; or

"(iii) Who have control of both companies by any other means whatsoever; or

"(b) A company and any person (other than a company) where at the time -

"(i) The person has a voting interest in the company equal to or exceeding 25 percent;  
or

"(ii) In any case where at the time a market value circumstance exists in respect of the company, the person has a market value interest in the company equal to or exceeding 25 percent; or

"(c) 2 persons who are at the time relatives; or

"(d) A partnership and any person who is -

"(i) At the time a partner in the partnership; or

"(ii) A person associated at the time (under any of the other provisions of this subsection) with a partner in the partnership.

"(2) For the purposes of subsection (1)(a) and (b) of this section, where any person (referred to in this subsection as the nominee) holds any rights at any time -

"(a) On behalf of or to the order of another person; or

"(b) Being a relative at the time of another person, -

the rights shall be deemed to be held at the time by the other person as well as by the nominee, as if the nominee, the other person and all other such nominees of the other person were at the time a single person.

**OO. Interpretation - voting and market value interests** - Section 8B of the principal Act is hereby amended by -

(a) Repealing the definition of the term "closely-held company":

(b) Omitting from the definition of the term "shareholder decision-making rights" the phrase "winding-up" and substituting the word "liquidation".

**OO. Commissioner may in certain cases demand special returns, and make special assessments** - Section 12(1)(f) of the principal Act is hereby amended by omitting the words "wound up" and substituting the word "liquidated".

**OO. Incomes wholly exempt from tax** - Section 61(34) of the principal Act is hereby amended by omitting the words "memorandum, articles of association" and substituting the word "constitution".

**OO. Income and expenditure where financial arrangement redeemed or disposed of** -

Section 64F(1)(c)(ii) of the principal Act is hereby amended by omitting the words "or by any deed" and substituting the words "or the Companies Act 1993 or the laws of any country or territory other than New Zealand or by any deed or agreement".

**OO. Shareholder-employee and shareholder superannuation contributions etc.** - Section 65A of the principal Act is hereby repealed.

**OO. Profits or gains from land transactions** - (1) Section 67(2) of the principal Act is hereby amended by repealing paragraphs (a) and (b) and substituting the following paragraphs -

"(a) Any 2 companies where there is a group of persons -

"(i) The aggregate of whose voting interests in each company is equal to or exceeds 50 percent; or

"(ii) In any case where a market value circumstance exists in respect of either company, the aggregate of whose market value interests in each company is equal to or exceeds 50 percent; or

"(iii) Who have control of both companies by any other means whatsoever; or

"(b) A company and any person (other than a company) where -

"(i) The person; and

"(ii) Any spouse of the person; and

"(iii) Any infant child of the person; and

"(iv) Any trustee for such spouse or infant child, -

have, when aggregated, a voting interest in the company equal to or exceeding 25 percent or, in any case where a market value circumstance exists in respect of the company, a market value interest in the company equal to or exceeding 25 percent; or"

(2) Section 67 of the principal Act is hereby further amended by repealing subsection (3) and substituting the following subsection -

"(3) For the purposes of subsection (2)(a) and (b) of this section, where any person (referred to in this subsection as the nominee) holds, directly or indirectly, any rights at any time on behalf of or to the order of another person, the rights shall be deemed to be held by the other person as well as by the nominee, as if the nominee, the other person and all other such nominees of the other person were at the time a single person.

**OO. Amounts remitted to be taken into account in computing income** - Section 78(2)(b) of the

principal Act is hereby amended by omitting the words ", or by any deed" and substituting the words "or the Companies Act 1993 or the laws of any country or territory other than New Zealand or by any deed or agreement".

**OO. Payment of excess salary or wages etc** - Section 97(1)(a) of the principal Act is hereby amended by omitting the word "proprietary" and substituting the words "closely-held".

**OO. Certain deductions not permitted** - Section 106(1) of the principal Act is hereby amended by repealing paragraph (j) and substituting the following paragraph -

"(j) Any expenditure or loss to the extent to which it is of a private or domestic nature:"

**OO. Gifts of money by companies not closely-held** - Section 147 of the principal Act is hereby amended by -

(a) Repealing subsection (1):

(b) Omitting, from subsection (2) in each place where the phrase appears, the phrase "public company" and substituting in each place the phrase "company (not being a closely-held company)".

**OO. Contributions to employees' superannuation schemes** - Section 150 of the principal Act is hereby amended by repealing subsection (1)(d) and (e) and subsections (2) and (3) to (7).

**OO. Pensions payable to former employees** - Section 151(2) of the principal Act is hereby amended by omitting the word "proprietary" and substituting the words "closely-held".

**OO. Notional interest on loans made to employees under employee share purchase scheme** - Section 166 of the principal Act is hereby amended by repealing subsections (2) and (3).

**OO. Refund from income equalisation reserve account of company on winding-up** - Section 183 of the principal Act is hereby amended by -

(a) Omitting the words "wound up" and substituting the word "liquidated":

(b) Omitting the words "winding up" from both places where those words appear and substituting in each case the word "liquidation".

**OO. Losses incurred may be set off against future profits** - Section 188(6) of the principal Act is hereby amended by inserting, after the words "Companies Act 1955", the words "or the Companies Act 1993 or the laws of any country or territory other than New Zealand".

**OO. Excessive remuneration by proprietary company to shareholder, director or relative** - Section 190 of the principal Act is hereby amended by omitting the word "proprietary" and substituting the words "closely-held".

**OO. Amalgamation** - The principal Act is hereby amended by inserting the following heading and section after section 191WC of the principal Act -

### **"Amalgamation**

**"191WD. Amalgamation of companies** - (1) For the purposes of this section -

**"Amalgamated company"** means the one company which is the result of and continues after an amalgamation, which may be one of the amalgamating companies or a new company:

**"Amalgamating companies"** means the two or more companies which amalgamate under an amalgamation:

**"Amalgamation"** means any amalgamation under Part VA or VC of the Companies Act 1955 or Part XIII or XV of the Companies Act 1993 or the law of any country or territory other than New Zealand which is to the same or similar effect, whereby two or more companies amalgamate and continue as one company:

**"Financial arrangement"** has the meaning assigned to that term by section 64B(1) of this Act:

**"Issuer"** has the meaning assigned to that term by section 64B(1) of this Act:

**"Qualifying amalgamation"** means any amalgamation where -

"(a) Each of the amalgamating companies and the amalgamated company is an eligible company (as defined in section 191D of this Act); and

"(b) If any of the amalgamating companies is a qualifying company (as defined in section 393B of this Act), each of the amalgamating companies and the amalgamated company is a qualifying company:

**"Trading stock"** has the meaning assigned to that term by section 85(1) of this Act.

"(2) Where an amalgamation occurs, each amalgamating company shall, within 63 working days of the date upon which documents evidencing the amalgamation are delivered to the Registrar of Companies for registration under Part VA or VC of the Companies Act 1955 or Part XIII or XV of the Companies Act 1993 (or the date upon which the equivalent procedure occurs under foreign law), give notice in writing to the Commissioner in such form as the Commissioner may approve, detailing -

"(a) The name and tax file number (if any) of each amalgamating company and the amalgamated company; and



"(b) The date upon which the amalgamation has effect; and

"(c) In any case where the amalgamated company has a non-standard balance date, the non-standard balance date; and

"(d) Such other information as the Commissioner may require.

"(3) Where any amalgamated company issues any shares on an amalgamation in consideration for the cancellation of or in respect of the conversion of any shares (not being shares held by another amalgamating company) in an amalgamating company, for the purposes of this Act in calculating the subscribed capital amount (as defined in section 4A(3) of this Act) of those shares of the amalgamated company, the aggregate consideration for which those shares of the amalgamated company have been issued shall be deemed to be equal to the aggregate subscribed capital amounts of those shares of the amalgamating company at the date of the amalgamation, after deducting any such subscribed capital amounts attributable to shares issued -

"(a) In anticipation of the amalgamation; and

"(b) In consideration for cash or other liquid property, -

which do not exceed, in aggregate, consideration provided or to be provided in the form of cash or other liquid property (not being shares in the amalgamated company) to the holders of shares in the amalgamating company in consideration for the amalgamation.

"(4) Where -

"(a) Any shares in an amalgamated company held by an amalgamating company are cancelled on an amalgamation; and

"(b) Any other shares of the same class (as defined in section 4A(2) of this Act) held by persons other than an amalgamating company remain on issue notwithstanding the amalgamation, -

for the purposes of this Act in calculating the subscribed capital amount (as defined in section 4A(3) of this Act) of shares of that class on issue after the amalgamation, the amount of item *g* in the definition of the term subscribed capital amount in section 4A(3) of this Act shall be increased by the amount calculated in accordance with the following formula -

$$a \times b$$

where -

*a* is the number of shares cancelled; and

*b* is the subscribed capital amount of each such share immediately prior to the amalgamation.

"(5) Where shares in any amalgamating company are -

"(a) Held by an amalgamating company; and

"(b) Trading stock of the shareholder or otherwise shares in respect of which any profit or gain derived on disposition would be required to be taken into account in calculating the assessable income of the shareholder; and

"(c) Cancelled on the amalgamation, -

for the purposes of this Act, the shares shall be deemed to have been disposed of by the shareholder immediately prior to the amalgamation for a consideration equal to -

"(d) In any case of trading stock held by the shareholder at the beginning of the income year in which the amalgamation takes place, the value of such trading stock at the beginning of the income year as determined under section 85 of this Act; or

"(e) In any other case, the cost to the shareholder of the shares.

"(6) Where any amalgamating company ceases to exist on an amalgamation, the amalgamated company shall, in accordance with section 209G of the Companies Act 1955 or section 225 of the Companies Act 1993, comply with all obligations of, and be entitled to all rights of, the amalgamating company under this Act with respect to the income year in which the amalgamation occurs and all preceding income years.

"(7) Where and to the extent that -

"(a) Any amalgamating company ceases to exist on an amalgamation; and

"(b) Before the amalgamation the amalgamating company supplies any services; and

"(c) The consideration in respect of those services is received by the amalgamated company after the amalgamation; and

"(d) The consideration would have been assessable income of the amalgamating company but is not, but for this subsection, assessable income of the amalgamated company, -

the consideration shall be assessable income of the amalgamated company.

"(8) Where any amalgamated company, on an amalgamation other than a qualifying amalgamation, acquires any property of an amalgamating company, or succeeds to any obligations of an amalgamating company in respect of a financial arrangement of which the amalgamating company was the issuer, for the purposes of this Act, -

"(a) The amalgamating company shall be treated as having disposed of the property or relieved itself of the obligations immediately before the amalgamation; and

"(b) The amalgamated company shall be treated as having acquired the property or assumed the obligations immediately after the amalgamation, -

for a consideration equal to the market value of the property, or market price for assuming such obligations, at the time.

"(9) Where any amalgamated company, on a qualifying amalgamation, acquires any property of an amalgamating company, for the purposes of this Act -

"(a) Except where paragraph (c) of this subsection applies, section 191N(1) to (4) of this Act shall apply as if -

"(i) The amalgamating company had disposed of the property and the amalgamated company had acquired the property at the time of the amalgamation; and

"(ii) The amalgamating company and the amalgamated company were at the time and at all times thereafter members of the same consolidated group; and

"(iii) The amalgamated company were the nominated company (as defined in section 191D of this Act) for the consolidated group; and

"(iv) The amalgamated company's return of income were the consolidated group's return of income; and

"(v) The reference in section 191N(4)(a)(iv) to deduction of such loss from the assessable income of the consolidated group for the income year under section 191O of this Act were instead a reference to deduction of such loss from the assessable income of the amalgamated company for the income year under subsection (11) of this section; and

"(b) Where the property is trading stock for both the amalgamating company and the amalgamated company, the amalgamating company shall be deemed to have disposed of the trading stock and the amalgamated company shall be deemed to have acquired the trading stock -

"(i) In any case of trading stock held by the amalgamating company at the beginning of the income year in which the amalgamation takes place, the value of such trading stock at the beginning of the income year as determined under section 85 of this Act; or

"(ii) In any other case, the cost to the amalgamating company of the trading stock; and

"(c) In any case where the property is either trading stock of the amalgamating company or otherwise property in respect of which any profit or gain on disposition would be required (other than under section 117 of this Act) to be taken into account in calculating assessable income of the amalgamating company (referred to in this paragraph as revenue property) and is neither trading stock nor revenue property of the amalgamated company, the

amalgamating company shall be deemed to have disposed of the property and the amalgamated company shall be deemed to have acquired the property at the time of the amalgamation for a consideration equal to its market value at the time.

"(10) Where any amalgamated company succeeds, on a qualifying amalgamation, to the obligations of an amalgamating company in respect of a financial arrangement to which sections 64B to 64L of this Act apply of which the amalgamating company was the issuer, then, notwithstanding section 64J of this Act, for the purposes of this Act -

"(a) In any case where -

"(i) The method of calculating expenditure or income in respect of the financial arrangement under section 64C of this Act remains the same notwithstanding the amalgamation; and

"(ii) The amalgamated company so elects by filing accordingly its return of income for the income year; and

"(iii) Neither the amalgamating company nor the amalgamated company is entitled, under section 188 of this Act, to claim to carry forward to the income year and deduct or set off any loss incurred by it in any preceding income year (except where the whole of such loss may be deducted from the assessable income of the amalgamated company for the income year under subsection (11) of this section), -

with respect to the income year in which the amalgamation takes place and each subsequent income year -

"(iv) The amalgamating company shall be treated as if it had never been the issuer of the financial arrangement prior to the amalgamation, with the result that section 64F of this Act does not apply to the amalgamating company with respect to the succession; and

"(v) The amalgamated company shall be treated as if it had -

"(A) Issued the financial arrangement at the same time and for the same acquisition price as the amalgamating company; and

"(B) Incurred all expenditure and derived all other gains incurred or derived by the amalgamating company with respect to the financial arrangement before the succession; and

"(C) Included in its returns of income under this Act the same amounts of expenditure and income with respect to the financial arrangement as were included by the amalgamating company; and

- "(b) In any other case where the method of calculating income or expenditure in respect of the financial arrangement under section 64C of this Act remains the same notwithstanding the amalgamation, the consideration for which the succession has taken place shall be deemed to be equal to such amount as will result in the base price adjustment in relation to the amalgamating company calculated in respect of the succession under section 64F of this Act being such amount (whether negative, positive, or a nil amount) as will result effectively in a fair and reasonable allocation, having regard to the tenor of section 64C of this Act, between the amalgamating company and the amalgamated company, of the expenditure or income which would have been deemed to be incurred or derived by the amalgamating company in respect of the financial arrangement in the income year in which the amalgamation takes place had the amalgamation not taken place; and
- "(c) In any other case, the consideration for which the succession takes place shall be deemed to be equal to the market price for which an assumption of such obligations would have taken place at the date of amalgamation.
- "(11) Where -
- "(a) Any amalgamating company ceases to exist on a qualifying amalgamation; and
- "(b) The amalgamating company has, in respect of an income year (referred to in this subsection as the income year of loss), incurred a loss, an attributed foreign loss (as defined in section 245A of this Act) or a foreign investment fund loss (as so defined) or a tax credit available for crediting under section 245K(1) of this Act; and
- "(c) The loss has not, under section 188, 191A, 245M, 245N, 245RJ or 245RK of this Act, been deducted from or set off against assessable income derived by the amalgamating company or any other company in any period prior to the amalgamation (including any part of the income year in which the amalgamation takes place) or the tax credit has not, under section 245K or 245L of this Act, been credited against the income tax payable by any such company in respect of any such period; and
- "(d) Under section 191A, 245N or 245RK of this Act, the loss could have been deducted from, or set off against, assessable income (on the assumption that there was sufficient such income) derived, in that part of the income year of the relevant company which ends with the date of the amalgamation, by each of the amalgamated company (unless it is a company incorporated only on the amalgamation) and any company which has, at any time prior to or during the income year in respect of which the loss is deducted or set off under this subsection, amalgamated with the amalgamated company or, under section 245L of this Act, the credit could have been credited against income tax payable (if any) in respect of such period by such companies, -

the loss shall be treated as if incurred by the amalgamated company and may be deducted from or set off against, under section 188, 191A, 245M, 245N, 245RJ or 245RK of this Act, or the tax credit shall be treated as a tax credit of the amalgamated company and may be credited, under section 245K or 245L of this Act, against income tax payable in respect of, assessable income

derived by the amalgamated company or any other company in periods commencing on or after the amalgamation but applying section 188 and 191A(1)(b) of this Act (and any other provisions of this Act the application of which is dependent upon the application of those provisions) as if, with respect to all periods prior to the amalgamation, the amalgamated company did not separately exist and was instead the amalgamating company with the same holders of shares and options over shares as the amalgamating company.

"(12) Where losses incurred by or tax credits of two or more amalgamating companies are permitted under subsection (11) of this section to be deducted from, or set off against income tax payable in respect of, the assessable income derived in an income year by the amalgamated company, those losses or tax credits shall -

"(a) If incurred, or resulting from tax payable, in 2 or more income years, be deducted in the same order as incurred or arising; and

"(b) If incurred, or resulting from tax payable, in the same income year, be deducted or credited, so far as the assessable income or tax extends, -

"(i) In the order elected by the amalgamated company by notice to the Commissioner in such form as the Commissioner may allow; or

"(ii) If no such election is made, on a pro rata basis.

"(13) Where any amalgamating company ceases to exist on an amalgamation, the residual income tax of the amalgamated company in the income year preceding the income year in which the amalgamation takes place shall be deemed, for the purposes of Part XII of this Act (but only with respect to instalments of provisional tax payable after the amalgamation), to be equal to the amount which would have been such residual income tax had the amalgamating company and the amalgamated company always been one company.

"(14) Where any amalgamating company ceases to exist upon a qualifying amalgamation -

"(a) If, immediately before the amalgamation, a credit or debit exists, determined by applying the procedure set out in section 394E(4), 394ZW(4) or 394ZZP(6) of this Act, in the amalgamating company's imputation credit account (as defined in section 394A of this Act), dividend withholding payment account (as so defined), branch equivalent tax account (as so defined) or policyholder credit account (as so defined), the credit or debit shall be treated with effect from the time of the amalgamation as a credit or debit in the equivalent account of the amalgamated company (or, if the amalgamated company does not have an equivalent account and except in the case of a branch equivalent tax account credit or debit, in its imputation credit account) and not as a credit or debit in the relevant account of the amalgamating company but applying section 394E(1)(g), 394ZW(1)(f) and 394ZZP(1)(e) and (3)(d) of this Act as if, with respect to all periods prior to the amalgamation, the amalgamated company did not separately exist and was instead the amalgamating company with the same holders of shares and options over shares as the amalgamating company; and

- "(b) Any credit (not being a credit arising under section 394ZZP(1)(e) of this Act) or debit (not being a debit arising under section 394E(1)(g), 394ZW(1)(f) or 394ZZP(3)(d) of this Act) would have arisen, but for the amalgamation, to be recorded in the imputation credit account, dividend withholding payment account or branch equivalent tax account of the amalgamating company on a date after the amalgamation, the credit or debit shall instead arise to be recorded in the equivalent account of the amalgamated company (or, if the amalgamated company does not have an equivalent account and except in the case of a branch equivalent tax account credit or debit, its imputation credit account); and
- "(c) Sections 394M and 394ZO of this Act shall apply with effect from the time of the amalgamation, with any necessary modifications, in respect of any tax paid by the amalgamating company as if it and the amalgamated company were a single company.

**OO. Deduction for dividends paid on certain preference shares** - (1) Section 194(2) of the principal Act is hereby amended by omitting the words "private company (as defined in section 2 of the Companies Act 1955)" and substituting the words "closely-held company".

(2) Section 194(5) of the principal Act is hereby amended by -

- (a) Omitting the words "nominal value" and substituting the words "subscribed capital amount (as defined in section 4A(3) of this Act)":
- (b) Omitting the words "ordinary paid-up capital" and substituting the words "subscribed capital amount (as so defined) of all the ordinary shares".

**OO. Interest on debentures issued in substitution for shares** - Section 195(2) of the principal Act is hereby amended by -

- (a) Omitting the words "nominal value or to the paid-up value" and substituting the words "subscribed capital amount (as defined in section 4A(3) of this Act)":
- (b) Omitting the words "wound up" and substituting the word "liquidated".

**OO. Distribution of trading stock to shareholders of company** - Section 197(2) of the principal Act is hereby amended by omitting the words "winding up" and substituting the word "liquidation".

**OO. Primary producer co-operative companies** - Section 197G(5) of this Act is hereby amended by -

- (a) Omitting the words "paid-up value" and substituting the words "subscribed capital amount (as defined in section 4A(3) of this Act)":
- (b) Omitting the words "winding up" and substituting the word "liquidation".

**OO. Non-resident may elect to be treated as resident** - Section 204M(3) of the principal Act is hereby amended by omitting the word "allotted" and substituting the word "issued".

**OO. Special partnerships** - Section 211B(10)(b) of the principal Act is hereby amended by omitting the words ", or by any deed" and substituting the words "or the Companies Act 1993 or the laws of any country or territory other than New Zealand or by any deed or agreement".

**OO. Interpretation - petroleum mining** - Section 214D(1) of the principal Act is hereby amended by omitting the words "and with the requirements of the Companies Act 1955" from both places where those words appear.

**OO. Associated persons** - Section 214E(1) of the principal Act is hereby amended by repealing paragraphs (a) and (b) and substituting the following paragraphs -

"(a) Any 2 companies where there is a group of persons -

"(i) The aggregate of whose voting interests in each company is equal to or exceeds 50 percent; or

"(ii) In any case where a market value circumstance exists in respect of either company, the aggregate of whose market value interests in each company is equal to or exceeds 50 percent; or

"(iii) Who have control of both companies by any other means whatsoever; or

"(b) A company and any person (other than a company) where -

"(i) The person has a voting interest in the company equal to or exceeding 50 percent; or

"(ii) In any case where a market value circumstance exists in respect of the company, the person has a market value interest in the company equal to or exceeding 50 percent; or"

**OO. Profit or gain from sale of mining shares by companies** - Section 218 of the principal Act is hereby amended by -

(a) Omitting from subsections (3) and (10) the word "allotted" and substituting in each case the word "issued":

(b) Omitting from subsection (9) the words "winding up" from both places where those words appear and substituting in each case the word "liquidation".



**OO. Interpretation - trusts** - Section 226(1) of the principal Act is hereby amended by -

- (a) Repealing the definition of the term "arrangement":
- (b) Omitting from the definition of the term "disposition of property" the word "allotment" and substituting the word "issue".

**OO. Interpretation - attributed foreign income** - Section 245A(1) of the principal Act is hereby amended by omitting, from the definition of the term "accounting period", the words "winding up" and substituting the word "liquidation".

**OO. Definition of term "associated persons"** - (1) Section 245B(a) of the principal Act is hereby amended by omitting subparagraphs (i) and (ii) and substituting the following subparagraph -

"(i) Any group of persons -

"(A) Has voting interests in each of those companies totalling in aggregate 50 percent or more; or

"(B) In any case where a market value circumstance exists in respect of either company, has market value interests in each of those companies totalling in aggregate 50 percent or more; or

"(C) Has control of each of those companies by any other means whatsoever; or"

(2) Section 245B(h)(ii) of the principal Act is hereby amended by omitting the words "25 percent or more of the paid-up capital of" and substituting the words "a direct voting interest (as defined in section 8B of this Act), or, where a market value circumstance exists in respect of the settlor, a direct market value interest (as so defined), of 25 percent or more in".

(3) Section 245B(i)(ii) of the principal Act is hereby amended by omitting the words "25 percent or more of the paid-up capital of" and substituting the words "a direct voting interest (as defined in section 8B of this Act), or, where a market value circumstance exists in respect of the other person, a direct market value interest (as so defined), of 25 percent or more in".

**OO. Calculation of control interest** - Section 245C(4) of the principal Act is hereby amended by -

(a) Repealing paragraphs (a) and (b) and substituting the following paragraph -

"(a) The percentage of the total shares (measured by reference to their subscribed capital amounts (as defined in section 4A(3) of this Act)) of the foreign company:"

- (b) Omitting from paragraph (e) the words "winding up" and substituting the word "liquidation".

**OO. Calculation of income interest** - Section 245D(2) of the principal Act is hereby amended by -

- (a) Repealing paragraphs (a) and (b) and substituting the following paragraph -

"(a) The percentage of the total shares (measured by reference to their subscribed capital amounts (as defined in section 4A(3) of this Act)) of the foreign company:"

- (b) Omitting from paragraph (e) the words "winding up" and substituting the word "liquidation".

**OO. Variation in control or income interests** - Section 245E(1) of the principal Act is hereby amended by repealing, from the definition of the term "foreign company aggregates", paragraphs (a) and (b) and substituting the following paragraph -

- "(a) The subscribed capital amounts (as defined in section 4A(3) of this Act) of shares in the foreign company:"

**OO. Branch equivalent income calculation** - Section 245J(12) of the principal Act is hereby repealed.

**OO. Liability for tax payable by company left with insufficient assets** - (1) Section 276(1) of the principal Act is hereby amended by omitting the phrase "Companies Act 1955" and substituting the phrase "Companies Act 1993".

- (2) Section 276 of the principal Act is hereby further amended by -

- (a) Omitting the words "wound up" from each place in subsections (8) and (10) where those words appear and substituting in each case the word "liquidated":

- (b) Omitting from subsection (8) the words "winding-up" and substituting the word "liquidation".

**OO. New interpretation provision in relation to non-resident withholding tax** - Section 309(2)(a)(ii) of the principal Act is hereby amended by -

- (a) Omitting the phrase "section 4A(1)(c)" and substituting the phrase "section 4A(1)(ca)":

- (b) Omitting the words "winding-up" in each case where those words appear and substituting in each case the word "liquidation".

**OO. Deduction of resident withholding tax** - Section 327C(1) of the principal Act is hereby amended by -

- (a) Omitting from paragraph (c) the words "taxable bonus issue" and substituting the words "bonus issue in lieu":
- (b) Repealing paragraph (d) and substituting the following paragraph -
  - (d) To the extent to which that payment consists of dividends being a bonus issue in lieu, the amount calculated in accordance with the following formula:

$$(a \times (b + c)) - c$$

where -

- a* is the rate of resident withholding tax, expressed as a percentage, specified in clause 2 of the Nineteenth Schedule to this Act; and
- b* is the amount of the money or money's worth offered as an alternative to the bonus issue (before the deduction of resident withholding tax); and
- c* is -
  - (A) In the case of any dividend paid in relation to shares issued by a company that is at the time of payment not resident in New Zealand, the amount of foreign withholding tax paid or payable in respect of that amount of dividend paid; or
  - (B) In the case of any other dividend, the aggregate of the amounts of any imputation credit attached to the dividend and any dividend withholding payment credit attached to the dividend:

**OO. Records to be kept** - Section 327P(6)(b)(iii) of the principal Act is hereby amended by omitting the words "wound-up and dissolved" and substituting the word "liquidated".

**OO. Interpretation - fringe benefit tax** - Section 336N(1) of the principal Act is hereby amended by omitting, from the definition of the term "shareholder-employee" -

- (a) The words "private company (as defined in section 2 of the Companies Act 1955)" and substituting the words "closely-held company":
- (b) The word "private".

**OO. Payment of fringe benefit tax on income year basis in respect of shareholder-employees -** Section 336TB(1) of the principal Act is hereby amended by omitting the words "private company as defined in section 2 of the Companies Act 1955" and substituting the words "closely-held company".

**OO. Tax deductions to be credited against tax assessed -** Section 362(2) of the principal Act is hereby amended by omitting the words "private company within the meaning of the Companies Act 1955" and substituting the words "closely-held company".

**OO. Recovery of tax deductions from employers -** Section 365(2) of the principal Act is hereby amended by repealing paragraph (b) and substituting the following paragraphs -

"(b) Where the employer is a company, upon the liquidation of the company, the amount of the tax deduction shall have the ranking provided for in the Seventh Schedule to the Companies Act 1993 (whether or not the company has been incorporated or registered under that Act); and

"(c) Where the employer is a company, upon the appointment of a receiver on behalf of the holder of any debenture given by the company secured by a charge over any property of the company or upon possession being taken on behalf of the debenture holder of the property, the amount of the tax deduction shall have the ranking provided for in the Seventh Schedule to the Companies Act 1993 (whether or not the company has been incorporated or registered under that Act), as if the receiver were a liquidator.

**OO. Unpaid tax deductions etc. to constitute charge on employer's property -** Section 367(1) of the principal Act is hereby amended by inserting, after the words "Companies Act 1955" the words "or the Companies (Registration of Charges) Act 1993".

**OO. Determination of assessable income -** Section 374B(1)(g) of the principal Act is hereby amended by omitting the words "private company (as defined in section 2 of the Companies Act 1955)" and substituting the words "closely-held company".

**OO. Guaranteed minimum family income credit of tax -** Section 374E(1) of the principal Act is hereby amended by omitting from paragraph (c) of the definition of the term "employment" the words "private company (as defined in section 2 of the Companies Act 1955)" and substituting the words "closely-held company".

**OO. Qualifying company regime -** Section 393 of the principal Act is hereby amended by omitting the words "closely held".

**OO. Period of grace for new election** - Section 393F(3) of the principal Act is hereby amended by omitting the word ", allotment,".

**OO. Revocation of loss attribution elections, and new elections** - Section 393O(2) of the principal Act is hereby amended by omitting the words "or allotment".

**OO. Taxation on election to become qualifying company** - Section 393K(2) of the principal Act is hereby amended by -

- (a) Omitting the words "wound up" and substituting the word "liquidated":
- (b) Repealing paragraph (iv) of the definition of item *a* and substituting the following paragraph -

"(iv) Paragraph (i) of the definition of item *i* of the definition of the term "transitional capital amount" in section 4A(3) of this Act were repealed; and"

**OO. Dividends from qualifying company** - Section 393M(1)(a) of the principal Act is hereby amended by repealing paragraph (ii) and substituting the following paragraph -

"(ii) The amount of the dividend which would not be a dividend if paragraph (i) of the definition of item *i* of the definition of the term "transitional capital amount" in section 4A(3) of this Act were repealed; and".

**OO. Loss attributing qualifying companies** - Section 393N of the principal Act is hereby amended by repealing paragraphs (b)(ii)(B), (C) and (D) and substituting the following sub-sub-paragraph -

"(B) Distributions of assets of the company on any acquisition, redemption or other cancellation by the company of its shares or other reduction in or return of share capital of the company, whether on its liquidation or otherwise, -"

**OO. Interpretation - full imputation** - Section 394A(1) of the principal Act is hereby amended by, omitting, from the definition of the term "paid", the word "allotment" and substituting the word "issue".

**OO. Debits arising to imputation credit account** - (1) Section 394E(1) of the principal Act is hereby amended by inserting, after paragraph (aa), the following paragraph -

"(ab) In the case of any on-market acquisition (as defined in section 4A(2) of this Act) by the company of a share in the company, the amount (not being less than nil) calculated in accordance with the following formula -

$$(a - b) \times \frac{c}{1 - c}$$

where -

- a* is the amount of the dividend arising from the on-market acquisition (calculated as if section 4A(1)(c) of this Act did not apply); and
- b* is the amount calculated with respect to the share and the on-market acquisition under the formula in section 4A(1)(c)(iv) of this Act applied as if the time of notice of, or proposing, the cancellation were the time of the acquisition; and
- c* is the rate of resident withholding tax, expressed as a percentage, stated in clause 2 of the Nineteenth Schedule to this Act and applying at the time the acquisition occurs:"

(2) Section 394E(2) of the principal Act is hereby amended by inserting, after paragraph (aa), the following paragraph -

"(ab) In the case of a debit referred to in paragraph (ab) of that subsection, on the date the acquisition occurs:"

**OO. Limits on refunds of tax** - Section 394M(4) of the principal Act is hereby amended by omitting the words "wound up" and substituting the word "liquidated".

**OO. Debits arising to dividend withholding payment account** - Section 394ZW(1)(c) is hereby amended by omitting the words "pursuant to section 394ZO of this Act".

**OO. Further dividend withholding payment payable etc** - Section 394ZZF(5) of the principal Act is hereby amended by omitting the words "wound up" and substituting the word "liquidated".

**OO. Deduction of tax from payment due to defaulters** - Section 400(1) of the principal Act is hereby amended by repealing paragraphs (a) and (b) of the definition of the term "bank".

**OO. Keeping of business records** - Section 428(4) of the principal Act is hereby amended by omitting the words "wound up and finally dissolved" and substituting the word "liquidated".

**OO. Keeping of returns where return information transmitted electronically** - Section 428A(2) of the principal Act is hereby amended by omitting the words "wound up and finally dissolved" and substituting the word "liquidated".

## **Goods and Services Tax Act 1985**

**OO. Interpretation** - Section 2(1) of the Goods and Services Tax Act 1985 is hereby amended by

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- (a) Omitting from the definition of the term "associated person" the words "or more" from both places where those words appear; and
- (b) Omitting, from the definition of the term "non-profit body" the words "memorandum, articles of association" and substituting the word "constitution".

**OO. Recovery of tax** - Section 42(2) of the Goods and Services Tax Act 1985 is hereby amended by repealing paragraph (b) and substituting the following paragraphs -

- "(b) Where the person is a company, upon the liquidation of the company, the amount of the tax payable shall have the ranking provided for in the Seventh Schedule to the Companies Act 1993 (whether or not the company has been incorporated or registered under that Act):
- "(ba) Where the person is a company, upon the appointment of a receiver on behalf of the holder of any debenture given by the company secured by a charge over any property of the company or upon possession being taken on behalf of the debenture holder of the property, the amount of the tax payable shall have the ranking provided for in the Seventh Schedule to the Companies Act 1993 (whether or not the company has been incorporated or registered under that Act), as if the receiver or person taking possession were a liquidator:

**OO. Deduction of tax from payments due to defaulters** - Section 43(1) of the Goods and Services Tax Act 1985 is hereby amended by repealing paragraphs (a) and (b) of the definition of the term "bank".

**OO. Group of companies** - Section 55(8) of the Goods and Services Tax Act 1985 is hereby amended by omitting the words "registered under the Companies Act 1955".

**OO. Keeping of records** - Section 75(4) of the Goods and Services Tax Act 1985 is hereby amended by omitting the words "wound up and finally dissolved" and substituting the word "liquidated".

**Inland Revenue Department Act 1974**

**OO. Evidence in proceedings before an authority** - Section 35 of the Inland Revenue Department Act 1974 is hereby amended by -

- (a) Omitting from subsection (2) the words "public company" and substituting the words "widely-held company":
- (b) Repealing from subsection (4) the definition of the term "public company" and substituting the following definition -

**"Widely-held company"** has the meaning assigned to that term by section 8B of the Income Tax Act 1976.



**Estate and Gift Duties Act 1968**

**OO. Interpretation** - Section 2(2) of the Estate and Gift Duties Act 1968 is hereby amended by omitting, from the definition of the term "disposition of property", the word "allotment" and substituting the word "issue".

**OO. Dutiable estate** - Section 6(2)(i) of the Estate and Gift Duties Act 1968 is hereby amended by adding the words "or the Companies Act 1993".

**OO. Valuation of shares** - Section 22 of the Estate and Gift Duties Act 1968 is hereby amended by -

- (a) Omitting the words "including a private company,";
- (b) Omitting the words "memorandum or articles of association" and substituting the word "constitution".

**OO. Exemption for certain payments by employers** - Section 75(1)(b) and (c) are hereby amended by omitting the words "nominal value of allotted shares" and substituting in each case "issued shares (measured by reference to their subscribed capital amounts (as defined in section 4A(3) of the Income Tax Act 1976))".

**Stamp and Cheque Duties Act 1971**

**OO. Interpretation** - Section 2 of the Stamp and Cheque Duties Act 1971 is hereby amended by -

- (a) Omitting from the definition of the term "instrument of nomination of shares" the words "or allotment" and "or allot" in each place where those words appear:
- (b) Omitting from the definition of the term "shares in a flat or office owning company" the word "articles" and substituting the word "constitution".

**OO. Conveyance duty** - Section 15(3) of the Stamp and Cheque Duties Act 1971 is hereby amended by inserting, after the words "Companies Act 1955", the words "or Companies Act 1993".

**OO. Valuing shares** - Section 44 of the Stamp and Cheque Duties Act 1971 is hereby amended by omitting the words "memorandum or articles of association" and substituting the word "constitution".

**OO. Valuation of consideration** - Section 47(1)(b) of the Stamp and Cheque Duties Act 1971 is hereby amended by omitting the words "or allotment".

**OO. Offence to issue certain shares** - Section 90 of the Stamp and Cheque Duties Act 1971 is hereby amended by omitting the words "or allot".



