EH – Financial arrangements rules

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Introductory provisions

EH 1 What this subpart applies to

Financial arrangements rules

(1) This subpart applies to the financial arrangements rules.

'Financial arrangements rules' defined

(2) **Financial arrangements rules** means—

- (a) the sections in this subpart; and
- (b) section FF 2 (Financial arrangements), section GD 11 (Accrual rules), and section NG 16A (Variation in non-resident withholding tax deductions to correct errors); and

(c) sections 90AA to 90AD of the Tax Administration Act 1994.

Purposes

(3) The purposes of the financial arrangements rules are—

(a) to require the parties to a financial arrangement to accrue over the term of the arrangement a reasonable amount of income derived or expenditure incurred from the arrangement, and so to prevent the deferral of income or the advancement of expenditure; and

(b) to require the parties to a financial arrangement, when accruing income or expenditure, to take into account all consideration, without regard to whether it is capital or revenue; and

(c) to require a party to a financial arrangement to calculate a base price adjustment when the rights and obligations of the party under the arrangement cease.

Origin:	(1) new. (2) OB 1 'accrual rules'. (3) EH 20.
Defined terms:	amount, consideration, derived, financial arrangement, financial arrangements rules, income.

EH 2 Application of financial arrangements rules

Calculation and allocation under financial arrangements rules

(1) A person to whom the financial arrangements rules apply (see sections EH 4 to EH 9) must calculate and allocate under the financial arrangements rules their income or expenditure for an income year from a financial arrangement to which the financial arrangements rules apply (see sections EH 10 to EH 17).

Relationship with other provisions

(2) Subsection (1) applies unless another provision specifies that income or expenditure from the financial arrangement must be calculated or allocated differently.

Origin:	(1) EH 26(1). (2) EH 26(1).
Defined terms:	financial arrangement, financial arrangements rules, income, income year, person.

EH 3 Other matters

The matters to which this subpart relates are—

(a) the persons to whom the financial arrangements rules apply (sections EH 4 to EH 9):

(b) the financial arrangements to which the financial arrangements rules apply, including a description of what a financial arrangement is and the date from which the rules apply (sections EH 10 to EH 17):

(c) the calculation and allocation of income and expenditure over a financial arrangement's term (sections EH 18 to EH 33):

(d) the calculation and allocation of income and expenditure when a person's rights and obligations under a financial arrangement cease (sections EH 34 to EH 37):

(e) consideration when a financial arrangement involves property or services (sections EH 38 to EH 41):

(f) consideration treated as paid to a person (sections EH 42 to EH 48):

(g) consideration treated as paid by a person (sections EH 49 to EH 53):

(h) consideration when a legal defeasance has occurred (section EH 54):

(i) consideration when an anti-avoidance provision applies (section EH 55):

(j) income and deductions related specifically to financial arrangements (sections EH 56 to EH 58):

(k) the adjustment required when a particular kind of financial arrangement defeats the intention of the financial arrangements rules (section EH 59):

(l) the application of the financial arrangements rules to cash basis persons, including a description of who is a cash basis person (sections EH 60 to EH 69).

Origin:	new.
Defined terms:	cash basis person, consideration, deduction, financial arrangement, financial arrangements rules, income, legal defeasance, person.

Persons to whom financial arrangements rules apply

EH 4 New Zealand resident

Description

(1) The financial arrangements rules apply to a party to a financial arrangement who is a New Zealand resident on the date on which the person becomes a party.

Date

(2) The rules apply on and from the date on which the person becomes a party.

Duration

(3) The rules apply while the person is both a party and a New Zealand resident.

Origin:	(1) EH 21(1). (2) EH 21(1). (3) EH 21(1).
Defined terms:	financial arrangement, financial arrangements rules, New Zealand resident, person.

EH 5 Non-resident party becoming resident

Description

(1) The financial arrangements rules apply to a party to a financial arrangement who is not a New Zealand resident on the date on which the person becomes a party but who later, while still a party, becomes a New Zealand resident.

Date

(2) The rules apply on and from the date on which the person becomes a New Zealand resident, unless the rules apply on and from an earlier date through the operation of section EH 6.

Duration

(3) The rules apply while the person is both a party and a New Zealand resident.

Origin:	(1) EH 50(1A). (2) EH 50(1A). (3) EH 50(1A).
Defined terms:	financial arrangement, financial arrangements rules, New Zealand resident, non-resident, person.

EH 6 Non-resident party carrying on business

Description

(1) The financial arrangements rules apply to a party to a financial arrangement who is not a New Zealand resident on the date on which the person becomes a party, but whose becoming a party on that date is for the purpose of a business they carry on through a fixed establishment in New Zealand. The rules apply to the extent to which the arrangement relates to the business.

Date

(2) The rules apply on and from the date on which the person becomes a party to the arrangement for that purpose.

Duration

(3) The rules apply while the person is a party to the arrangement for that purpose.

Origin:	(1) EH 21(3), (4)(a). (2) EH 50(2)(a). (3) EH 21(3), (4)(a).
Defined terms:	business, financial arrangement, financial arrangements rules, fixed establishment, New Zealand, New Zealand resident, non-resident, person.

EH 7 Trustee not resident

The financial arrangements rules apply to a party to a financial arrangement who is a trustee and not a New Zealand resident, but the rules apply only if and while—

(a) the settlor of the trust is resident in New Zealand; and

(b) neither section HH 4 (3) nor HH 4 (6) (Trustee income) applies to the trustee.

Origin:	EH 21(3), (4)(b), (5).
Defined terms:	financial arrangement, financial arrangements rules, New Zealand resident, resident in New Zealand, trustee.

EH 8 Trustee of deceased's estate

Description

(1) The financial arrangements rules apply to a party to a financial arrangement who is a trustee of a deceased's estate that contains the arrangement.

Date

(2) The rules apply on and from the date of the deceased's death.

Duration

(3) The rules apply while the trustee is both a party and a New Zealand resident.

Origin:	(1) new. (2) new. (3) new.
Defined terms:	financial arrangement, financial arrangements rules, New Zealand resident, trustee.

EH 9 Party changing from private or domestic purpose

Description

(1) The financial arrangements rules apply to a party to a financial arrangement who is a person described in section EH 14 (1).

Date

(2) The rules apply on and from the date on which the person becomes a party to the arrangement, as described in section EH 14 (2).

Duration

(3) The rules apply while the person is both a party and a New Zealand resident.

Origin:	(1) new. (2) new. (3) new.
Defined terms:	financial arrangement, financial arrangements rules, New Zealand resident, person.

Financial arrangements to which financial arrangements rules apply: meaning of financial arrangement

EH 10 What is a financial arrangement

Meaning

(1) **Financial arrangement** means an arrangement described in any of subsections (2) to (4).

Money received for money provided

(2) A financial arrangement is an arrangement under which a person receives money in consideration for that person, or another person, providing money to any person—

(a) at a future time; or

(b) on the occurrence or non-occurrence of a future event, whether or not the event occurs because notice is given or not given.

Examples of money received for money provided

(3) Without limiting subsection (2), each of the following is a financial arrangement:

(a) a debt, including a debt that arises by law:

(b) a debt instrument:

(c) the deferral of the payment of some or all of the consideration for an absolute assignment of some or all of a person's rights under another financial arrangement or under an excepted financial arrangement:

(d) the deferral of the payment of some or all of the consideration for a legal defeasance releasing a person from some or all of their obligations under another financial arrangement or under an excepted financial arrangement.

Excepted financial arrangement ceasing to be excepted

(4) In relation to section EH 14 and section EH 15,—

(a) an excepted financial arrangement that ceases to be an excepted financial arrangement through the operation of section EH 14 is a financial arrangement:

(b) an excepted financial arrangement that ceases to be an excepted financial arrangement for a party through the operation of section EH 15 is a financial arrangement for the party.

Origin:	(1) EH 22. (2) EH 22(1)(b). (3) EH 22(1)(a). (4) EH 24(2).
Defined terms:	consideration, excepted financial arrangement, financial arrangement, legal defeasance, money, person.

EH 11 What is not a financial arrangement

Absolute assignment

(1) An absolute assignment of some or all of a person's rights under another financial arrangement or under an excepted financial arrangement is not a financial arrangement, except to the extent described in section EH 10 (3)(c).

Legal defeasance

(2) A legal defeasance releasing a person from some or all of their obligations under another financial arrangement or under an excepted financial arrangement is not a financial arrangement, except to the extent described in section EH 10 (3)(d).

Excepted financial arrangement

(3) An excepted financial arrangement is not a financial arrangement.

Origin:	(1) EH 22(2), (3). (2) EH 22(2), (3). (3) EH 22(4).
Defined terms:	excepted financial arrangement, financial arrangement, legal defeasance, person.

EH 12 What is an excepted financial arrangement

Meaning

(1) **Excepted financial arrangement** means an arrangement described in any of subsections (2) to (23). However,—

(a) an arrangement described in any of subsections (16) to (18) may cease to be an excepted financial arrangement through the operation of section EH 14:

(b) an arrangement described in any of subsections (19) to (23) may cease to be an excepted financial arrangement for a party who makes an election under section EH 15.

Annuity

(2) Each of the following is an excepted financial arrangement:

(a) an annuity for a term contingent on human life:

(b) an annuity for a term not contingent on human life to which section EG 2 (2)(c) ('Life insurance' defined) applies.

Bet

(3) A bet on any of the following is an excepted financial arrangement:

(a) a race (as defined in section 2 of the Racing Act 1971):

(b) a sporting event under a sports betting system established under Part VB of the Racing Act 1971:

(c) a game of chance, lottery, or prize competition (as those terms are defined in section 2 of the Gaming and Lotteries Act 1977):

(d) a New Zealand lottery or New Zealand prize competition (as those terms are defined in section 71 of the Gaming and Lotteries Act 1977).

Employment contract

(4) An employment contract is an excepted financial arrangement.

Farm-out arrangement

(5) A farm-out arrangement is an excepted financial arrangement.

Group investment fund

(6) An interest in a group investment fund is an excepted financial arrangement.

Hire purchase: livestock or bloodstock

(7) A hire purchase agreement for livestock or bloodstock is an excepted financial arrangement.

Insurance contract

(8) An insurance contract is an excepted financial arrangement.

Lease not finance lease

(9) A lease that is not a finance lease is an excepted financial arrangement.

Loan in New Zealand currency

(10) A loan to which all the following apply is an excepted financial arrangement for the lender:

(a) the loan is in New Zealand currency; and

(b) the loan is interest-free; and

(c) the loan is repayable on demand.

Partnership or joint venture

(11) An interest in a partnership or a joint venture is an excepted financial arrangement.

Share or option

(12) A share, or an option to acquire or to dispose of shares, is an excepted financial arrangement, if the share is acquired, or the person becomes a party to the option, on or after 20 May 1999. This subsection does not apply to a withdrawable share or to an option to acquire or to dispose of withdrawable shares.

Specified preference share

(13) A specified preference share to which section FZ 1 (Deduction for dividends paid on certain preference shares) applies is an excepted financial arrangement.

Superannuation

(14) A membership of a superannuation scheme is an excepted financial arrangement.

Warranty

(15) A warranty for goods or services is an excepted financial arrangement.

Loan in foreign currency: private or domestic purpose

(16) A loan to which all the following apply is an excepted financial arrangement for the borrower:

(a) the loan is in foreign currency; and

(b) the borrower is a cash basis person; and

(c) the borrower uses the loan for a private or a domestic purpose.

Option: private or domestic purpose

(17) An option to acquire or dispose of property, other than an interest in a financial arrangement, is an excepted financial arrangement for a person who becomes a party to the option for a private or a domestic purpose.

Private or domestic agreement for the sale and purchase of property or services

(18) A private or a domestic agreement for the sale and purchase of property or services is an excepted financial arrangement.

Agreement for the sale and purchase of property or services

(19) An agreement for the sale and purchase of property or services is an excepted financial arrangement, except for a party who makes an election under section EH 15, if—

(a) all a party's sales or purchases under the agreement are prepaid; and

(b) for all the party's agreements under which all sales and purchases are prepaid, the total value of prepayments, on every day in an income year, is $50,000 or less.

Short-term agreement for the sale and purchase of property or services

(20) A short-term agreement for the sale and purchase of property or services is an excepted financial arrangement, except for a party who makes an election under section EH 15.

Short-term option

(21) A short-term option is an excepted financial arrangement, except for a party who makes an election under section EH 15.

Travellers' cheques

(22) Travellers' cheques are excepted financial arrangements, except for a party who makes an election under section EH 15.

Variable principal debt instrument

(23) A variable principal debt instrument is an excepted financial arrangement, except for a party who makes an election under section EH 15, if the total value on every day in an income year of all variable principal debt instruments to which a person is a party is $50,000 or less.

Origin:	(1) EH 24. (2) EH 24(1). (3) EH 24(1). (4) EH 24(1). (5) EH 24(1). (6) EH 24(1). (7) EH 24(1). (8) EH 24(1). (9) EH 24(1). (10) EH 24(1). (11) EH 24(1). (12) EH 24(1). (13) EH 24(1). (14) EH 24(1). (15) EH 24(1). (16) EH 24(1). (17) EH 24(1).

	(18) EH 24(1). (19) EH 24(1). (20) EH 24(1). (21) EH 24(1). (22) EH 24(1). (23) EH 24(1).
Defined terms:	agreement for the sale and purchase of property or services, arrangement, bloodstock, cash basis person, excepted financial arrangement, farm-out arrangement, finance lease, financial arrangement, group investment fund, hire purchase agreement, income year, insurance contract, lease, New Zealand, person, private or domestic agreement for the sale and purchase of property or services, property, share, short-term agreement for the sale and purchase of property or services, short-term option, specified preference share, superannuation scheme, variable principal debt instrument, withdrawable share.

EH 13 Relationship between financial arrangements and excepted financial arrangements

Excepted financial arrangement may be included

(1) An excepted financial arrangement may be included in a financial arrangement.

Income or expenditure from specific excepted financial arrangements

(2) If an excepted financial arrangement described in any of section EH 12 (2) to (15) is included in a financial arrangement, gain or loss solely attributable to the excepted financial arrangement is not income or expenditure under the financial arrangements rules.

Income or expenditure from remaining excepted financial arrangements

(3) If an excepted financial arrangement described in any of section EH 12 (16) to (23) is included in a financial arrangement, gain or loss solely attributable to the excepted financial arrangement is income or expenditure under the financial arrangements rules.

'Gain or loss' defined

(4) In this section, **gain or loss** includes income or expenditure from a financial arrangement.

Origin:	(1) EH 22(4). (2) EH 23(1). (3) EH 23(2). (4) new.
Defined terms:	excepted financial arrangement, financial arrangement, financial arrangements rules, gain or loss, income.

EH 14 Change from private or domestic purpose

When this section applies

(1) This section applies when a person who is a party to an excepted financial arrangement described in any of section EH 12 (16) to (18) stops using it for a private or a domestic purpose.

Excepted financial arrangement becomes financial arrangement

(2) On and after the date on which the person stops using the excepted financial arrangement for a private or a domestic purpose,—

(a) it ceases to be an excepted financial arrangement; and

(b) the person becomes a party to a financial arrangement.

Origin:	(1) EH 24(3).
	(2) EH 24(3)(a), (b).
Defined terms:	excepted financial arrangement, financial arrangement, person.

EH 15 Election to treat certain excepted financial arrangements as financial arrangements

Election

(1) A person may choose to treat as financial arrangements all the excepted financial arrangements to which the person is a party that are described in section EH 12 (19) or (20) or (21) or (22) or (23).

Election for class of short-term agreements

(2) A person may choose to treat a class of short-term agreements for the sale and purchase of property or services as financial arrangements. The person must identify the class by—

(a) the currency that applies to the agreements; or

(b) the term of the agreements; or

(c) both the currency and the term.

How to choose

(3) The person makes an election by returning income derived or expenditure incurred from the chosen arrangements under the financial arrangements rules in their return of income.

How to revoke

(4) The person revokes the election by giving notice to the Commissioner with their return of income and within the time that the return must be filed under section 37 of the Tax Administration Act 1994.

Effect of revocation

(5) The revocation applies to financial arrangements the person enters into after the income year in which the notice is given.

Origin:	(1) EH 25(1). (2) EH 25(2), (3). (3) EH 25(4). (4) EH 25(6). (5) EH 25(5).
Defined terms:	Commissioner, derived, excepted financial arrangement, financial arrangement, financial arrangements rules, income, income year, notice, person, return of income.

Financial arrangements to which financial arrangements rules apply: date on and after which rules apply

EH 16 Financial arrangements to which financial arrangements rules apply

Entered into on or after 20 May 1999

(1) The financial arrangements rules apply to a financial arrangement that all its parties enter into on or after 20 May 1999.

Existing immediately before 20 May 1999

(2) The financial arrangements rules apply to a financial arrangement existing immediately before 20 May 1999 to the extent to which a person becomes a party to the arrangement on or after 20 May 1999.

Rollover, extension, or advance on or after 20 May 1999

(3) The financial arrangements rules apply to a financial arrangement that is rolled over or extended, or under which an advance is made, on or after 20 May 1999, in accordance with a binding contract entered into before 20 May 1999.

Binding contract before 20 May 1999

(4) However, the financial arrangements rules do not apply to a financial arrangement to which both the following apply:

(a) all its parties enter into it on or after 20 May 1999; and

(b) they enter into it in accordance with a binding contract entered into before 20 May 1999.

Transferred under matrimonial agreement

(5) The financial arrangements rules apply to a financial arrangement to which all the following apply, to the extent to which the transferee becomes a party to it:

(a) the transferor is a party to it before 20 May 1999; and

(b) it is rolled over or extended, or an advance is made under it, on or after 20 May 1999, in accordance with a binding contract entered into before 20 May 1999; and

(c) it is transferred under a matrimonial agreement on or after 20 May 1999.

Binding contract before 20 May 1999 and transfer under matrimonial agreement

(6) However, the financial arrangements rules do not apply to a financial arrangement to which all the following apply:

(a) all its parties enter into it on or after 20 May 1999; and

(b) they enter into it in accordance with a binding contract entered into before 20 May 1999; and

(c) it is transferred under a matrimonial agreement on or after 20 May 1999.

Origin:	(1) EH 19(1). (2) EH 19(1). (3) EH 19(2)(a). (4) EH 19(3)(a). (5) EH 19(2)(b). (6) EH 19(3)(b).
Defined terms:	financial arrangement, financial arrangements rules, matrimonial agreement, person.

Matters to which financial arrangements rules do not apply

EH 17 Financial arrangements rules do not apply

The financial arrangements rules do not apply to—

(a) the calculation of non-resident withholding income:

(b) interest paid by the Commissioner under Part VII of the Tax Administration Act 1994 for an overpayment of income tax:

(c) interest payable to the Commissioner under Part VII of the Tax Administration Act 1994 for an underpayment of income tax.

Origin:	EH 21(2).
Defined terms:	Commissioner, financial arrangements rules, income tax, interest, non-resident withholding income, pay.

Calculation and allocation of income and expenditure over financial arrangement's term

EH 18 When use of spreading method required

A party to a financial arrangement must use one of the spreading methods to calculate an amount of income or expenditure from the arrangement for each income year over the arrangement's term, and to allocate it to the income year, unless section EH 19 applies.

Origin:	EH 33(1).
Defined terms:	amount, financial arrangement, income, income year, spreading method.

EH 19 When use of spreading method not required

Base price adjustment year

(1) A person does not use any of the spreading methods for a financial arrangement in the income year in which section EH 35 requires them to calculate a base price adjustment for it.

Trustee of personal injury compensation trust

(2) A trustee to whom both the following apply does not use any of the spreading methods:

(a) the trustee is a cash basis person or would be a cash basis person if the trustee were a natural person; and

(b) the trustee holds a financial arrangement in trust to manage compensation paid for personal injury under the Accident Insurance Act 1998, any of the former Acts (as defined in section 13 of the Accident Insurance Act 1998), the Workers Compensation Act 1956, or a court order.

Cash basis person

(3) A cash basis person is not required to use any of the spreading methods, but may choose to do so under section EH 67.

Origin:	(1) EH 33(1). (2) EH 33(4)(b). (3) EH 33(4)(a).
Defined terms:	cash basis person, financial arrangement, income year, person, spreading method, trustee.

EH 20 What spreading methods do

Description

(1) The spreading methods are methods of calculating and allocating income and expenditure from a financial arrangement over the arrangement's term.

Methods

(2) The spreading methods are—

- (a) the yield to maturity method or an alternative, to which sections EH 22, EH 25, and EH 29 are relevant:
- (b) the straight-line method, to which sections EH 23 and EH 25 are relevant:
- (c) a market valuation method, to which sections EH 24, EH 25, and EH 29 are relevant:
- (d) a determination method or an alternative, to which sections EH 26 and EH 29 are relevant:
- (e) a substitute method, to which sections EH 27 and EH 29 are relevant:
- (f) a default method, to which section EH 28 is relevant.

Result

(3) The amount calculated for and allocated to the income year under a spreading method is—

- (a) income, under section CC 3 (Financial arrangements), derived by the person in the income year; or
- (b) expenditure incurred by the person in the income year.

Origin:	(1) EH 33. (2) EH 33. (3) EH 33(3).
Defined terms:	amount, derived, financial arrangement, income, income year, person, spreading method.

EH 21 What is included when spreading methods used

Consideration and amounts

(1) A person using a spreading method must include—

- (a) all consideration that has been paid, and all consideration that is or will be payable, to the person for or under the financial arrangement, ignoring non-contingent fees; and
- (b) all consideration that has been paid, and all consideration that is or will be payable, by the person for or under the financial arrangement, ignoring non-contingent fees; and

(c) all amounts that have been remitted, and all amounts that are to be remitted, by the person under the financial arrangement; and

(d) all amounts that would have been payable to the person under the financial arrangement if the amounts had not been remitted by law.

Consideration in particular cases

(2) If any of sections EH 38 to EH 54 applies, the consideration referred to in subsection (1)(a) and (b) is adjusted in accordance with the relevant section.

Origin:	(1) EH 33(2). (2) EH 48(1).
Defined terms:	amount, consideration, financial arrangement, non-contingent fees, person, spreading method.

EH 22 Yield to maturity method or alternative

Who may use yield to maturity method

(1) A person who is a party to a financial arrangement may use the yield to maturity method.

Who may use alternative

(2) A person who is a party to a financial arrangement may use an alternative to the yield to maturity method, but may do so only if the alternative—

(a) has regard to the principles of accrual accounting; and

(b) conforms with commercially acceptable practice; and

(c) results in the allocation to each income year of amounts that are not materially different from those that would have been allocated using the yield to maturity method; and

(d) is also used by the person for financial reporting purposes for financial arrangements of the same or a similar class (although section EH 29 may apply if the alternative is not used in this way).

Origin:	(1) EH 34(1). (2) EH 34(2), (3).
Defined terms:	amount, financial arrangement, income year, person.

EH 23 Straight-line method

Who may use straight-line method

(1) A person who is a party to a financial arrangement may use the straight-line method if—

(a) the total value of all the financial arrangements to which the person is a party in an income year has been $1,500,000 or less on every day in the income year; and

(b) the person complies with section EH 31 (1).

Calculation of total value of financial arrangements

(2) When calculating total value, the person must—

(a) include every one of their financial arrangements, whether the financial arrangements rules or the old financial arrangements rules apply to it; and

(b) use the following values:

(i) for a fixed principal financial arrangement, its face value:

(ii) for a variable principal debt instrument, the amount owing by or to the person under the financial arrangement on the relevant day:

(iii) for a financial arrangement to which the old financial arrangements rules apply, the value determined under those rules.

Increase in amount

(3) The Governor-General may, by Order in Council, increase the amount specified in subsection (1).

Origin:	(1) EH 35(1). (2) EH 35(5), (6). (3) EH 58.
Defined terms:	amount, financial arrangement, financial arrangements rules, fixed principal financial arrangement, income year, old financial arrangements rules, person, variable principal debt instrument.

EH 24 Market valuation method

A person who is a party to a financial arrangement may use, for the arrangement, a market valuation method if—

(a) either—

(i) the person's business includes dealing in financial arrangements of the class to which the arrangement belongs; or

(ii) the financial arrangement is an exchange traded option, a forward contract for foreign exchange, or a futures contract; and

(b) the parties to the financial arrangement are not associated persons; and

(c) either—

(i) the Commissioner has approved the market, the method, and the source of information used to determine market values by a determination under section 90AC (1)(c) of the Tax Administration Act 1994; or

(ii) the person can demonstrate market prices that are reliable; and

(d) the method conforms with commercially acceptable practice; and

(e) the person complies with section EH 31 (4); and

(f) the method is also used by the person for financial reporting purposes for financial arrangements of the same or a similar class (although section EH 29 may apply if the method is not used in this way).

Origin:	EH 36(1), (2), (3).
Defined terms:	associated person, business, Commissioner, financial arrangement, forward contract, futures contract, person.

EH 25 Choice among first 3 spreading methods

A person who may use the yield to maturity method or an alternative, the straight-line method, or a market valuation method for a financial arrangement may choose to use whichever of those methods the person can use for the arrangement.

Origin:	EH 34(1); EH 35(1), (2); EH 36(3).
Defined terms:	financial arrangement, person, spreading method.

EH 26 Determination method or alternative

Who may use determination method

(1) A person who is a party to a financial arrangement may use a determination method, that is, a method in a determination made by the Commissioner under section 90AC (1)(d) of the Tax Administration Act 1994 and applying to the arrangement, if—

(a) the person cannot use the yield to maturity method or an alternative; and

(b) the person either—

(i) may not use the straight-line method or a market valuation method; or

(ii) may use the straight-line method or a market valuation method but chooses not to do so.

Who may use alternative

(2) A person who is a party to a financial arrangement may use an alternative to a determination method, but may do so only if—

(a) the person cannot use the yield to maturity method or an alternative; and

(b) the person either—

(i) may not use the straight-line method or a market valuation method; or

(ii) may use the straight-line method or a market valuation method but chooses not to do so; and

(c) the alternative has regard to the principles of accrual accounting; and

(d) the alternative conforms with commercially acceptable practice; and

(e) the alternative results in the allocation to each income year of amounts that are not materially different from those that would have been allocated using a determination method; and

(f) the alternative is also used by the person for financial reporting purposes for financial arrangements of the same or a similar class (although section EH 29 may apply if the alternative is not used in this way).

Origin:	(1) EH 37; EH 38(1). (2) EH 37; EH 38(2), (3).
Defined terms:	amount, Commissioner, financial arrangement, income year, person.

EH 27 Substitute method

A person who is a party to a financial arrangement may use a substitute method if—

(a) the person cannot use the yield to maturity method or an alternative; and

(b) the person either—

(i) may not use the straight-line method or a market valuation method; or

(ii) may use the straight-line method or a market valuation method but chooses not to do so; and

(c) the Commissioner has not made a determination for the financial arrangement under section 90AC (1)(d) of the Tax Administration Act 1994; and

(d) the method conforms with commercially acceptable practice; and

(e) the method is also used by the person for financial reporting purposes for financial arrangements of the same or a similar class (although section EH 29 may apply if the method is not used in this way); and

(f) the method allocates a reasonable amount to each income year over the financial arrangement's term.

Origin:	EH 37; EH 39.
Defined terms:	amount, Commissioner, financial arrangement, income year, person.

EH 28 Default method

A person who is a party to a financial arrangement may use a default method if—

(a) the person cannot use the yield to maturity method or an alternative; and

(b) the person either—

   (i) may not use the straight-line method or a market valuation method; or

   (ii) may use the straight-line method or a market valuation method but chooses not to do so; and

(c) the person may not use a determination method or an alternative, or a substitute method; and

(d) the person either—

   (i) does not prepare financial accounts; or

   (ii) does not report the income derived or expenditure incurred from a financial arrangement for financial reporting purposes; and

(e) the method conforms with commercially acceptable practice; and

(f) the method allocates a reasonable amount to each income year over the financial arrangement's term.

Origin:	EH 40.
Defined terms:	amount, derived, financial arrangement, income, income year, person.

EH 29 Failure to use method for financial reporting purposes

When this section applies

(1) This section applies when a person would be allowed to use a method but for the fact that the person does not comply with whichever is relevant of sections EH 22 (2)(d), EH 24 (f), EH 26 (2)(f), or EH 27 (e).

Person treated as complying

(2) The person is treated as complying with whichever is relevant of sections EH 22 (2)(d), EH 24 (f), EH 26 (2)(f), or EH 27 (e) if the method that the person uses for each financial arrangement—

(a) is used for the financial arrangement, and each financial arrangement of the same or a similar class, for every income year over its term for the purposes of the financial arrangements rules; and

(b) appropriately reflects the dominant purpose for which the person entered into the financial arrangement; and

(c) is not used for the purpose of tax avoidance; and

(d) has been approved for use in circumstances applying to the person by the Commissioner, either by giving notice to the person or by making a determination under section 90AC (1)(f) of the Tax Administration Act 1994.

Qualification on subsection (2)(a)

(3) A method complies with subsection (2)(a), even if it is a change from a previous method, as long as the Commissioner approves the change in method under the circumstances or conditions specified in a determination under section 90AC (1)(g) of the Tax Administration Act 1994.

Origin:	(1) EH 42(1). (2) EH 42(1), (2). (3) EH 42(3).
Defined terms:	Commissioner, financial arrangement, financial arrangements rules, income year, notice, person, tax avoidance.

EH 30 Consistency of use of spreading method

Consistency required

(1) A person must use the same spreading method for financial arrangements of the same or a similar class for every income year. This subsection is overridden by subsection (3).

Straight-line method and market valuation method

(2) Section EH 31 sets out particular consistency requirements for the straight-line method and a market valuation method.

Change of spreading method

(3) Section EH 32 sets out the circumstances in which a person may change their spreading method.

Origin:	(1) EH 41.
	(2) EH 41.
	(3) EH 41.
Defined terms:	financial arrangement, income year, person, spreading method.

EH 31 Consistency of use of straight-line method and market valuation method

Straight-line method for all financial arrangements

(1) A person using the straight-line method in an income year for a financial arrangement must use it for all financial arrangements—

(a) to which the person is a party at the end of the income year; and

(b) for which the person can use it.

Straight-line method for every year of term

(2) A person who starts to use the straight-line method for a financial arrangement must use it over the arrangement's remaining term until section EH 35 requires them to calculate a base price adjustment for the arrangement, unless section EH 32 (1) applies.

Total value may be over $1,500,000

(3) Subsection (2) applies even if the total value of all the financial arrangements to which the person is a party is over $1,500,000 at any time in the arrangement's remaining term.

Market valuation method

(4) A person who starts to use a market valuation method for a financial arrangement must use it over the arrangement's remaining term until section EH 35 requires them to calculate a base price adjustment for the arrangement, unless section EH 32 (1) applies.

Increase in amount

(5) The Governor-General may, in an Order in Council made under section EH 23 (3), increase the amount specified in subsection (3).

Origin:	(1) EH 35(3).
	(2) EH 35(3).
	(3) EH 35(4).
	(4) EH 36(4).
	(5) EH 58.
Defined terms:	amount, financial arrangement, income year, person.

EH 32 Change of spreading method

Change of straight-line or market valuation method

(1) A person may change from the straight-line method or the market valuation method with the Commissioner's written authorisation.

Change of other method

(2) A person may change from any other spreading method if they have a sound commercial reason for doing so. The advancement, deferral, or reduction of an income tax liability is not a sound commercial reason.

Spreading method adjustment

(3) When a person changes their spreading method under subsection (2),—

(a) they must use the formula in section EH 33 to calculate a spreading method adjustment for the income year in which they change the method; and

(b) their only income or expenditure from the financial arrangement for the income year to which the formula is applied is the spreading method adjustment.

Positive or negative spreading method adjustment

(4) A spreading method adjustment calculated under section EH 33 is,—

(a) if positive, income, under section CC 3 (Financial arrangements), derived by the person in the income year for which the calculation is made:

(b) if negative, expenditure incurred by the person in the income year for which the calculation is made.

Origin:	(1) EH 35(3)(b); EH 36 (4). (2) EH 43(1). (3) EH 43(2); EH 44(4). (4) EH 44(3).
Defined terms:	Commissioner, derived, financial arrangement, income, income tax liability, income year, person, spreading method.

EH 33 Spreading method adjustment formula

Calculation of spreading method adjustment

(1) A person calculates a spreading method adjustment using the formula in subsection (3).

What formula applies to

(2) The person must apply the formula to each financial arrangement to which they—

(a) are a party at the end of the income year in which they change their spreading method; and

(b) were a party at the end of the previous income year.

Formula

(3) The formula is—

income (new method) – expenditure (new method) – income (old method) + expenditure (old method).

Definition of items in formula

(4) The items in the formula are defined in subsections (5) to (8).

Income (new method)

(5) **Income (new method)** is the amount that would have been income derived by the person from the financial arrangement if the new method had been used for the arrangement in the period starting on the date on which the person became a party to the arrangement and ending on the last day of the income year for which the calculation is made.

Expenditure (new method)

(6) **Expenditure (new method)** is the amount that would have been expenditure incurred by the person from the financial arrangement if the new method had been used for the arrangement in the period starting on the date on which the person became a party to the arrangement and ending on the last day of the income year for which the calculation is made.

Income (old method)

(7) **Income (old method)** is income, under section CC 3 (Financial arrangements), derived by the person from the financial arrangement in previous income years.

Expenditure (old method)

(8) **Expenditure (old method)** is expenditure incurred by the person from the financial arrangement in previous income years.

Origin:	(1) EH 44(1). (2) EH 44(1). (3) EH 44(2), (3). (4) EH 44(2), (3). (5) EH 44(2), (3). (6) EH 44(2), (3). (7) EH 44(2), (3). (8) EH 44(2), (3).
Defined terms:	amount, derived, financial arrangement, income, income year, person, spreading method.

Calculation and allocation of income and expenditure when rights and obligations under financial arrangement cease

EH 34 How base price adjustment calculated

A party to a financial arrangement who must calculate a base price adjustment (see sections EH 35 and EH 36) calculates it using the formula in section EH 37.

Origin:	new.
Defined terms:	financial arrangement.

EH 35 When calculation of base price adjustment required

Ceasing to be New Zealand resident

(1) A party to a financial arrangement who ceases to be a New Zealand resident must calculate a base price adjustment as at the date of the party's ceasing to be a New Zealand resident. This subsection is overridden by section EH 36 (1) and (2).

Ceasing to be party for purpose of New Zealand business

(2) A person who is not a New Zealand resident and who is a party to a financial arrangement for the purpose of a business the party carries on through a fixed establishment in New Zealand must calculate a base price adjustment as at the date of the party's ceasing to be a party to the arrangement for that purpose.

Maturity

(3) A party to a financial arrangement must calculate a base price adjustment as at the date on which the arrangement matures.

Treated as maturity

(4) A financial arrangement that has not matured because an amount has not been paid is treated as if it had matured if—

(a) the amount not paid is immaterial; and

(b) the arrangement has been structured to avoid the application of section EH 37.

Disposal

(5) A party to a financial arrangement who disposes of the arrangement must calculate a base price adjustment as at the date of the disposal.

Absolute assignment

(6) A party to a financial arrangement who makes an absolute assignment of all the party's rights under the arrangement must calculate a base price adjustment as at the date of the absolute assignment.

Defeasance

(7) A party to a financial arrangement who makes a legal defeasance of all the party's obligations under the arrangement must calculate a base price adjustment as at the date of the legal defeasance.

Sale at discount to associated person

(8) A party to a financial arrangement that is a debt must calculate a base price adjustment as at the date on which the creditor sells the debt to a person associated with the debtor and at a discount in the circumstances described in section EH 51 (1) to (4).

Discharge without consideration

(9) A party to a financial arrangement must calculate a base price adjustment as at the date on which a party to the arrangement is discharged from making all remaining payments under the arrangement without fully adequate consideration.

Operation of law

(10) A party to a financial arrangement must calculate a base price adjustment as at the date on which a party to the arrangement is released from making all remaining payments under the arrangement under the Insolvency Act 1967 or the Companies Act 1993 or the laws of a country or territory other than New Zealand.

Composition with creditors

(11) A party to a financial arrangement must calculate a base price adjustment as at the date on which a party to the arrangement is released from making all remaining payments under the arrangement by a deed or agreement of composition with the party's creditors.

Lapse of time

(12) A party to a financial arrangement must calculate a base price adjustment as at the date on which all remaining payments under the arrangement become irrecoverable or unenforceable through the lapse of time.

Trust of deceased's estate

(13) A party to a financial arrangement who is a trustee of a deceased's estate that contains the arrangement must calculate a base price adjustment as at—

(a) the date of the deceased's death, as if the deceased had disposed of the arrangement on that date; and

(b) the date on which the trustee distributes the arrangement to a specific legatee or a residuary beneficiary, as if the trustee had acquired the arrangement on the date of the deceased's death and disposed of it on the date of the distribution.

Origin:	(1) EH 45(1). (2) EH 45(1). (3) EH 45(1). (4) EH 45(2). (5) EH 45(1). (6) EH 45(3). (7) EH 45(4). (8) EH 45(1). (9) EH 45(1). (10) EH 45(1). (11) EH 45(1). (12) EH 45(1). (13) EH 45(5).
Defined terms:	amount, associated person, business, consideration, financial arrangement, fixed establishment, legal defeasance, maturity, New Zealand, New Zealand resident, person, trustee.

EH 36 When calculation of base price adjustment not required

Cash basis person who ceases to be temporary New Zealand resident

(1) A cash basis person who ceases to be a New Zealand resident before the first day of the fourth income year following the income year in which they first became a New Zealand resident does not calculate a base price adjustment for a financial arrangement to which they—

(a) were a party before first becoming a New Zealand resident; and

(b) are a party on the date on which they cease to be a New Zealand resident.

Other party who ceases to be New Zealand resident

(2) A party to a financial arrangement who ceases to be a New Zealand resident does not calculate a base price adjustment to the extent to which the arrangement relates to a business the party carries on through a fixed establishment in New Zealand.

Creditor when legal defeasance occurs

(3) A party who has a right to receive money under a financial arrangement the obligations of which are the subject of a legal defeasance does not calculate a base price adjustment on the date of the defeasance if the defeasance requires another person to meet the remaining obligations of the arrangement.

Origin:	(1) EH 46(1). (2) EH 46(2). (3) EH 46(3).
Defined terms:	business, cash basis person, financial arrangement, fixed establishment, income year, legal defeasance, money, New Zealand, New Zealand resident, person.

EH 37 Base price adjustment formula

Calculation of base price adjustment

(1) A person calculates a base price adjustment using the formula in subsection (5).

When formula applies

(2) The person calculates the base price adjustment for the income year in which section EH 35 applies to them.

Positive base price adjustment

(3) A base price adjustment, if positive, is income, under section CC 3 (Financial arrangements), derived by the person in the income year for which the calculation is made. However, it is not income to the extent to which it arises from expenditure incurred by the person from the financial arrangement in previous income years and for which a deduction was not allowed in those income years.

Negative base price adjustment

(4) A base price adjustment, if negative, is expenditure incurred by the person in the income year for which the calculation is made. The person is allowed a deduction for the expenditure to the extent to which it arises from income, under section CC 3 (Financial arrangements), derived by the person from the financial arrangement in previous income years.

Formula

(5) The formula is—

$$\text{consideration} - \text{income} + \text{expenditure} + \text{amount remitted.}$$

Definition of items in formula

(6) The items in the formula are defined in subsections (7) to (11).

Consideration

(7) **Consideration** is all consideration that has been paid, and all consideration that is or will be payable, to the person for or under the financial arrangement, ignoring non-contingent fees, minus all consideration that has been paid, and all consideration that is or will be payable, by the person for or under the financial arrangement, ignoring non-contingent fees.

Consideration in particular cases

(8) If any of sections EH 38 to EH 54 applies, the consideration referred to in subsection (7) is adjusted in accordance with the relevant section.

Income

(9) **Income** is—

(a) income, under section CC 3 (Financial arrangements), derived by the person from the financial arrangement in previous income years; and

(b) dividends derived by the person from the remission of the financial arrangement; and

(c) income derived under section CF 2 (2) and (3) (Remission of specified suspensory loans).

Expenditure

(10) **Expenditure** is expenditure incurred by the person from the financial arrangement in previous income years.

Amount remitted

(11) **Amount remitted** is an amount that is not included in the consideration paid or payable to the person because it has been remitted—

(a) by the person; or

(b) by law.

Origin:	(1) EH 47(1). (2) EH 47(1). (3) EH 47(2), (3). (4) EH 47(2), (4). (5) EH 47(1). (6) EH 47(1). (7) EH 47; EH 48(1). (8) new. (9) EH 47(1). (10) EH 47(1). (11) EH 47(1).
Defined terms:	amount, consideration, deduction, derived, dividend, financial arrangement, income, income year, non-contingent fee, person.

Consideration when financial arrangement involves property or services

EH 38 Consideration for agreement for sale and purchase of property or services, hire purchase agreement, specified option, or finance lease

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to or by the original parties to certain financial arrangements. The arrangements are an agreement for the sale and purchase of property or services, a hire purchase agreement, a specified option, or a finance lease, if the agreement, option, or lease has proceeded and is for a consideration that includes property or services.

Value of property or services

(2) The value of the property or services is determined by applying subsections (3) to (6) in numerical order until a subsection applies.

Lowest price

(3) The value of the property or services is the lowest price the parties would have agreed on, on the date the agreement, option, or lease was entered into, if payment had been required in full at the time the first right in the property was transferred or the services provided. Two qualifications on this subsection are as follows:

(a) the subsection does not apply to an agreement for the sale and purchase of property or services or a specified option included in another financial arrangement:

(b) section EH 40 applies if the consideration is in a foreign currency.

Cash price

(4) The value of the property or services is the cash price of the property or services to which the agreement, option, or lease relates, as determined by section 2 (1) of the Credit Contracts Act 1981, if that Act applies to the agreement, option, or lease.

Future or discounted value

(5) The value of the property or services is the future value, or the discounted value, or a combination of both the future and discounted values, of the amounts paid or payable on the date on which the first right in the property is transferred or the services are provided, as determined by the Commissioner under a determination under section 90AC (1)(i) of the Tax Administration Act 1994.

Determined by Commissioner

(6) The value of the property or services is the amount determined by the Commissioner when either party to the arrangement applies to the Commissioner for a specific determination. Both parties must use this amount.

Origin:	(1) EH 48(2). (2) EH 48(2). (3) EH 48(2), (3), (4). (4) EH 48(2), (3). (5) EH 48(2), (3). (6) EH 48(2), (3).
Defined terms:	agreement for the sale and purchase of property or services, amount, Commissioner, consideration, finance lease, financial arrangement, hire purchase agreement, property, specified option.

EH 39 Consideration for hire purchase agreement or finance lease

When this section applies

(1) This section applies when it is necessary to determine what is included in the consideration paid to or by a party to a hire purchase agreement or a finance lease.

Consideration

(2) The consideration for a hire purchase agreement or a finance lease includes expenditure or loss incurred by the lessor in preparing and installing the hire purchase asset or lease asset for use to the extent to which it is not taken into account under section EH 38.

Origin:	(1) new. (2) EH 48(5).
Defined terms:	consideration, finance lease, hire purchase agreement, hire purchase asset, lease asset, lessor.

EH 40 Consideration in foreign currency

When this section applies

(1) This section applies when the consideration payable under a financial arrangement to which section EH 38 (3) applies is in a foreign currency.

Lowest price

(2) The lowest price referred to in section EH 38 (3) is the lowest price the parties would have agreed on in the foreign currency, converted into New Zealand dollars using the rate that the original party applying section EH 38 (3) selects from the rates in subsection (3). The party may select the rate in subsection (3)(b) only if the period between the date on which the first right in the property is to be transferred and the date on which final payment is to be made is 5 years or less.

Rates

(3) The rates are—

(a) the rate, on the date on which the parties enter into the financial arrangement, available to the party from a New Zealand registered bank for the exchange of New Zealand dollars for the foreign currency for one of the following dates:

(i) the date on which the first right in the property is to be transferred; or

(ii) if that date is uncertain on the date on which the parties enter into the financial arrangement, the date on which the parties reasonably expect, when entering into the arrangement, that the first right in the property will be transferred; or

(b) the rate, on the date on which the parties enter into the financial arrangement, available to the party from a New Zealand registered bank for the exchange of New Zealand dollars for the foreign currency for one of the following dates:
   (i) the date on which final payment is to be made; or
   (ii) if that date is uncertain on the date on which the parties enter into the financial arrangement, the date on which the parties reasonably expect, when entering into the arrangement, that final payment will be made; or

(c) an exchange rate approved by the Commissioner for this subsection in the circumstances applicable to the party in a determination under section 90AC (1)(k) of the Tax Administration Act 1994.

Rate must be applied consistently

(4) The party must apply the selected rate to the financial arrangement for every income year over its term.

Origin:	(1) OB 7(2). (2) OB 7(2). (3) OB 7(1), (2), (4). (4) OB 7(3).
Defined terms:	Commissioner, consideration, financial arrangement, income year, New Zealand, property.

EH 41 Value relevant for non-financial arrangements rule

When this section applies

(1) This section applies when it is necessary to determine what the value is when property acquired or disposed of under a financial arrangement, or the consideration for it, is relevant in determining a person's income or deductions under any provision of this Act that is not a financial arrangements rule.

Value

(2) The person is treated as having acquired or disposed of the property for a value determined by applying section EH 38 (2).

Origin:	(1) EH 26(2). (2) EH 26(3).
Defined terms:	consideration, deduction, financial arrangement, financial arrangements rules, income, person, property.

Consideration treated as paid to a person

EH 42 Consideration when resident party ceases to be resident

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to a party to a financial arrangement who is treated as having disposed of the arrangement because the party, who was a New Zealand resident, ceases to be a New Zealand resident.

Consideration

(2) The party is treated as having been paid the market value the financial arrangement has on the date on which the party ceases to be a New Zealand resident.

Origin:	(1) new.
	(2) EH 50(1).
Defined terms:	consideration, financial arrangement, New Zealand resident.

EH 43 Consideration when non-resident ceases to be party

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to a party to a financial arrangement who is treated as having disposed of the arrangement because the party, who was not a New Zealand resident but was a party to the arrangement for the purpose of a business the party carried on through a fixed establishment in New Zealand, ceases to be a party to the arrangement for that purpose.

Consideration

(2) The party is treated as having been paid the market value the financial arrangement has on the date on which the party ceases to be a party for that purpose.

Origin:	(1) new.
	(2) EH 50(2)(b), (3).
Defined terms:	business, consideration, financial arrangement, fixed establishment, New Zealand, New Zealand resident, non-resident.

EH 44 Consideration when party dies

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to a party to a financial arrangement who is treated as having disposed of the arrangement because the party dies.

Consideration

(2) The party is treated as having been paid the market value the financial arrangement has on the date of the party's death.

Origin:	(1) new.
	(2) new.
Defined terms:	consideration, financial arrangement.

EH 45 Consideration when financial arrangement distributed

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to a party to a financial arrangement who is a trustee of a deceased's estate that contains the arrangement and who is treated as having disposed of the arrangement because the trustee distributes it to a specific legatee or a residuary beneficiary.

Consideration

(2) The party is treated as having been paid the market value the financial arrangement has on the date of the distribution.

Origin:	(1) new.
	(2) new.
Defined terms:	consideration, financial arrangement, trustee.

EH 46 Consideration affected by unfavourable factors

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to a party to a financial arrangement who disposes of the arrangement for a consideration affected by any of the following factors:

(a) the occurrence of an event reducing or cancelling the other party's obligations under the arrangement; or

(b) the occurrence of one of the following between the date on which the arrangement was entered into and the date of the disposal:

(i) a decline in the other party's creditworthiness; or

(ii) an increase in the possibility that the other party will not meet an obligation under the arrangement.

This subsection is overridden by subsection (2).

When this section does not apply

(2) This section does not apply when—

(a) the party's business includes dealing in financial arrangements of the class disposed of; and

(b) the parties to the arrangement disposed of are not associated persons.

Consideration

(3) The party is treated as having been paid the market value the financial arrangement has on the date of the disposal, as if the consideration had not been affected by a factor described in subsection (1).

Origin:	(1) EH 49(3).
	(2) EH 49(5).
	(3) EH 49(4).
Defined terms:	associated person, business, consideration, financial arrangement.

EH 47 Consideration when disposal for no, or inadequate, consideration

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to a party to a financial arrangement when the following circumstances exist:

(a) the party disposes of the arrangement; and

(b) the disposal—

(i) is not for monetary consideration; or

(ii) is for a consideration that is less than the market value the arrangement has on the date of the disposal.

Disposal and acquisition at market value

(2) The party is treated as having been paid the market value the financial arrangement has on the date of the disposal.

No market value

(3) If the financial arrangement has no market value, the party is treated as having been paid the amount that might reasonably be expected to be paid on a disposal at arm's length.

Origin:	(1) EH 49(1).
	(2) EH 49(1).
	(3) EH 49(2).
Defined terms:	amount, consideration, financial arrangement.

EH 48 Consideration when financial arrangement distributed in kind

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to a party to a financial arrangement who distributes it in kind.

Consideration

(2) The party is treated as having been paid the market value the financial arrangement has on the date of the distribution.

Origin:	(1) new.
	(2) EH 48(8).
Defined terms:	consideration, financial arrangement.

Consideration treated as paid by a person

EH 49 Consideration when any of sections EH 5, EH 6, EH 8, and EH 9 applies

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid by a person who is treated as having acquired a financial arrangement because the person is a party to whom the financial arrangements rules apply under any of sections EH 5, EH 6, EH 8, and EH 9.

Consideration

(2) The person is treated as having paid the market value the financial arrangement has on the date on which the financial arrangements rules start to apply to them.

Origin:	(1) new.
	(2) EH 24(3)(c); EH 50(1A), (2), (3).
Defined terms:	consideration, financial arrangement, financial arrangements rules, person.

EH 50 Consideration when disposal for no, or inadequate, consideration

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid by a person when the following circumstances exist:

(a) the person acquires a financial arrangement; and

(b) the acquisition—

(i) is not for monetary consideration; or

(ii) is for a consideration that is less than the market value of the arrangement on the date of the acquisition.

Acquisition at market value

(2) The person is treated as having paid the market value the financial arrangement has on the date of the acquisition.

No market value

(3) If the financial arrangement has no market value, the person is treated as having paid the amount that might reasonably be expected to be paid on a disposal at arm's length.

Origin:	(1) EH 49(1).
	(2) EH 49(1).
	(3) EH 49(2).
Defined terms:	amount, consideration, financial arrangement, person.

EH 51 Consideration when debt sold at discount to associate of debtor

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid by a debtor when the creditor sells the debt on or after 20 May 1999 to a person associated with the debtor and at a discount.

Person associated

(2) A person is associated with the debtor if the relationship between the person and the debtor is described in section OD 8 (3) (Further definitions of associated persons).

At a discount

(3) A creditor sells a debt at a discount if the creditor sells it for 80% or less of the market value of the debt.

Market value

(4) The market value of a debt affected by any of the following factors is determined as if its market value were not affected by the factor. The factors are—

- (a) the occurrence of an event reducing or cancelling the debtor's obligations under the debt; or
- (b) the occurrence of one of the following between the date on which the debt was entered into and the date of the disposal:
  - (i) a decline in the debtor's creditworthiness; or
  - (ii) an increase in the possibility that the debtor will not meet an obligation under the debt.

Consideration

(5) The debtor is treated as having paid the creditor the amount that the person associated with the debtor pays the creditor.

Origin:	(1) EH 53(1).
	(2) EH 53(5).
	(3) EH 53(2).

	(4) EH 53(3), (4).
	(5) EH 48(6); EH 53.
Defined terms:	amount, associated person, consideration.

EH 52 Consideration when debtor released from obligation

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid by a person when the following circumstances exist:

(a) the person is released from the obligation to pay an amount owing under a financial arrangement; and

(b) the release occurs under section 114 of the Insolvency Act 1967 or any of the Inland Revenue Acts or a loan described in subsection (2).

Social assistance suspensory loan

(2) A loan referred to in subsection (1)(b) is a loan that—

(a) is made by a department or instrument of the executive government of New Zealand; and

(b) provides for the person's liability to pay to be wholly or partly remitted if they meet conditions intended to promote a social policy objective of the government of New Zealand; and

(c) is of a class declared by the Governor-General by Order in Council to be a social assistance suspensory loan.

Declaration as social assistance suspensory loan

(3) The Governor-General may, by Order in Council, declare a class of loan that meets the criteria in subsection (2) to be a social assistance suspensory loan.

Consideration

(4) The person is treated as having paid the amount on the date on which they are released from the obligation to pay it.

Origin:	(1) EH 51.
	(2) EH 51; EH 59.
	(3) EH 51; EH 59.
	(4) EH 51.
Defined terms:	amount, consideration, financial arrangement, Inland Revenue Acts, New Zealand, person.

EH 53 Consideration when debt forgiven for natural love and affection

When this section applies: first case

(1) This section applies when it is necessary to determine the consideration that is paid by a person when the following circumstances exist:

(a) the person is a debtor; and

(b) the creditor is a natural person; and

(c) the creditor forgives the debtor's debt because of the natural love and affection the creditor has for the debtor.

When this section applies: second case

(2) This section also applies when it is necessary to determine the consideration that is paid by a trust when the following circumstances exist:

(a) the trust is a debtor; and

(b) the trust was established mainly to benefit one or both of the following:

(i) a natural person for whom the creditor has natural love and affection:

(ii) an organisation or a trust whose income is exempt under section CW 30 (Charities: non-business income) or section CW 31 (Charities: business income); and

(c) the creditor is a natural person; and

(d) the creditor forgives the debtor's debt.

How subsections (1) and (2) apply

(3) For the purposes of subsections (1) and (2),—

(a) the debtor's debt includes an amount accrued and unpaid at the time of the forgiveness; and

(b) the means by which the debt is forgiven, whether in a will or otherwise, is immaterial.

Consideration

(4) The debtor is treated as having paid the debt on the date on which the creditor forgives it.

Origin:	(1) EH 52(1).
	(2) EH 52(1).
	(3) EH 52(1).
	(4) EH 52(1).
Defined terms:	amount, consideration, income, person, trust.

Consideration when legal defeasance has occurred

EH 54 Legal defeasance

When this section applies

(1) This section applies when it is necessary to determine what is included in the consideration when the following circumstances exist:

- (a) the obligations of a financial arrangement were the subject of a legal defeasance that required another person to meet the remaining obligations of the arrangement; and
- (b) the person who has a right to receive money under the arrangement is now required by section EH 35 to calculate a base price adjustment for it.

Consideration

(2) The consideration received by the person who has a right to receive money under the arrangement is the total of—

- (a) the amounts received from the original debtor; and
- (b) the amounts received from the person required to meet the remaining obligations.

Origin:	(1) new. (2) EH 48(7).
Defined terms:	amount, consideration, financial arrangement, legal defeasance, money, person.

Consideration when anti-avoidance provision applies

EH 55 Anti-avoidance provisions

When this section applies

(1) This section applies when it is necessary to determine the consideration that is paid to or by a person in a case to which any of the following provisions applies:

- (a) section GD 11 (Accrual rules); or
- (b) section GD 13 (3) (Cross-border arrangements between associated persons); or
- (c) section GD 13 (4) (Cross-border arrangements between associated persons).

Consideration

(2) The consideration is the amount determined under the relevant provision.

Origin:	(1) new. (2) EH 48(1).
Defined terms:	amount, consideration, person.

Income and deduction provisions specifically related to financial arrangements

EH 56 Income when debt forgiven to trustee

When this section applies

(1) This section applies when—

(a) a trust is a debtor; and

(b) the trust was established mainly to benefit one or both of the following:

(i) a natural person for whom the creditor has natural love and affection:

(ii) an organisation or a trust whose income is exempt under section CW 30 (Charities: non-business income) or section CW 31 (Charities: business income); and

(c) the creditor is a natural person; and

(d) the creditor forgives the debtor's debt; and

(e) a trustee of the trust makes a distribution to a beneficiary; and

(f) the beneficiary is neither—

(i) a natural person for whom the creditor has natural love and affection; nor

(ii) an organisation or a trust whose income is exempt under section CW 30 (Charities: non-business income) or section CW 31 (Charities: business income); and

(g) the distribution is made on or after 20 May 1999.

How subsection (1) applies

(2) For the purposes of subsection (1),—

(a) the debtor's debt includes an amount accrued and unpaid at the time of the forgiveness; and

(b) the means by which the debt is forgiven, whether in a will or otherwise, is immaterial.

Distribution is income of trustee

(3) The distribution is income of the trustee, under section CC 3 (2) (Financial arrangements), to the extent to which it is less than or equal to the total amount of the debts of the trust forgiven to it by creditors.

Distribution subtracted from total amount forgiven

(4) The distribution is subtracted from the total amount of the debts of the trust forgiven to it by creditors as the total amount stands at the time of the distribution. The total amount reduces, every time a distribution that is income of the trustee is made, by the amount of the distribution.

Allocation

(5) The income is derived by the trustee in the income year in which the distribution is made.

Origin:	(1) EH 52(1), (2). (2) EH 52(1). (3) EH 52(3)(b). (4) EH 52(4). (5) EH 52(3)(a).
Defined terms:	amount, derived, distribution, income, income year, person, trustee.

EH 57 Income and deduction when debt sold at discount to associate of debtor

When this section applies

(1) This section applies when a creditor sells a debt on or after 20 May 1999 to a person associated with the debtor and at a discount.

Person associated

(2) A person is associated with the debtor if the relationship between the person and the debtor is described in section OD 8 (3) (Further definitions of associated persons).

At a discount

(3) A creditor sells a debt at a discount if the creditor sells it for 80% or less of the market value of the debt.

Market value

(4) The market value of a debt affected by any of the following factors is determined as if its market value were not affected by the factor. The factors are—

(a) the occurrence of an event reducing or cancelling the debtor's obligations under the debt; or

(b) the occurrence of one of the following between the date on which the debt was entered into and the date of the disposal:

(i) a decline in the debtor's creditworthiness; or

(ii) an increase in the possibility that the debtor will not meet an obligation under the debt.

Original debt replaced with interest-free loan

(5) The associated person is treated as having provided the debtor with an interest-free loan for the amount paid for the debt.

Repayment: income and deduction

(6) If the debtor later repays the person associated with the debtor more than the amount the associated person paid for the debt, the excess amount paid by the debtor is—

(a) income, under section CC 3 (3) (Financial arrangements), of the person associated with the debtor; and

(b) a deduction that the debtor is allowed under section DB 7 (1) (Repayment of debt sold at discount to associate of debtor).

Origin:	(1) EH 53(1). (2) EH 53(5). (3) EH 53(2). (4) EH 53(3), (4). (5) EH 53(6). (6) EH 53(7).
Defined terms:	amount, associated person, deduction, income, person.

EH 58 Deduction for security payment

When subsection (2) applies: loss generally

(1) Subsection (2) applies when a person is allowed a deduction under section DB 9 (2) (Security payment).

Amount of deduction

(2) The person is allowed a deduction no greater than the amount of the security payment.

When subsection (4) applies: share loss

(3) Subsection (4) applies when a person is allowed a deduction under section DB 9 (4) (Security payment).

Amount of deduction

(4) The person is allowed a deduction no greater than the amount of the security payment.

Origin:	(1) EH 55(1). (2) EH 55(1). (3) EH 55(2). (4) EH 55(2).
Defined terms:	amount, deduction, person, security payment.

One kind of avoidance

EH 59 Adjustment required

When this section applies

(1) This section applies when—

(a) the terms of a financial arrangement give either party, both parties, or an associated person the discretion to decide on an amount payable under the arrangement; and

(b) it is not generally accepted commercial practice to make financial arrangements containing such terms; and

(c) a change in the amount brought about by the exercise of the discretion does not reflect changes in commodity, economic, financial, or industrial indices, or in banking or general commercial rates; and

(d) the effect of the financial arrangement is to defeat the intention of the financial arrangements rules.

Parties to calculate adjustment

(2) Each person who is a party to the financial arrangement must calculate an adjustment for the income years specified in subsection (3) by following the steps in subsections (4) to (6).

Income years

(3) The adjustment must be calculated for the following income years:

(a) until the person ceases to be a party, the fifth income year after the income year in which the parties entered into the financial arrangement and every fifth income year after that; and

(b) the income year in which the person ceases to be a party.

First step

(4) The first step the person takes is to calculate income or expenditure from the financial arrangement for each income year using the yield to maturity method in the manner prescribed by the Commissioner in a determination under section 90AC (1)(a) of the Tax Administration Act 1994.

Consideration and amounts to be included at first step

(5) The person must include the following amounts in the calculation:

(a) for every income year for which the calculation is made, as described in subsection (3), the consideration and amounts described in section EH 21 for the period starting on the date on which the person became a party to the financial arrangement and ending on the last day of the income year for which the calculation is made; and

(b) for every fifth income year, as described in subsection (3)(a),—

(i) an amount equal to the financial arrangement's market value on the last day of the income year, as if the person had disposed of the arrangement for that amount; or

(ii) if the financial arrangement has no market value, the amount that might reasonably be expected to be paid on a disposal at arm's length.

Second step

(6) The second step the person takes is to calculate the income tax liability for each income year using the income or expenditure calculated under subsections (4) and (5) in substitution for the income or expenditure previously calculated for the financial arrangement for each income year.

Origin:	(1) EH 57(1). (2) EH 57(1). (3) EH 57(2). (4) EH 57(3). (5) EH 57(3), (4). (6) EH 57(3).
Defined terms:	amount, associated person, Commissioner, consideration, financial arrangement, financial arrangements rules, income, income tax liability, income year, person, prescribed.

Application of financial arrangements rules to cash basis persons

EH 60 Description of cash basis person

Who is cash basis person

(1) A cash basis person is—

(a) a natural person who meets the criteria in section EH 62:

(b) a trustee of a deceased's estate, whether or not a natural person, in the circumstances described in section EH 66.

Natural persons excluded by Commissioner

(2) A natural person may be excluded under section EH 65 from being a cash basis person for a class of financial arrangements.

Origins:	(1) EH 27; EH 29. (2) EH 27(8).
Defined terms:	cash basis person, Commissioner, financial arrangement, person, trustee.

EH 61 Effect of being cash basis person

Use of spreading method

(1) A cash basis person is not required to apply any of the spreading methods to any of their financial arrangements, but may choose to do so under section EH 67.

Calculation of base price adjustment

(2) A cash basis person is not excused from the requirement to calculate a base price adjustment when any of section EH 35 (1) to (13) applies to them just because they do not use any of the spreading methods for the financial arrangement.

Origin:	(1) EH 33(4)(a). (2) EH 45(1).
Defined terms:	cash basis person, financial arrangement, spreading method.

EH 62 Natural person

Criteria for natural person as cash basis person

(1) A natural person is a cash basis person for an income year if—

(a) one of the following applies in the person's case for the income year:

(i) section EH 63 (1); or

(ii) section EH 63 (2); and

(b) section EH 63 (3) applies in the person's case for the income year.

Financial arrangements, income, and expenditure relevant to application of criteria

(2) The calculations required by section EH 63 (1) to (3) are done for the financial arrangements, or the income and expenditure, described in section EH 64.

Increase in amounts

(3) The Governor-General may, by Order in Council, increase an amount specified in any of section EH 63 (1) to (3).

Origin:	(1) new. (2) new. (3) EH 58.
Defined terms:	amount, cash basis person, financial arrangement, income, income year, person.

EH 63 Thresholds

Income and expenditure threshold

(1) For the purposes of section EH 62 (1)(a)(i), this subsection applies if the absolute value of the person's income and expenditure in the income year for all financial arrangements to which the person is a party is $100,000 or less.

Absolute value threshold

(2) For the purposes of section EH 62 (1)(a)(ii), this subsection applies if, on every day in the income year, the absolute value of all financial arrangements to which the person is a party added together is $1,000,000 or less. The value of each arrangement is,—

(a) for a fixed principal financial arrangement, its face value:

(b) for a variable principal debt instrument, the amount owing by or to the person under the financial arrangement:

(c) for a financial arrangement to which the old financial arrangements rules apply, the value determined under those rules.

Deferral threshold

(3) For the purposes of section EH 62 (1)(b), this subsection applies if the result of applying the formula in subsection (4) to each financial arrangement to which the person is a party at the end of the income year and adding the outcomes together is $40,000 or less.

Formula

(4) The formula is—

$$(\text{accrual income} - \text{cash basis income}) + (\text{cash basis expenditure} - \text{accrual expenditure}).$$

Definition of items in formula

(5) The items in the formula are defined in subsections (6) to (9).

Accrual income

(6) **Accrual income** is the amount that would have been income derived by the person from the financial arrangement if the person had been required to use a spreading method in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made. It is calculated using one of the following methods:

(a) the yield to maturity method, whether or not the person may use it, or has chosen to use it, for their financial arrangement; or

(b) the straight-line method, whether or not the person may use it, or has chosen to use it, for their financial arrangement; or

(c) an alternative method approved by the Commissioner.

Cash basis income

(7) **Cash basis income** is the amount that would have been income derived by the person from the financial arrangement if the person had been a cash basis person in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made.

Cash basis expenditure

(8) **Cash basis expenditure** is the amount that would have been expenditure incurred by the person from the financial arrangement if the person had been a cash basis person in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made.

Accrual expenditure

(9) **Accrual expenditure** is the amount that would have been expenditure incurred from the financial arrangement if the person had been required to use a spreading method in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made. It is calculated using one of the following methods:

(a) the yield to maturity method, whether or not the person may use it, or has chosen to use it, for their financial arrangement; or

(b) the straight-line method, whether or not the person may use it, or has chosen to use it, for their financial arrangement; or

(c) an alternative method approved by the Commissioner.

Origin:	(1) EH 27(1)(a). (2) EH 27(1)(b), (7). (3) EH 27(2), (3). (4) EH 27(4). (5) EH 27(4). (6) EH 27(5). (7) EH 27(4). (8) EH 27(4). (9) EH 27(4).
Defined terms:	absolute value, amount, cash basis person, Commissioner, derived, financial arrangement, fixed principal financial arrangement, income, income year, incurred, old financial arrangements rules, person, spreading method, variable principal debt instrument.

EH 64 Financial arrangements, income, and expenditure relevant to criteria

Inclusions in and exclusions from thresholds

(1) The calculations required by section EH 63 (1) to (3) are done for every financial arrangement to which the natural person is a party or, as the relevant subsection requires, to income and expenditure from such an

arrangement, whether the financial arrangements rules or the old financial arrangements rules apply to the arrangement. Two qualifications on this subsection are as follows:

(a) the calculations include an arrangement, or income and expenditure, to which subsection (2) or subsection (3) applies only to the extent of the person's interest in it, as described in each subsection; and

(b) the calculations exclude the value of an arrangement, and income and expenditure, in which the person has the interest described in subsection (4) or subsection (5).

Natural person who is partner

(2) This subsection applies when a partnership required to make a joint return of income under section 42 (1) of the Tax Administration Act 1994 is a party to a financial arrangement. A natural person who is a partner in the partnership—

(a) is a party to the arrangement to the extent of the partner's share in the arrangement; and

(b) derives income or incurs expenditure from the arrangement to the extent of the partner's share in the income or expenditure of the partnership.

Natural person who is beneficiary of bare trust

(3) This subsection applies when a bare trust is a party to a financial arrangement. A natural person who is a beneficiary of the bare trust—

(a) is treated as a party to the arrangement; and

(b) is treated as deriving income or incurring expenditure from the arrangement to the extent of the beneficiary's share of the beneficial interest in the arrangement.

Natural person who is beneficiary of trust other than bare trust

(4) This subsection applies when a natural person is a beneficiary of a trust, other than a bare trust, that is a party to a financial arrangement. The following are excluded from the calculations required by section EH 63 (1) to (3):

(a) the value of the arrangement, if it produces trustee income or beneficiary income under the trust rules or sections HI 1 to HI 5; and

(b) income from the arrangement that is trustee income or beneficiary income under the trust rules or sections HI 1 to HI 5.

Natural person who is trustee

(5) This subsection applies when a natural person is a party to a financial arrangement as a trustee. The following are excluded from the calculations required by section EH 63 (1) to (3):

(a) the value of the arrangement, if it produces trustee income or beneficiary income under the trust rules or sections HI 1 to HI 5; and

(b) income from the arrangement that is trustee income or beneficiary income under the trust rules or sections HI 1 to HI 5; and

(c) the value of the arrangement, if expenditure is incurred from it; and

(d) expenditure incurred from the arrangement.

Origin:	(1) EH 27(6). (2) EH 30. (3) EH 28(4). (4) EH 28(2). (5) EH 28(1), (2), (3).
Defined terms:	beneficiary income, derive, financial arrangement, financial arrangements rules, income, old financial arrangements rules, person, return of income, trust rules, trustee, trustee income.

EH 65 Exclusion by Commissioner

The Commissioner may treat a natural person who would otherwise be a cash basis person for a class of financial arrangements as not being a cash basis person for the class if that or any other person has structured and promoted the class to defer an income tax liability.

Origin:	EH 27 (8).
Defined terms:	cash basis person, Commissioner, financial arrangement, income tax liability, person.

EH 66 Trustee of deceased's estate

When trustee of estate is cash basis person

(1) A trustee of a deceased's estate is a cash basis person for financial arrangements in the estate in the circumstances described in subsection (2) for the period described in subsection (3).

Circumstances

(2) The circumstances are that, at the time of the deceased's death,—

(a) the deceased is a cash basis person; and

(b) the financial arrangements in the deceased's estate meet the requirements of section EH 62 (1)(a) and (b).

Period

(3) The period is the income year in which the deceased dies and in each of the 4 following income years. However, if at any time in those 5 income years the financial arrangements in the deceased's estate cease to meet the requirements of section EH 62 (1)(a) and (b), the trustee ceases to be a cash basis person for financial arrangements in the estate and cannot again be a cash basis person for them.

Modifications to be read in

(4) For the purposes of this section, sections EH 62 to EH 64 are read with the modifications necessary to make them refer to the case of a deceased estate.

Origin:	(1) EH 29(1). (2) EH 29(1). (3) EH 29(1), (2). (4) new.
Defined terms:	cash basis person, financial arrangement, income year, trustee.

EH 67 Election to use spreading method

Election of spreading method

(1) A cash basis person may choose to use a spreading method, unless subsection (2) applies.

Election not allowed

(2) A cash basis person may not choose to use a spreading method for a financial arrangement in the income year in which section EH 35 requires them to calculate a base price adjustment for the arrangement.

How to choose

(3) The person makes the election by calculating a cash basis adjustment under section EH 68 (1).

Effect of election

(4) The person must use a spreading method for—

(a) all financial arrangements to which the person is a party at the time of making the election; and

(b) all financial arrangements the person enters into after the income year in which they make the election.

How to revoke

(5) The person revokes the election by giving notice to the Commissioner with a return of income and within the time that the return must be filed under section 37 of the Tax Administration Act 1994.

Effect of revocation

(6) The revocation applies to all financial arrangements the person enters into after the income year in which the notice is given.

Origin:	(1) EH 31(1). (2) EH 31(3). (3) EH 31(2). (4) EH 31(5). (5) EH 31(6), (7). (6) EH 31(6).
Defined terms:	cash basis person, Commissioner, financial arrangement, income year, notice, return of income, spreading method.

EH 68 When and how calculation of cash basis adjustment required

Choosing spreading method

(1) A cash basis person who chooses to use a spreading method must calculate a cash basis adjustment for the income year in which they choose to use a spreading method as if they had ceased to be a cash basis person.

Person becoming cash basis person

(2) A person who becomes a cash basis person in an income year must calculate a cash basis adjustment for a financial arrangement to which they—

(a) are a party at the end of the income year; and

(b) were a party at the end of the previous income year.

Exceptions

(3) However,—

(a) a person who becomes a cash basis person in an income year and who chooses to continue using a spreading method in the income year must not calculate a cash basis adjustment; and

(b) a person who becomes a cash basis person in an income year must not calculate a cash basis adjustment for a financial arrangement that is already being accounted for on a cash basis.

Person ceasing to be cash basis person

(4) A person who ceases to be a cash basis person in an income year must calculate a cash basis adjustment for a financial arrangement to which they—

(a) are a party at the end of the income year; and

(b) were a party at the end of the previous income year.

Exception

(5) However, a person who ceases to be a cash basis person must not calculate a cash basis adjustment for a financial arrangement that is already subject to a spreading method.

Person not cash basis person if adjustment not made

(6) A person who would be a cash basis person for a financial arrangement if they calculated a cash basis adjustment for it, and who does not calculate the adjustment, is not a cash basis person for the arrangement.

Cash basis adjustment

(7) A person calculates a cash basis adjustment using the formula in section EH 69.

Adjustment is income or expenditure

(8) The only income or expenditure from the financial arrangement for the income year to which the formula is applied is the cash basis adjustment.

Positive or negative cash basis adjustment

(9) A cash basis adjustment is,—

(a) if positive, income, under section CC 3 (1) (Financial arrangements), derived by the person in the income year for which the calculation is made:

(b) if negative, expenditure incurred by the person in the income year for which the calculation is made.

Origin:	(1) EH 32(1). (2) EH 32(1). (3) EH 31(4); EH 32(2). (4) EH 32(1). (5) EH 32(3). (6) EH 32(7). (7) EH 32(4). (8) EH 32(6). (9) EH 32(5).
Defined terms:	cash basis person, derived, financial arrangement, income, income year, person, spreading method.

EH 69 Cash basis adjustment formula

Formula

(1) A person calculates a cash basis adjustment using the formula—

$$\text{adjusted income} - \text{adjusted expenditure} - \text{previous income} + \text{previous expenditure}.$$

Definition of items in formula

(2) The items in the formula are defined in subsections (3) to (6).

Adjusted income

(3) **Adjusted income** is,—

(a) for a person who becomes a cash basis person, the amount that would have been income derived by the person from the financial arrangement if the person had been a cash basis person in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made; and

(b) for a person who ceases to be a cash basis person, the amount that would have been income derived by the person from the financial arrangement if the person had been required to use a spreading method in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made.

Adjusted expenditure

(4) **Adjusted expenditure** is,—

(a) for a person who becomes a cash basis person, the amount that would have been expenditure incurred by the person from the financial arrangement if they had been a cash basis person in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made; and

(b) for a person who ceases to be a cash basis person, the amount that would have been expenditure incurred by the person from the financial arrangement if the person had been required to use a spreading method in the period starting on the date on which they became a party to the arrangement and ending on the last day of the income year for which the calculation is made.

Previous income

(5) **Previous income** is income derived by the person from the financial arrangement in previous income years.

Previous expenditure

(6) **Previous expenditure** is expenditure incurred by the person from the financial arrangement in previous income years.

Origin:	(1) EH 32(4). (2) EH 32(4). (3) EH 32(4). (4) EH 32(4).

	(5) EH 32(4).
	(6) EH 32(4).
Defined terms:	amount, cash basis person, derived, financial arrangement, income, income year, person, spreading method.

EI – Controlled foreign company and foreign investment fund rules

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Controlled foreign company (CFC) rules

When a company is a controlled foreign company

EI 1 When a company is a CFC

A foreign company is a CFC if any of the following tests is met:

(a) there is a group of 5 or fewer New Zealand residents whose total control interests in the company are more than 50% in any one of the control interest categories:

(b) a single New Zealand resident holds a control interest of 40% or more unless at the same time—
   (i) another person also holds a 40% or greater control interest in the same control interest category; and
   (ii) the other person is not a New Zealand resident; and
   (iii) the other person is not associated with the New Zealand resident:

(c) there is a group of 5 or fewer New Zealand residents who can control the exercise of the shareholder decision-making rights for the company and, as a result, control the company's affairs.

Origin:	CG 4(1).
Defined terms:	associated person, CFC, company, control interest, control interest category, foreign company, New Zealand resident, person, shareholder decision-making rights.

How to calculate a person's control interest

EI 2 Four categories for calculating control interests

Direct control interests arise in four separate categories

(1) Under section EI 5 (1), direct control interests in a foreign company can arise in each of 4 separate categories of rights.

List of categories

(2) The 4 categories are—

(a) shareholding in the foreign company:
(b) shareholder decision-making rights for the foreign company:
(c) rights to receive income from the foreign company:
(d) rights to receive distributions of the company's net assets.

In each case, more detailed calculation rules appear in section EI 5.

Consequently, four categories of control interests

(3) Accordingly, the rules in section EI 3 for calculating control interests by totalling various direct and indirect control interests and associated parties' interests are applied on a category-by-category basis.

Origin:	(1) new. (2) new. (3) new.
Defined terms:	associated person, control interest, foreign company, income, shareholder decision-making rights.
Comment:	This section is explanatory only.

EI 3 Control interest: total of direct, indirect, and associated person interests

A New Zealand resident's control interest in a foreign company at any time is the total of the following for the relevant control interest category:

(a) any direct control interest that the person holds in the company:

(b) any direct control interests in the company held by persons associated with the New Zealand resident:

(c) any indirect control interests that the person holds in the company:

(d) any indirect control interests in the company held by persons associated with the New Zealand resident.

Origin:	CG 4(2).
Defined terms:	associated person, control interest, control interest category, foreign company, New Zealand resident, person.

EI 4 Limits to requirement to include associated person interests

Non-resident relatives

(1) For the purposes of section EI 3, a New Zealand resident is associated with a non-resident relative only if the New Zealand resident holds a direct control interest or indirect control interest in the foreign company.

No double counting

(2) Despite section EI 3 (b) and (d), for the purposes of determining whether a foreign company is a CFC, a direct control interest or indirect control interest may be counted only once.

Origin:	(1) CG 4(3). (2) CG 4(7).
Defined terms:	associated person, CFC, control interest, foreign company, New Zealand resident, non-resident, relative.
Comment:	Current section CG 4 (7) appears necessary only to deal with the associated person aggregation, even though it is more broadly drafted.

EI 5 Direct control interests

Categories of direct control interest

(1) A person has a direct control interest in a foreign company at any time if they hold—

(a) any of the shares in the foreign company:

(b) any of the shareholder decision-making rights (as defined in section OB 1 (Definitions)) for the company:

(c) a right to receive (or to apply) any of the income of the company for the accounting period in which the time falls:

(d) a right to receive (or to apply) any of the value of the net assets of the company, if they are distributed.

Percentage of total is counted

(2) The direct control interest in each control interest category is the percentage of the total that the person holds.

Available subscribed capital measurement

(3) When the direct control interest in the category in subsection (1)(a) is calculated, the percentage is the total of the available subscribed capital per share of the shares held as a percentage of the total available subscribed capital per share of all shares in the company.

Varying decision-making rights

(4) When the direct control interest in the category in subsection (1)(b) is calculated, if the percentage varies between the rights described in the different paragraphs of the definition in section OB 1 (Definitions), the highest percentage is taken.

Income distribution rights: assumptions

(5) When the direct control interest in the category in subsection (1)(c) is calculated, it is assumed that—

(a) the income is distributed on the last day of the accounting period; and

(b) the person's entitlement is unchanged during the period; and

(c) a payment of interest on a debenture subject to section FC 1 (Floating rate of interest on debentures) or section FC 2 (Interest on debentures issued in substitution for shares) is a distribution of income.

Origin:	(1) CG 4(4). (2) new. (3) CG 4(4)(a). (4) CG 4(4)(b). (5) CG 3(c); CG 4(4)(c).
Defined terms:	accounting period, available subscribed capital, control interest, control interest category, foreign company, income, payment, person, share, shareholder decision-making rights.

EI 6 Direct control interests include options and similar rights

Options and similar rights included in total

(1) For the purposes of section EI 5, a person is treated as holding something if they are entitled to acquire it or extinguish it.

Examples of entitlement

(2) A person is entitled to acquire or extinguish something if the entitlement is absolute or contingent and whether the entitlement—

(a) arises under a company's constitution; or

(b) arises under the terms of an option; or

(c) arises under the terms of a convertible note; or

(d) arises under the terms of any arrangement substantially similar to any of those described in paragraphs (a) to (c); or

(e) arises in some other way.

Standard security arrangements

(3) Despite subsections (1) and (2), a person is not treated as being entitled to acquire something if—

(a) the entitlement arises under a security arrangement; and

(b) the person acquired the security arrangement in a transaction entered into on an arm's length basis; and

(c) the security arrangement's terms conform to generally accepted commercial practice.

No double counting

(4) Despite subsections (1) and (2), for the purposes of determining whether a foreign company is a CFC, each of the percentage holdings described in section EI 5 may be counted only once.

Origin:	(1) CG 4(4). (2) CG 3(b). (3) CG 3(b) proviso. (4) CG 4(8).
Defined terms:	arrangement, CFC, company, control interest, convertible note, foreign company, person, security arrangement.

EI 7 Indirect control interests

How an indirect control interest arises

(1) A person has an indirect control interest in a foreign company to the extent to which the rules in this section attribute to them some or all of the direct control interests held by a CFC in the foreign company.

Attribution of the CFC's direct interests

(2) A CFC's direct control interest in another foreign company is attributed under the following subsections.

Associates

(3) For the purposes of this section, the CFC is treated as also holding any direct control interests in the foreign company held by persons associated with the CFC.

Attribution of direct interests to smallest controlling group

(4) The rules in subsections (6) to (11) apply to attribute the CFC's direct control interests to the smallest controlling group, to ensure that the attribution exercise does not dilute recognition of a factual chain of control.

Attribution on basis of respective income interests

(5) If the CFC's direct control interests are attributed to more than 1 person, the direct control interests are divided in proportion to each group member's respective income interest in the CFC.

If only one controlling group

(6) If there is only 1 group of New Zealand residents whose control interests have caused the CFC to be a CFC under section EI 1, the CFC's direct control interests are treated as being held by that group.

More than one group but one is smallest

(7) If there is more than 1 group whose control interests have caused the CFC to be a CFC under section EI 1, the CFC's direct control interests are attributed to the smallest group.

Equal smallest groups

(8) If there are 2 or more groups that are equally the smallest, and 1 group has the greatest total control interests in the CFC, the attribution is to that group.

Equal smallest groups with equal greatest control interests

(9) If there are 2 or more smallest groups with equal greatest total control interests in the CFC, the attribution is made in full to each group.

No double counting

(10) Despite subsection (9), for the purposes of determining whether a foreign company is a CFC, a direct control interest may be counted only once.

Applying this section sequentially down a chain

(11) If a foreign company becomes a CFC under this section, this section is then applied to attribute its direct control interests.

Origin:	(1) CG 4(5)(a).
	(2) new.
	(3) CG 4(6).
	(4) new.
	(5) CG 4(5)(a).
	(6) CG 4(5)(a)(i).
	(7) CG 4(5)(a)(ii).
	(8) CG 4(5)(a)(iii).
	(9) CG 4(5)(a)(iv).

	(10) CG 4(5)(a)(iv) proviso.
	(11) CG 4(5)(b).
Defined terms:	associated person, CFC, control interest, foreign company, income interest, New Zealand resident, person.
Comment:	It may be that an attempt should be made to simplify these rules into a simpler chain of control approach, such as in the Overseas Investment Act and Regulations definition of 'overseas person'.

How to calculate a person's income interest

EI 8 Income interest: total of direct and indirect interests

A person's income interest in a CFC at any time is the total of the following:

(a) any direct income interest that the person holds in the CFC:

(b) any indirect income interest that the person holds in the CFC.

Origin:	CG 5(1).
Defined terms:	CFC, direct income interest, income interest, indirect income interest, person.

EI 9 Direct income interests

Categories of direct income interest

(1) A person has a direct income interest in a CFC at any time if they hold—

(a) any of the shares in the foreign company:

(b) any of the shareholder decision-making rights (as defined in section OB 1 (Definitions)) for the company:

(c) a right to receive (or to apply) any of the income of the company for the accounting period in which the time falls:

(d) a right to receive (or to apply) any of the value of the net assets of the company, if they are distributed.

Percentage of total is counted

(2) The person's direct income interest is the percentage of the total that the person holds.

Highest taken if varying percentages

(3) However, if the percentage varies between the different categories, the person's direct income interest is the highest.

Available subscribed capital measurement

(4) When the direct income interest in the category in subsection (1)(a) is calculated, the percentage is the total of the available subscribed capital per share of the shares held as a percentage of the total available subscribed capital per share of all shares in the company.

Varying decision-making rights

(5) When the direct income interest in the category in subsection (1)(b) is calculated, if the percentage varies between the rights described in the different paragraphs of the definition in section OB 1 (Definitions), the highest percentage is taken.

Income distribution rights: assumptions

(6) When the direct income interest in the category in subsection (1)(c) is calculated, it is assumed that—

(a) the income is distributed on the last day of the accounting period; and

(b) the person's entitlement is unchanged during the period; and

(c) a payment of interest on a debenture subject to section FC 1 (Floating rate of interest on debentures) or section FC 2 (Interest on debentures issued in substitution for shares) is a distribution of income.

Origin:	(1) CG 5(2). (2) CG 5(2). (3) CG 5(2). (4) CG 5(2)(a). (5) CG 5(2)(b). (6) CG 5(2)(c), CG 3(c).
Defined terms:	accounting period, available subscribed capital, CFC, direct income interest, foreign company, income, payment, person, share, shareholder decision-making rights.

EI 10 Indirect income interests

Indirect income interest determined by looking through CFCs

(1) If a person has a direct income interest in a CFC, and the first CFC has a direct income interest in another CFC, the person has an indirect income interest in the other CFC.

Calculate indirect interest by multiplying

(2) The indirect income interest is calculated by multiplying the person's direct income interest in the first CFC by the first CFC's direct income interest in the other CFC.

Chains of CFCs

(3) If there are 2 or more CFCs in a chain of direct income interests between the person and a CFC, the person has an indirect income interest in the CFC at the end of the chain that is calculated by multiplying all the direct income interests in the chain.

Origin:	(1) CG 5(3). (2) CG 5(3). (3) CG 5(3).
Defined terms:	CFC, direct income interest, indirect income interest, person.

EI 11 Options and similar rights counted in some cases

Increase in income interest

(1) The rules in this section apply to increase a person's income interest in a CFC (the first CFC) in some cases.

Existence of option or similar right

(2) This section applies if the person (or some other person, such as another CFC taken into account when calculating an indirect income interest of the person in the first CFC) is at any time entitled to acquire one of the things listed in section EI 9 (1) in relation to the first CFC but does not hold it. (The entitlement is called the option in the rest of this section.)

Actual holder outside CFC rules attribution

(3) For this section to apply, the actual holder of the thing subject to the option must not be either—

(a) another CFC:

(b) a New Zealand resident, unless they are a New Zealand resident whose income interest in the first CFC for the accounting period in question is less than 10%.

Terms of option indicating person's economic ownership

(4) For this section to apply, the option must have one of the following features:

(a) if this section did not exist, the effect of the option would be to defeat the intent and application of subpart CQ (Attributed income from foreign equity), subpart DN (Attributed losses from foreign equity), or this subpart, taking into account the economic benefit that the person gets as a result of the CFC deriving income:

(b) the consideration payable for exercise of the option is less than the market value of the thing acquired at the time of the acquisition:

(c) the holder of the option (or an associated person) has directly or indirectly funded or assisted the actual holder to acquire or hold the thing subject to the option.

Income interest calculated as if option exercised

(5) If each requirement for this section to apply is met, the person's income interest is calculated as if the option holder had exercised the option.

Origin:	(1) CG 5(4). (2) CG 5(4). (3) CG 5(4). (4) CG 5(4). (5) CG 5(4).
Defined terms:	accounting period, associated person, CFC, derived, income, income interest, indirect income interest, New Zealand resident, person.

EI 12 Reduction if total interests more than 100%

When this section applies

(1) This section applies if the total income interests for a CFC for an accounting period would be more than 100% (because section EI 9 (3) requires the highest percentage to be taken if varying percentage shareholder rights are held).

Proportional reduction

(2) Each person's income interest for the period is reduced to the amount calculated using the formula—

$$\text{income interest before reduction} \quad x \quad \frac{100}{\text{total income interests before reduction.}}$$

Origin:	(1) CG 9. (2) CG 9.
Defined terms:	accounting period, amount, CFC, income interest, person.

EI 13 Income interests of partners

When this section applies

(1) This section applies when a partnership holds rights that would be an income interest in a CFC if the partnership were an individual.

Partners hold in proportion

(2) When income interests in the CFC are calculated, each partner is treated as holding a share of anything held by the partnership, in proportion to the partner's interest in the partnership.

Origin:	(1) CG 5(7). (2) CG 5(7)(a), (b), (c).
Defined terms:	CFC, income interest.

Ten percent threshold and variations in income interest level

EI 14 Attribution only if 10% threshold reached

A person has attributed CFC income or attributed CFC loss from a CFC only if the person's income interest in the CFC is 10% or more for the relevant accounting period.

Origin:	CG 6(1)(b).
Defined terms:	accounting period, attributed CFC income, attributed CFC loss, CFC, income interest, person.

EI 15 Associates included when applying 10% test

Associates included

(1) Solely for the purpose of applying the 10% threshold in section EI 14 (and the equivalent test in section EI 46 (1)(b)), a person's income interest in a CFC is increased by each income interest in the CFC for the accounting period of a person associated with the person.

Associates not included if CFCs

(2) Despite subsection (1), the income interest of an associate is not counted if the associate is a CFC.

Origin:	(1) CG 6(2). (2) CG 6(2).
Defined terms:	accounting period, associated person, CFC, income interest, person.
Comment:	In draft subsection (2), does it matter if the CFC is only a CFC for part of the period?

EI 16 Zero income interest on days when non-resident

Section applies if change of residence

(1) This section applies if a person becomes or ceases to be a New Zealand resident during an accounting period in which the person holds an income interest in a CFC.

Zero income interest on days non-resident

(2) If at all times during a particular day a person is not a New Zealand resident, their income interest in the CFC on that day is zero and section EI 17 applies accordingly.

Attribution not prevented

(3) This section does not override—

(a) section CD 11, which treats a dividend resulting from attributed repatriation as being derived while the person deriving it is a New Zealand resident; or

(b) section CQ 2 (3), which treats any attributed CFC income as being derived while the person deriving it is a New Zealand resident; or

(c) section CQ 5 (4), which treats any FIF income as being derived while the person deriving it is a New Zealand resident.

Origin:	(1) CG 5(6). (2) CG 5(6). (3) CG 5(6).
Defined terms:	accounting period, attributed CFC income, attributed repatriation, CFC, derived, income interest, New Zealand resident, non-resident, person.
Comment:	Draft subsection (3) may be unnecessary.

EI 17 Variations during accounting period: weighted average used

Section applies if income interest varies

(1) This section applies if a person's income interest in a CFC varies during an accounting period.

Weighted average used

(2) The person's income interest for the accounting period is a weighted average calculated by adding the amount calculated using the formula in subsection (3) for each period during the accounting period in which the income interest is unchanged.

Formula

(3) The formula is—

$$\text{income interest} \quad x \quad \frac{\text{days when unchanged}}{\text{days in the accounting period.}}$$

First day, last day

(4) The number of days when the income interest is unchanged—

(a) excludes the first day of the unchanging period:

(b) includes the last day of the unchanging period.

Origin:	(1) CG 5(5). (2) CG 5(5). (3) CG 5(5). (4) CG 5(5).
Defined terms:	accounting period, amount, CFC, income interest, person.

Calculation of attributed CFC income or loss

EI 18 Attributed CFC income or loss formula

If a person has attributed CFC income under section CQ 2 (When attributed CFC income arises) or an attributed CFC loss under section DN 2 (When attributed CFC loss arises), the amount of a person's attributed CFC income or loss from a CFC for an accounting period is calculated using the formula—

$$\text{person's income interest for accounting period} \quad x \quad \text{branch equivalent income or loss of CFC for accounting period.}$$

Origin:	CG 7(2).
Defined terms:	accounting period, amount, attributed CFC income, attributed CFC loss, branch equivalent income, CFC, income interest, loss, person.

EI 19 If CFC derives taxable distribution from non-qualifying trust

When section applies

(1) This section applies if—

(a) a CFC derives a taxable distribution from a non-qualifying trust in an accounting period; and

(b) a person has attributed CFC income or loss from the CFC for the period (or would have if the taxable distribution were included in the CFC's branch equivalent income).

Additional attributed CFC income

(2) The taxable distribution is excluded (under section EI 21 (32)) when calculating the CFC's branch equivalent income or loss, and instead the person has additional attributed CFC income.

Amount of additional attributed CFC income

(3) The amount of the additional attributed CFC income is calculated using the formula—

$$\text{person's income interest in CFC for accounting period} \quad x \quad \text{taxable distribution.}$$

Non-qualifying trust tax rate

(4) The person is liable for income tax on the additional attributed CFC income at the rate in schedule 1 that applies to section HH 3 (4) amounts (Gross income assessable to beneficiaries).

Origin:	(1) CG 7(4). (2) CG 7(4)(a). (3) CG 7(4)(a). (4) CG 7(4)(b).
Defined terms:	accounting period, amount, attributed CFC income, branch equivalent income, CFC, income tax, loss, non-qualifying trust, person, taxable distribution.
Comment:	Should the branch equivalent income simply be grossed up instead?

EI 20 Reduced attributed CFC loss if economic loss not equivalent

When no economic loss

(1) This section applies if—

(a) a person has an amount of attributed CFC loss; and

(b) the person suffers no, or substantially no, corresponding economic loss, whether because of a call option, a put option, or any other reason.

When attributed CFC loss excessive

(2) This section also applies if—

(a) a person has an amount of attributed CFC loss; and

(b) the amount is more than any corresponding economic loss of the person, whether because of the application of the rules for calculating the person's income interest or for any other reason.

Attributed CFC loss reduced to economic loss

(3) The attributed CFC loss is reduced to be equal to the economic loss (if any).

Origin:	(1) CG 7(3)(a). (2) CG 7(3)(b). (3) CG 7(3).
Defined terms:	amount, attributed CFC loss, income interest, person.
Comment:	This section is extremely broad and, arguably, its purpose should be left to a tax avoidance provision to achieve.

Calculation of branch equivalent income or loss

EI 21 Branch equivalent income or loss: calculation rules

Rules set out in this section

(1) For the purposes of calculating a person's attributed CFC income or loss, the branch equivalent income or loss of the CFC for an accounting period is calculated under the rules in this section. (The person is called the taxpayer in these rules.)

CFC treated as New Zealand resident

(2) The rules in this Act are applied as if the CFC were always a New Zealand resident, and—

(a) the CFC's branch equivalent income for the accounting period is equal to the CFC's net income for the period; and

(b) the CFC's branch equivalent loss for the accounting period is equal to the CFC's net loss for the period.

Modifications to rules

(3) However, the rules in the Act are modified by the following subsections when doing the calculation.

Conversion to New Zealand dollars

(4) The taxpayer must choose either—

(a) for all the calculations to be done in New Zealand dollars; or

(b) for all the calculations to be done in the currency of the CFC's financial accounts. (If the CFC has no financial accounts, the currency used is that of the CFC's country of residence.) The result is then converted into New Zealand dollars at the average of the close of trading spot exchange rates for the fifteenth day of each complete month that falls in the period.

Consent for change of currency

(5) Having chosen a currency, the taxpayer must use the same currency for calculating branch equivalent income or loss for the CFC for each later consecutive accounting period, unless the Commissioner allows the taxpayer to choose again.

Change for commercial purpose

(6) The Commissioner may consent to a change under subsection (5) only if satisfied that—

(a) the taxpayer's main purpose in changing is a commercial one (the advancing, deferring, or reducing of tax not being a commercial purpose); and

(b) the change does not have an effect of defeating the intent and application of subpart CQ (Attributed income from foreign equity), subpart DN (Attributed losses from foreign equity), or this subpart.

New Zealand currency for financial arrangements

(7) Despite subsections (4) to (6), New Zealand currency calculations must be used to calculate that part of the branch equivalent income or loss attributable to financial arrangements if—

(a) the total value of financial arrangements to which the CFC is a party is more than $1,000,000 at any time during the relevant accounting period (applying section EH 23 (2)(b) to measure the values); or

(b) the CFC's total net foreign exchange loss attributable to financial arrangements, calculated under subsections (4) to (6) for the accounting period, is more than $100,000.

Limit to subsection (7)

(8) Subsection (7) does not apply to a financial arrangement if—

(a) it is a variable principal debt instrument; and

(b) all the rights and obligations of all the parties to the financial arrangement are expressed in the currency chosen under subsection (4)(b); and

(c) no other party to the financial arrangement is associated with the CFC; and

(d) no person enters into the financial arrangement under an arrangement that has a purpose of defeating the application of subsection (7).

Opening cost base: tangible assets: first period

(9) If the taxpayer had no attributed CFC income or loss from the CFC for the previous accounting period, the taxpayer must choose whether to measure the cost base at the start of an accounting period of premises, plant, machinery, equipment, and trading stock of the CFC at—

(a) historical cost minus accumulated depreciation (if any), or another value used by the CFC as the starting value for the period for income tax calculations in the country in which the CFC is resident (but only if the value is below market value); or

(b) the starting value that would be used under this Act if the CFC had always been a New Zealand resident.

Opening cost base: tangible assets: later periods

(10) If the taxpayer had attributed CFC income or loss from the CFC for the previous period, the cost base at the start of an accounting period of premises, plant, machinery, equipment, and trading stock of the CFC is the closing value at the end of the previous period used to calculate the income or loss.

Opening cost base: financial arrangements: first period

(11) If the taxpayer had no attributed CFC income or loss from the CFC for the previous accounting period, the taxpayer must choose to calculate the consideration under the financial arrangements rules for a financial arrangement at the start of an accounting period, at either—

(a) the market value of the financial arrangement; or

(b) the absolute value calculated using the formula—

$$\text{consideration paid to the CFC} + \text{expenditure} - \text{consideration paid by the CFC} - \text{income.}$$

Definition of items in formula

(12) In the formula,—

(a) **consideration paid to the CFC** is the consideration paid to the CFC for all periods before the accounting period:

(b) **expenditure** is expenditure that would have been incurred under the financial arrangements rules for all periods before the accounting period if the CFC had been resident in New Zealand:

(c) **consideration paid by the CFC** is the consideration paid by the CFC for all periods before the accounting period:

(d) **income** is income that would have been derived under the financial arrangements rules for all periods before the accounting period if the CFC had been resident in New Zealand.

Provisions that do not apply

(13) The following provisions do not apply:

(a) the consolidation rules:

(b) sections CD 32 to CD 39, subpart CQ (Attributed income from foreign equity), subpart DN (Attributed losses from foreign equity), or this subpart to the extent to which any of the sections or subparts would result in attributed CFC income, attributed CFC loss, or attributed repatriation for the CFC:

(c) section CW 8 (Money lent to government of New Zealand):

(d) section CW 37 (1) (Local and regional promotion bodies):

(e) section DO 1 (Enhancements to land, except trees) and section DO 2 (Shelter belts):

(f) section EH 6 (Non-resident party carrying on business), section EH 7 (Trustee not resident), and section EH 17 (a) (Financial arrangements rules do not apply):

(g) section CB 26 (Refunds under income equalisation scheme), subpart DQ (Income equalisation schemes), and subpart EN (Income equalisation schemes):

(h) subpart FG (Apportionment of interest costs):

(i) section GC 3 (Effect on continuity provisions of change in beneficiaries of trust):

(j) section IE 1 (Net losses may be offset against future net income) and section IF 1 (Net losses may be offset against future net income):

(k) section IG 2 (Net loss offset between group companies) and section IG 3 (Special provisions in relation to group companies for 1991-92 income year).

Business treated as if carried on in New Zealand

(14) The following provisions apply as if the CFC's business activities were carried on in New Zealand:

(a) sections CT 1 to CT 4, CT 6 to CT 8, CX 38, DT 1 to DT 14, DT 16, DT 17, DT 19, and IH 3, all of which are sections dealing with petroleum mining:

(b) sections DO 4, DO 6, DO 7, DP 1, DP 3 to DP 5, and DP 9, all of which are sections dealing with farming and forestry expenditure:

(c) section EZ 11 (Additional depreciation loss for excluded depreciable property that is plant or machinery):

(d) the definitions in subpart OB (General definitions) that specifically apply for the purposes of those sections.

Transfer pricing rules

(15) Section GD 13 (Cross-border arrangement between associated persons) applies only to a transaction that has a purpose or effect of defeating any of the jurisdictional ring-fencing rules for CFC losses and tax credits in section DN 4 (Ring-fencing cap on deduction), section IE 3 (Attributed foreign net losses), section IG 4 (Group of companies attributed foreign net losses), section LC 4 (Foreign tax credits-controlled foreign companies), and section LC 5 (Group of companies controlled foreign company tax credits). Also, when section GD 13 is applied, the relevant definitions of associated persons are those in both section OD 7 (Defining when 2 persons are associated persons) and section OD 8 (3) (Further definitions of associated persons).

Dividends generally

(16) Sections CW 9 to CW 11 (which are sections dealing with exempt income from equity) and section CZ 8 (Treatment of units and interests in unit trusts and group investment funds on issue as at 1 April 1996) do not apply and dividends are income that is not exempt income, unless subsection (17) applies.

Some dividends exempt income

(17) Despite subsection (16), dividends are exempt income of the CFC if either—

(a) the dividends are derived by the CFC from another CFC and the taxpayer has a 10% or greater income interest (under the rules in sections EI 14 to EI 17) in the other CFC for an accounting period falling in the same relevant income year or the previous income year; or

(b) the dividends are from shares that are an attributing interest in a FIF of the CFC.

Benefits from money advanced

(18) When section CC 9 (Consideration other than in money) is applied, the borrower is treated as if it carries on a business in New Zealand.

No tainting by association

(19) Sections CB 6 to CB 8 (which are sections dealing with the disposal of land within 10 years) and section CV 1 (Companies within wholly-owned groups) do not apply to treat an amount derived by the CFC as income merely because of the activities of a person associated with the CFC if the associate is a non-resident.

Crown acquisition of land

(20) The reference in section EJ 4 (1) (Disposal of land to Crown) to the Crown includes any relevant government outside New Zealand.

Depreciation recovered

(21) When sections EF 40 to EF 43 are applied, the CFC is treated as having had a deduction for an amount of depreciation allowance or depreciation loss, and to have an adjusted tax value accordingly, if an amount of depreciation allowance or depreciation loss has been deducted when calculating the CFC's branch equivalent income or loss for any period and the attributed CFC income or loss of any person.

GST and value-added taxes

(22) When section CX 1 (Goods and services tax), section DB 2 (Goods and services tax), section EF 37 (Consideration for purposes of section EF 36), section EF 44 (Cost: goods and services tax), section EZ 1 (FIF interests held on 1 April 1993), and section EZ 12 (Additional depreciation loss for acquisitions or qualifying improvements between 16 December 1991 and 1 April 1994) are applied, references to output tax, input tax or goods and services tax payable include a reference to the equivalent item arising under the value-added tax or other tax rules of a country or territory outside New Zealand if the rules have a similar intent and application to the New Zealand goods and services tax rules.

Government grants to businesses

(23) When section DF 1 (Government grants to businesses) is applied, a reference to the New Zealand government includes a government outside New Zealand but, to the extent to which section DF 1 still does not apply to a grant or subsidy to the CFC from a government, the grant or subsidy is income of the CFC.

Subvention payments

(24) If an amount is paid as consideration for the transfer of tax losses,—

(a) it is income if derived by the CFC; and

(b) it is a deduction if payable by the CFC but only if paid to a person resident in the same country as the CFC and if deductible under the taxation law of that country.

Life insurer

(25) Subsection (26) applies if—

(a) the CFC itself carries on the business of providing life insurance; or

(b) shares in the CFC are held (directly or indirectly) by a foreign company (the parent company, in subsection (26)) that carries on the business of providing life insurance and those shares have to be taken into account under sections EI 8 to EI 13 to calculate the taxpayer's income interest in the CFC.

Policyholders

(26) If the test in subsection (25) is met, the life insurance rules do not apply and the branch equivalent income or loss of the CFC is the amount actuarially determined to be the part of the CFC's net income or loss to which shareholders (and not policyholders in either the CFC or the parent) are entitled.

When subsection (26) does not apply

(27) Despite subsection (25), subsection (26) does not apply if the Commissioner—

(a) considers that the amount calculated is not a reasonable reflection of the part attributable to shareholders; or

(b) has requested and not received sufficient information to enable the actuarial calculation to be reviewed.

Mineral mining activities

(28) Sections CG 13 to CG 15, CU 1 to CU 25, CX 39 to CX 41, CZ 5, CZ 6, DU 1 to DU 12, DZ 5, IH 4, and IH 5 (all of which are sections dealing with mineral mining) apply, with any necessary modifications, if the CFC carries on activities outside New Zealand that are substantially the same as the activities to which those sections apply.

Petroleum mining activities

(29) Sections CT 1 to CT 4, CT 6 to CT 8, CX 38, DT 1 to DT 14, DT 16, DT 17, DT 19, and IH 3 (all of which are sections dealing with petroleum mining) apply, with any necessary modifications, if the CFC carries on petroleum mining activities outside New Zealand that are substantially the same as the petroleum mining activities to which those sections apply.

Finance leases and specified leases

(30) A lease entered into by the CFC before the start of the first accounting period in which the CFC is a CFC is neither a finance lease (subject to the financial arrangements rules and sections FC 8A to FC 8I) nor a specified lease (subject to the rules in sections FC 6 to FC 8).

When subsection (30) does not apply

(31) Subsection (30) does not apply if another party to the lease is either a CFC or a New Zealand resident.

Taxable distribution from non-qualifying trust

(32) If the CFC gets a taxable distribution from a non-qualifying trust—

(a) section HH 3 (4) (Gross income assessable to beneficiaries) does not apply; and

(b) the taxable distribution is not taken into account in calculating the CFC's branch equivalent income or loss; and

(c) section EI 19 applies.

CFC with interest in FIF

(33) If the CFC has rights in a FIF,—

(a) the rights are not prevented from being an attributing interest of the CFC in a FIF merely because the notional New Zealand residence of the CFC under subsection (2) causes section EI 32 to apply; and

(b) the CFC's FIF income or loss is not taken into account in calculating the branch equivalent income; and

(c) section EI 46 applies.

Transitional treatment of cross-border reinsurance

(34) Section CZ 2 (General insurance with risk period straddling 1 July 1993) applies as if the reference to New Zealand were a reference to the CFC's country of residence.

Origin:	(1) CG 11(1). (2) CG 11(1). (3) CG 11(2). (4) CG 11(3). (5) CG 11(3A). (6) CG 11(3B). (7) CG 11(3C). (8) CG 11(3D). (9) CG 11(4)(b). (10) CG 11(4)(a). (11) CG 11(5). (12) CG 11(5). (13) CG 11(6), (16).

	(14) CG 11(7). (15) CG 11(8). (16) CG 11(9). (17) CG 11(9)(a), (b). (18) CG 11(10). (19) CG 11(11). (20) CG 11(12). (21) CG 11(13). (22) CG 11(14). (23) CG 11(15). (24) CG 11(18). (25) CG 11(19)(a), (b). (26) CG 11(19). (27) CG 11(19)(c), (d). (28) CG 11(21). (29) CG 11(22). (30) CG 11(23), (23A). (31) CG 11(23), (23A). (32) CG 11(24). (33) CG 11(25)(a). (34) CG 11(17).
Defined terms:	absolute value, accounting period, adjusted tax value, amount, arrangement, associated person, attributed CFC income, attributed CFC loss, attributed repatriation, attributing interest, branch equivalent income, branch equivalent loss, business, CFC, close of trading spot exchange rate, Commissioner, consideration, consolidation rules, deduction, derived, dividend, exempt income, FIF, FIF income, finance lease, financial arrangement, financial arrangements rules, foreign company, goods and services tax, goods and services tax payable, income, income interest, income tax, income year, input tax, lease, life insurance, life insurance rules, life insurer, loss, mineral, net income, net loss, New Zealand, New Zealand resident, non-qualifying trust, non-resident, output tax, person, petroleum, policyholder, resident in New Zealand, share, shareholder, specified lease, tax, taxable distribution, variable principal debt instrument.
Comment:	Although the length of this section is contrary to standard rewrite practice, an exception is considered justified because of the fact that the subsections are a list of items that have a similar function. An alternative is to put the modifying rules in a separate schedule, but it is debatable whether separation would assist readers. Draft subsection (21) needs further review to ensure it reflects the current depreciation rules. The interrelationship of draft subsections (29) and (14)(a) needs further review. The subsections should possibly be combined.

Grey list exemption

EI 22 Unqualified grey list CFCs

Meaning

(1) A CFC is an unqualified grey list CFC for an accounting period if—

(a) at all times in the accounting period it is resident in a country listed in schedule 3, part A; and

(b) in that country the CFC's income tax liability has not been reduced by applying any of the concessions listed in schedule 3, part B.

No attributed income or loss

(2) Section CQ 2 (g) (When attributed CFC income arises) and section DN 2 (g) (When attributed CFC loss arises) provide that no attributed CFC income or attributed CFC loss arises from an unqualified grey list CFC.

CFC with interest in FIF: look-through approach

(3) This section does not prevent FIF income or loss arising under section EI 46, if an unqualified grey list CFC has an interest in a FIF.

Origin:	(1) CG 13(1). (2) CG 13(1). (3) CG 13(1).
Defined terms:	accounting period, attributed CFC income, attributed CFC loss, CFC, FIF, FIF income, grey list, income tax, loss.

EI 23 Qualified grey list CFCs

Meaning

(1) A CFC is a qualified grey list CFC for an accounting period if—

(a) at all times in the accounting period it is resident in a country listed in schedule 3, part A; and

(b) in that country the CFC's income tax liability has been reduced by applying any of the concessions listed in schedule 3, part B.

Attribution using country's tax rules

(2) In the case of a qualified grey list CFC,—

(a) section EI 21 does not apply for the accounting period; and

(b) when section EI 18 is applied, the amount of branch equivalent income or loss for the period is equal to the net income or net loss calculated under the income tax law of the CFC's country of residence but—

  (i) excluding any allowance for carrying forward prior period losses; and

  (ii) adjusted to exclude the benefit of concessions listed in schedule 3, part B; and

  (iii) converted to New Zealand dollars under section EI 21 (4)(b).

Origin:	(1) CG 13(2). (2) CG 13(2).
Defined terms:	accounting period, amount, branch equivalent income, CFC, grey list, income tax, income tax, loss, net income, net loss, New Zealand.

Residence of companies

EI 24 Residence in grey list country

Necessary liability to income tax

(1) When each of subpart CQ (Attributed income from foreign equity), subpart DN (Attributed losses from foreign equity), and this subpart is applied, a CFC is resident in a country listed in schedule 3, part A, only if it is liable to income tax in the country because the CFC has any of the following in the country:

(a) its domicile:

(b) its residence:

(c) its place of incorporation:

(d) its place of management.

Section OE 2 overridden

(2) This section overrides section OE 2 (Determination of residence of company).

Origin:	(1) CG 13(1)(a). (2) CG 13(1)(a).
Defined terms:	CFC, grey list, income tax.

EI 25 Company moving to or from New Zealand

Company becoming foreign

(1) If a company becomes a foreign company, an accounting period of the company starts on the day when the company became a foreign company and the former accounting period ends on the previous day.

Company ceasing to be foreign

(2) If a foreign company ceases to be a foreign company, an accounting period of the company starts on the day when the company ceased to be a foreign company and the former accounting period ends on the previous day.

Pro-rating

(3) If subsection (1) or (2) applies to shorten an accounting period of a CFC, a person with attributed CFC income or loss from the CFC for the period may choose to calculate the branch equivalent income or loss of the CFC either—

- (a) using the results for the shortened period only; or
- (b) by applying the pro-rating formula in subsection (4) to the results for the unshortened period.

Pro-rating formula

(4) The formula for calculating branch equivalent income or loss under subsection (3)(b) is—

$$\text{unshortened period branch equivalent income or loss} \quad x \quad \frac{\text{days in shortened period}}{\text{days in unshortened period.}}$$

Origin:	(1) CG 12(1). (2) CG 12(2). (3) CG 12(3). (4) CG 12(3)(a).
Defined terms:	accounting period, attributed CFC income, branch equivalent income, CFC, company, foreign company, loss, New Zealand, person.

Change of CFC's balance date

EI 26 Change of CFC's balance date

When this section applies

(1) This section applies if a person—

- (a) has an income interest in a CFC; and
- (b) has calculated attributed CFC income or loss or attributed repatriation from the CFC on the basis of one accounting year (the old accounting year); and

(c) wants to change to use a different accounting year (the new accounting year) for the calculations.

Change requiring Commissioner's consent

(2) The person may make the change only if the Commissioner agrees.

Commissioner's reasons

(3) The Commissioner may consider any relevant factors when making the decision, including—

(a) whether the change is sought because ownership of the CFC has changed:

(b) whether the change is sought because of taxation or other legal requirements in a country where the CFC is resident or does business:

(c) whether the change is sought to achieve consistent balance dates in a group of companies:

(d) whether the change would postpone liability to income tax on attributed CFC income or on attributed repatriation or to dividend withholding payment on attributed repatriation.

No transitional deferral

(4) If the new accounting year ends in a later income year than the year the old accounting year ends in, and that fact would result in an amount of attributed CFC income or attributed repatriation being derived in the later income year, the amount is not deferred to the later income year and instead is treated as derived in the previous income year. However, this subsection applies only once, in the year of the transition.

Origin:	(1) CG 10(1). (2) CG 10(1). (3) CG 10(2). (4) CG 10(1).
Defined terms:	accounting year, amount, attributed CFC income, attributed repatriation, business, CFC, Commissioner, derived, dividend withholding payment, group of companies, income tax, income year, loss, person.

Ownership measurement concession

EI 27 Use of quarterly measurement

Use of quarterly measurement times

(1) In order to simplify the process of calculating a person's control interest or income interest in a foreign company, the person is treated as holding at all times during a calendar quarter the same interest (including a zero one) as the interest they hold at the end of the quarter.

Anti-avoidance

(2) The concession in subsection (1) is subject to the anti-avoidance rules in section GC 9 (Variations in control or income interests in foreign companies) and section GC 10 (Attributed foreign income and foreign investment fund income–arrangements in respect of elections).

Ignoring concession

(3) A person may choose not to apply the concession in subsection (1) when calculating their attributed CFC income or loss from a foreign company.

Election

(4) An election under subsection (3)—

(a) must be in the form required by the Commissioner; and

(b) is irrevocable; and

(c) applies in the income year in which it is made and later.

Origin:	(1) CG 3(e). (2) CG 3(e). (3) CG 3(e). (4) CG 3(e).
Defined terms:	attributed CFC income, Commissioner, control interest, foreign company, income interest, income year, loss, person, quarter.
Comment:	It would probably be preferable to reverse the default rule, that is, daily measurement used unless the person chooses to measure quarterly. If not reversed, this is, arguably, too obscure a spot for this rule.

Anti-avoidance rule: stapled stock

EI 28 Anti-avoidance rule: stapled stock

When this section applies

(1) This section applies when—

(a) a New Zealand resident holds rights (the stapled rights) that give rise to an income interest or control interest in a foreign company; and

(b) the rights may, or may ordinarily, be disposed of only together with rights in another company; and

(c) the other company is a New Zealand resident or a CFC.

Stapled rights held by company

(2) When each of subpart CQ (Attributed income from foreign equity), subpart DN (Attributed losses from foreign equity), and this subpart is applied, the stapled rights are held by the other company and not by the person.

Origin:	(1) CG 3(d). (2) CG 3(d).
Defined terms:	CFC, company, control interest, foreign company, income interest, New Zealand resident, person.

Foreign investment fund (FIF) rules

What is a foreign investment fund?

EI 29 Foreign investment funds (FIFs)

A FIF (foreign investment fund) is any of the following:

(a) a foreign company:

(b) a foreign superannuation scheme:

(c) an insurer under a life insurance policy, but not if the policy is offered or entered into in New Zealand (in which case the insurer is subject to the life insurance rules in relation to the policy):

(d) an entity described in schedule 4, part A.

Origin:	new.
Defined terms:	FIF, foreign company, foreign investment fund, foreign superannuation scheme, life insurance policy, life insurance rules, offered or entered into in New Zealand.

What is an attributing interest in a FIF?

EI 30 Attributing interests in FIFs

Three categories

(1) A person has an attributing interest in a FIF if—

(a) the person holds rights in one of the categories of rights described in subsections (2) to (4); and

(b) none of the exemptions in sections EI 32 to EI 37 applies to those rights.

Category 1: direct income interest in foreign company

(2) The first category is a direct income interest in a foreign company, as defined in section EI 31 (or in an entity described in schedule 4, part A).

Category 2: foreign superannuation scheme entitlement

(3) The second category is rights to benefit from a foreign superannuation scheme, as a beneficiary or a member.

Category 3: foreign life policy entitlement

(4) The third category is rights to benefit from a life insurance policy in relation to which a FIF is the insurer.

Inclusion of contingent rights in categories 2 and 3

(5) The second and third categories include rights that are contingent or discretionary.

Origin:	(1) CG 15(1). (2) CG 15(1)(a). (3) CG 15(1)(b). (4) CG 15(1)(c). (5) OB 1 'entitlement of the person to benefit'.
Defined terms:	attributing interest, FIF, direct income interest, foreign company, foreign superannuation scheme, life insurance policy, person.

EI 31 Direct income interest in a FIF

Categories of direct income interest

(1) A person has a direct income interest in a foreign company at any time if they hold—

(a) any of the shares in the foreign company:

(b) any of the shareholder decision-making rights (as defined in section OB 1 (Definitions)) for the company:

(c) a right to receive (or to apply) any of the income of the company for the accounting period in which the time falls:

(d) a right to receive (or to apply) any of the value of the net assets of the company, if they are distributed.

Percentage of total

(2) The person's direct income interest is the percentage of the total that the person holds.

Highest taken if varying percentages

(3) However, if the percentage varies between the different categories, the person's direct income interest is the highest.

Available subscribed capital measurement

(4) When the direct income interest in the category in subsection (1)(a) is calculated, the percentage is the total of the available subscribed capital per share of the shares held as a percentage of the total available subscribed capital per share of all shares in the company.

Varying decision-making rights

(5) When the direct income interest in the category in subsection (1)(b) is calculated, if the percentage varies between the rights described in the different paragraphs of the definition in section OB 1 (Definitions), the highest percentage is taken.

Income distribution rights: assumptions

(6) When calculating the direct income interest in the category in subsection (1)(c), it is assumed that—

(a) the income is distributed on the last day of the accounting period; and

(b) the person's entitlement is unchanged during the period; and

(c) a payment of interest on a debenture subject to section FC 1 (Floating rate of interest on debentures) or section FC 2 (Interest on debentures issued in substitution for shares) is a distribution of income.

'Company' defined

(7) In this section, and in defined terms referred to in this section, **company** includes an entity listed in schedule 4, part A.

Origin:	(1) CG 15(1)(a); CG 5(2). (2) CG 15(1)(a); CG 5(2). (3) CG 15(1)(a); CG 5(2). (4) CG 15(1)(a); CG 5(2)(a). (5) CG 15(1)(a); CG 5(2)(b). (6) CG 15(1)(a); CG 5(2)(c), CG 3(c). (7) new.
Defined terms:	accounting period, available subscribed capital, company, direct income interest, FIF, foreign company, income, payment, person, share, shareholder decision-making rights.

EI 32 CFC rules exemption

A person's rights in a FIF at any time are not an attributing interest if—

(a) the FIF is a CFC (controlled foreign company) at the time; and

(b) the person has an income interest of 10% or more in the CFC for the accounting period during which the time falls.

Origin:	CG 15(2)(a).
Defined terms:	accounting period, attributing interest, CFC, controlled foreign company, FIF, income interest, person.

EI 33 Grey list exemption

Exemption

(1) A person's rights in a FIF in an income year are not an attributing interest if, at all times in the year, the FIF is—

(a) resident in a country listed in schedule 3, part A (residence being determined under the rules in section OE 2 (3) to (6) (Determination of residence of company), which apply whether or not the FIF is a company); and

(b) liable to income tax in the country, because it has its domicile, residence, place of incorporation, or place of management there; and

(c) not an entity described in schedule 4, part B.

Exemption: categories 2 and 3

(2) Subsection (1) does not apply if the rights of the person are those described in section EI 30 (3) or (4).

Origin:	(1) CG 15(2)(b). (2) CG 15(2)(b).
Defined terms:	attributing interest, company, FIF, grey list, income tax, income year, person.

EI 34 Foreign exchange control exemption

A person's rights in a FIF are not an attributing interest if and to the extent to which—

(a) the person is a natural person; and

(b) the person acquired the rights—

  (i) before first becoming a New Zealand resident; or

  (ii) before exchange controls applying to the person and the interest were imposed by a foreign country; or

  (iii) before 8 pm (New Zealand Standard Time) on 2 July 1992; and

(c) the exchange controls prevent the person from deriving amounts from the rights, or from disposing of the rights, in New Zealand dollars (or consideration that is readily convertible into New Zealand dollars).

Origin:	CG 15(2)(c), (2)(e).
Defined terms:	amount, attributing interest, derived, FIF, person, New Zealand, New Zealand resident.

EI 35 Immigrant's four-year exemption

Categories 2 and 3

(1) Subsection (2) applies only to rights described in section EI 30 (3) or (4).

Exemption for four years after immigration

(2) A person's rights in a FIF at any time are not an attributing interest if—

(a) the person is a natural person; and

(b) the person had rights in the FIF (whether the same rights or different) before first becoming a resident of New Zealand; and

(c) the time in question is before the end of the period of 3 income years following the year in which they first became a New Zealand resident.

Origin:	(1) CG 15(2)(f). (2) CG 15(2)(f).
Defined terms:	attributing interest, FIF, income year, New Zealand, New Zealand resident, resident, person.

EI 36 Immigrant's exemption for accrued superannuation entitlement

Exemption

(1) The rights of a natural person to benefit, as a beneficiary or a member, from a foreign superannuation scheme at any time are not an attributing interest in a FIF to the extent to which the requirements in subsections (2) to (9) are met at the time.

Rights accruing before first becoming resident

(2) The rights must have accrued before the person first became a New Zealand resident.

Attribution formula

(3) The extent to which the rights have accrued before the person first became a resident is calculated using the formula—

$$\frac{\text{adjusted immigration value}}{\text{current value}} \quad x \quad \text{current value.}$$

Definition of items in formula

(4) In the formula,—

(a) **adjusted immigration value** is the market value of the rights on the day on which the person first became a New Zealand resident, adjusted to the extent reasonable to allow for the rate of earnings (or loss) of the scheme from that day until the relevant time:

(b) **current value** is the market value of the rights at the relevant time.

Employee scheme or self-employed

(5) Either—

(a) the scheme must be one where the person's rights can be acquired only through the person's employment; or

(b) the person must be wholly or mainly self-employed, either when the person first acquired the rights or at the relevant time for applying this section.

Contributions or benefits: link to income

(6) The amount contributed to the scheme by or on behalf of the person must be calculated—

(a) by some fixed relationship to the person's income from employment or self-employment; or

(b) to provide benefits that bear a fixed relationship to the person's income from employment or self-employment, except to the extent to which the benefits are adjusted by reference to an objective measure of inflation.

Contributions by person, employer, or other scheme

(7) Contributions to the scheme for the person's benefit must be made only by or on behalf of—

(a) the person; or

(b) the person's employer (or a person associated with the employer); or

(c) the representatives of another superannuation scheme—

(i) as a transfer of the person's benefit rights in the other scheme; and

(ii) if those benefit rights would have qualified for the exemption in this section.

Restricted rights to assign or cash in

(8) The person's future benefits under the scheme must not be able to be assigned, or exchanged for a current receipt of cash (or other property), except—

(a) if the person becomes physically incapacitated; or

(b) if the person is transferring the benefit rights into another, similar, scheme; or

(c) when or after the person retires at normal retiring age; or

(d) if the person is assigning the benefit rights to a spouse under a matrimonial property agreement; or

(e) at the cost of a substantial decrease in the present value of the benefits.

Matrimonial property assignment

(9) When the person has obtained the rights by their being assigned under a matrimonial property agreement, the exemption in this section applies if the assignor spouse would have been entitled to it.

Origin:	(1) CG 15(2)(c). (2) OB 1 ‘interest in an employment-related foreign superannuation scheme’. (3) CG 14(3). (4) CG 14(3). (5) OB 1 ‘interest in an employment-related foreign superannuation scheme’. (6) OB 1 ‘interest in an employment-related foreign superannuation scheme’. (7) OB 1 ‘interest in an employment-related foreign superannuation scheme’. (8) OB 1 ‘interest in an employment-related foreign superannuation scheme’. (9) OB 1 ‘interest in an employment-related foreign superannuation scheme’.
Defined terms:	amount, associated person, attributing interest, employer, FIF, foreign superannuation scheme, income, income from employment, New Zealand resident, person, superannuation scheme.
Comment:	In draft subsection (7), paragraphs (d) and (e) of the old definition in section OB 1 have been combined, as they seem to overlap and be contradictory.

EI 37 Non-resident’s pension or annuity exemption

Exemption

(1) The rights of a natural person to benefit from a pension or annuity provided by a FIF are not an attributing interest if the requirements in subsections (2) and (3) are met.

Relevant period of non-residence

(2) The person must have provided the consideration for acquiring the rights—

(a) when the person was not resident in New Zealand; or

(b) when the person was resident in New Zealand but in the period ending 3 years after the end of the income year in which they last became a New Zealand resident; or

(c) when the person was resident in New Zealand but as a result of commuting or transferring their interest in a superannuation fund in anticipation of their ceasing to be a New Zealand resident.

Restricted rights to assign or cash in

(3) The person’s future benefits must not be able to be assigned, or exchanged for a current receipt of cash (or other property), except—

(a) if the person is assigning the benefit rights to a spouse under a matrimonial property agreement; or

(b) at the cost of a substantial decrease in the present value of the benefits.

Elective exclusion of pre-1996-97 rights

(4) Subsection (1) does not apply if—

(a) the rights were acquired before the 1996-97 income year; and

(b) the person chose to treat the rights as an interest in a foreign investment fund for the 1996-97 and later income years by complying with the requirements in the section CG 15 (4) that was in this Act immediately before the section was repealed by the Income Tax Amendment Act 2002.

Origin:	(1) CG 15(2)(g). (2) OB 1 'qualifying private foreign annuity'. (3) OB 1 'qualifying private foreign annuity'. (4) CG 15(4).
Defined terms:	attributing interest, FIF, foreign investment fund, income year, New Zealand resident, non-resident, person, resident in New Zealand, superannuation fund.
Comment:	Should there be an exception for physical incapacity? Should there be an exception for transfers to another scheme? Should there be an exception for retirement at normal retiring age? See draft section EI 36 (7) for a comparison. The *Tax Information Bulletin* vol 13, no 2 (February 2001) expresses the view that the correct interpretation of the 4-year rule in draft subsection (2)(b) is that, if consideration is provided after the 4-year period, the interest becomes a FIF only from the end of the 4-year exemption for immigrants. However, this does not seem to reflect the statutory wording – which may well have contemplated only a single lump sum payment for any annuity, – meaning that a payment after the end of the 4-year period will normally coexist with the fact that the annuity only first arises then in any event. The reference in draft subsection (4) to the Income Tax Amendment Act 2002 is a reference to the Act that will implement the rewrite of Parts A to E.

Calculation of FIF income or loss

EI 38 Four calculation methods

Use of one calculation method

(1) If the tests in section CQ 5 (When FIF income arises) or section DN 6 (When FIF loss arises) are met, the amount of a person's FIF income or loss is calculated under—

(a) the accounting profits method; or

(b) the branch equivalent method; or

(c) the comparative value method; or

(d) the deemed rate of return method.

Choosing method

(2) The person must choose which calculation method applies by completing their return of income accordingly, but the choice is limited by the rules in sections EI 40, EI 41, and EI 50.

Origin:	(1) CG 16(1). (2) CG 17(1).
Defined terms:	accounting profits method, amount, branch equivalent method, calculation method, comparative value method, deemed rate of return method, FIF income, loss, person, return of income.

EI 39 Exclusion of death benefit amounts

Death benefit not included in FIF income

(1) When this section applies, a person is treated as not deriving FIF income to the extent to which the income arises solely from receiving a death benefit under a life insurance policy.

Contract before becoming resident

(2) This section applies if—

(a) the person (or the deceased) (the contracting party), when not a New Zealand resident, entered into a binding contract that gave rise to the benefit; and

(b) at the time the contract was entered into, the contracting party either had not previously been a New Zealand resident or had not been a resident for at least the previous 10 years; and

(c) the benefit was not increased by a voluntary action taken after the contracting party became a resident.

Pre-1992 contracts

(3) This section also applies if—

(a) before 2 July 1992 the person (or the deceased) entered into a binding contract giving rise to the benefit; and

(b) the benefit was not increased by a voluntary action taken on or after 2 July 1992.

Origin:	(1) CG 16(7). (2) CG 16(7). (3) CG 16(7).
Defined terms:	amount, derived, FIF income, income, life insurance policy, New Zealand resident, person.

EI 40 Limits on choice of calculation methods

Same method for same FIF

(1) If a person has 2 or more attributing interests in the same FIF for the same period, the person must use the same calculation method for calculating FIF income or loss from each interest in that period, except to the extent to which—

(a) the interests are of different classes; and

(b) this section prevents the same method being used.

Accounting profits method

(2) A person may use the accounting profits method for an accounting period to calculate FIF income or loss from an attributing interest in a FIF only if—

(a) the FIF is a company; and

(b) at all times during the accounting period when the FIF exists, interests in the FIF similar to the person's attributing interest were—

(i) quoted on the official list of a recognised exchange; or

(ii) offered widely by or on behalf of the FIF to the public in one or more countries; and

(c) the net after-tax accounting profits or losses of the FIF for the accounting period are calculated under generally accepted accounting principles (or an equivalent standard for consistent and undistorted reporting of net profits) of the country in which the FIF is resident; and

(d) the net after-tax accounting profits or losses are detailed in financial statements—

(i) sent or made available to shareholders in the FIF; and

(ii) readily available to interested members of the public; and

(iii) audited by a chartered accountant (or accountant of equivalent professional standard in the country in which the FIF is resident); and

(iv) for which such an accountant has given a standard audit opinion, without qualifications, to the effect that the financial statements represent the income and financial position of the FIF to the degree of validity normally required in the country in which the FIF is resident; and

(e) the net after-tax accounting profits or losses are calculated, in any case in which the FIF has one or more subsidiaries, on a consolidated basis; and

(f) the net after-tax accounting profits or losses include any extraordinary items; and

(g) the person has no reason to believe that the net after-tax accounting profits or losses do not fairly represent the net after-tax profits or losses of the FIF for the accounting period; and

(h) the FIF is not an entity described in schedule 4, part C; and

(i) the Commissioner has not concluded that the net after-tax accounting profits or losses do not fairly represent the net after-tax profits or losses of the FIF for the accounting period.

Branch equivalent method

(3) A person may use the branch equivalent method to calculate FIF income or loss from an attributing interest in a FIF for an accounting period only if—

(a) the FIF is a company; and

(b) the person can provide to the Commissioner, if requested, sufficient information to enable the Commissioner to check the calculations required by section EI 43.

Deemed rate of return method

(4) A person may use the deemed rate of return method to calculate FIF income or loss from an attributing interest in a FIF for an income year only if any of the following apply:

(a) it is not reasonably practicable for the person to use either—

(i) the comparative value method, because the person cannot determine the market value of the attributing interest at the end of the income year; or

(ii) the accounting profits method for any accounting period that falls wholly or partly in the year; or

(b) the person is a natural person and at all times during the income year the total value of attributing interests in FIFs held by the person is not more than $250,000, the value of each interest being—

(i) its book value (calculated under section EI 45 (7)) at the end of the previous income year, if the person held the interest then and used the deemed rate of return method to calculate FIF income for all attributing interests in the previous year:

(ii) its market value, in any other case; or

(c) section EI 41 requires the person to use that method; or

(d) section EI 49 requires the person to continue using that method.

Origin:	(1) CG 17(2). (2) CG 17(4), (6). (3) CG 17(4), (5). (4) CG 17(3).
Defined terms:	accounting period, accounting profits method, attributing interest, branch equivalent method, calculation method, Commissioner, company, comparative value method, deemed rate of return method, FIF, FIF income, income year, loss, person, recognised exchange, shareholder, tax.

EI 41 Default calculation method

When this section applies

(1) This section applies if—

(a) a person does not choose a calculation method to calculate FIF income or loss from an attributing interest for a period; and

(b) the rules in sections EI 40 and EI 50 do not have the effect of requiring a particular calculation method to be used.

Default choice

(2) The person is treated as having chosen to use, for the interest and the period,—

(a) if section EI 40 (2) allows the use of the accounting profits method and it is practical to use that method, that method; and

(b) if use of that method is not allowed or not practical,—

(i) the comparative value method if it is practical to use it; and

(ii) the deemed rate of return method if it is not practical to use the comparative value method.

Origin:	(1) CG 17(7). (2) CG 17(7).
Defined terms:	accounting profits method, attributing interest, calculation method, comparative value method, deemed rate of return period, FIF income, loss, person.

EI 42 Accounting profits method

Calculation formula

(1) If a person is using the accounting profits method to calculate FIF income or loss from an attributing interest in a FIF, the total FIF income or loss from all their attributing interests in the FIF for the relevant accounting period is calculated using the formula—

$$\text{accounting profits or losses} \quad x \quad \text{income interest.}$$

Definition of items in formula

(2) The items in the formula are defined in subsections (3) and (4).

Accounting profits or losses

(3) **Accounting profits or losses** is the net after-tax accounting profits or losses of the FIF for the accounting period.

Income interest

(4) **Income interest** is the person's income interest in the FIF for the accounting period. The income interest is calculated under all the following CFC rules (applying as if the FIF were a CFC):

(a) sections EI 8 to EI 11 and EI 13 (which, in general, describe how to calculate an income interest by totalling direct and indirect interests):

(b) sections EI 16 and section EI 17 (which describe how to deal with periods of non-residence and variations in ownership during an accounting period):

(c) section EI 27 (which describes a concession to allow ownership to be measured only on quarterly measurement dates) but subject to subsection (5).

Election to measure on 31 March only

(5) In order to simplify the process of calculating the person's income interest, the person may choose to be treated as holding, at all times during a tax year, the same interest (including a zero one) that they held at the end of the tax year. The person makes the election by completing their return of income accordingly for the relevant income year.

Choice irrevocable

(6) An election under subsection (5) is—

(a) irrevocable and applies to the person and all their attributing interests in the FIF in later years; but

(b) subject to the anti-avoidance rules in section GC 9 (Variations in control or income interests in foreign companies) and section GC 10 (Attributed foreign income and foreign investment fund income–arrangements in respect of elections).

Conversion to New Zealand dollars

(7) The person must choose either—

(a) for all the calculations to be done in the currency of the FIF's financial accounts, the result being then converted into New Zealand dollars at the average of the close of trading spot exchange rates for the fifteenth day of each complete month that falls in the accounting period; or

(b) for all the calculations of the net after-tax accounting profits or losses of the FIF to be done in New Zealand dollars.

Reduced FIF loss if economic loss not equivalent

(8) In the cases described in subsections (9) and (10), the amount of any FIF loss calculated under subsection (1) is reduced to be equal to the person's corresponding economic loss (if any).

Application of subsection (8) if no economic loss

(9) Subsection (8) applies if the person suffers no, or substantially no, economic loss corresponding to the FIF loss, whether because of a call option, a put option, or any other reason.

Application of subsection (8) if FIF loss excessive

(10) Subsection (8) also applies if the amount of FIF loss is more than any corresponding economic loss suffered by the person, whether because of the application of the rules for calculating the person's income interest or any other reason.

Origin:	(1) CG 20(1). (2) CG 20(1). (3) CG 20(1). (4) CG 20(1). (5) CG 20(2). (6) CG 20(2). (7) CG 16(11)(a), (12). (8) CG 20(3). (9) CG 20(3)(a). (10) CG 20(3)(b).
Defined terms:	accounting period, accounting profits method, amount, attributing interest, CFC, close of trading spot exchange rate, FIF, FIF income, FIF loss, income interest, income year, loss, New Zealand, person, return of income, tax, tax year.
Comment:	The 'income interest' calculation includes all the person's rights in the FIF. Therefore, the calculation result has to be the result for all the person's attributing interests in the FIF. Arguably, therefore, draft section EI 40 (1) should require the accounting profits or branch equivalent methods to be used for all interests in a FIF, even if in different classes. Rather than cross-referring, in draft subsection (3), to the CFC rules, it would have been possible to repeat those rules, but this would be a lengthy exercise.

EI 43 Branch equivalent method

Calculation formula

(1) If a person is using the branch equivalent method to calculate FIF income or loss from an attributing interest in a FIF, the total FIF income or loss from all their attributing interests in the FIF for the relevant accounting period is calculated using the formula—

$$\text{branch equivalent income or loss} \quad x \quad \text{income interest.}$$

Definition of items in formula

(2) The items in the formula are defined in subsections (3) and (4).

Branch equivalent income or loss

(3) **Branch equivalent income or loss** is the branch equivalent income or loss of the FIF for the accounting period. This is calculated by applying section EI 21 of the CFC rules—

(a) as if the FIF were a CFC and the person were calculating their attributed CFC income or loss; but

(b) subject to subsections (5) and (6).

Income interest

(4) **Income interest** is the person's income interest in the FIF for the accounting period. The income interest is calculated under all the following CFC rules (applying as if the FIF were a CFC):

(a) sections EI 8 to EI 11 and EI 13 (which, in general, describe how to calculate an income interest by totalling direct and indirect interests):

(b) sections EI 16 and EI 17 (which describe how to deal with periods of non-residence and variations in ownership during an accounting period):

(c) section EI 27 (which describes a concession to allow ownership to be measured only on quarterly measurement dates).

Taxable distribution

(5) If the FIF derives a taxable distribution from a non-qualifying trust in the accounting period,—

(a) the taxable distribution is excluded when calculating the FIF's branch equivalent income or loss (due to the combined effect of subsection (1) and section EI 21 (32)); and

(b) the person has additional attributed CFC income calculated by multiplying the taxable distribution by the person's income interest in the FIF; and

(c) the person is liable for income tax on the additional attributed CFC income at the rate in schedule 1 that applies to amounts under section HH 3 (4) (Gross income assessable to beneficiaries).

Interest in foreign company

(6) If the FIF itself has an income interest (calculated under subsection (4)) in a foreign company for the accounting period, the person has additional FIF income or loss calculated using the formula—

$$\text{interest} \quad x \quad \text{FIF's FIF income or loss.}$$

Definition of items in formula

(7) In the formula,—

(a) **interest** is the person's income interest in the FIF for the period:

(b) **FIF's FIF income or loss** is the FIF's FIF income or loss calculated under the rules in section EI 46 (4) and (5), as if the FIF were the CFC.

Application of CFC rules tax credit rules

(8) The rules in section LC 4 (Foreign tax credits—controlled foreign companies) and section LC 5 (Group of companies controlled foreign company tax credits) apply to allow the person to claim foreign tax credits but on the basis of the assumptions made in subsection (9). The rules in those sections allow foreign tax credits relating to attributed CFC income but apply a jurisdictional ring-fencing approach to the use of tax credits.

Assumptions in reading tax credit rules

(9) The rules in section LC 4 (Foreign tax credits—controlled foreign companies) and section LC 5 (Group of companies controlled foreign company tax credits) are applied as if—

(a) the FIF were a CFC; and

(b) the FIF income of the person from the FIF were attributed CFC income; and

(c) the person's income interest (calculated under subsection (4)) were their relevant income interest for the purposes of those sections; and

(d) any relevant person's FIF income calculated under the branch equivalent method from a FIF that is resident in the relevant country were attributed CFC income.

Reduced FIF loss if economic loss not equivalent

(10) In the cases described in subsections (11) and (12), the amount of any FIF loss calculated under subsections (1) and (6) is reduced to be equal to the person's corresponding economic loss (if any).

Application of subsection (10) if no economic loss

(11) Subsection (10) applies if the person suffers no, or substantially no, economic loss corresponding to the FIF loss, whether because of a call option, a put option, or any other reason.

Application of subsection (10) if FIF loss excessive

(12) Subsection (10) also applies if the amount of FIF loss is more than any corresponding economic loss suffered by the person, whether because

of the application of the rules for calculating the person's income interest or any other reason.

Origin:	(1) CG 21(1). (2) CG 21(1). (3) CG 21(1). (4) CG 21(1). (5) CG 21(2)(a). (6) CG 21(1)(b)(iii), (2)(b). (7) CG 21(1)(b)(iii), (2)(b). (8) CG 21(3). (9) CG 21(3). (10) CG 21(4). (11) CG 21(4). (12) CG 21(4).
Defined terms:	accounting period, amount, attributed CFC income, attributing interest, branch equivalent income, branch equivalent method, CFC, FIF, FIF income, FIF loss, foreign company, income interest, income tax, loss, non-qualifying trust, person, tax, taxable distribution.
Comment:	See the first comment under draft section EI 42. In draft subsection (4), rather than applying the special tax rate, should the amount simply be grossed up to achieve the same result? Rather than cross-referring, in draft subsections (3), (6), (7), and (8), to the CFC rules, it would have been possible to repeat those rules, but this would be a lengthy exercise.

EI 44 Comparative value method

Calculation formula

(1) If a person is using the comparative value method to calculate FIF income or loss from an attributing interest in a FIF, the FIF income or loss from that interest for the relevant income year is calculated using the formula—

$$(\text{closing value} \quad + \quad \text{gains}) \quad - \quad (\text{opening value} \quad + \quad \text{costs}).$$

Definition of items in formula

(2) The items in the formula are defined in subsections (3) to (6).

Closing value

(3) **Closing value** is the market value of the person's interest in the FIF at the end of the income year. (The value is zero if the person has disposed of the interest or is then applying another calculation method to it).

Gains

(4) **Gains** is the total of all amounts that the person derives during the income year from holding or disposing of the interest. The amounts include any foreign withholding tax or other tax that the person is allowed as a credit under section LC 1 (Credits in respect of tax paid in a country or territory outside New Zealand).

Opening value

(5) **Opening value** is the market value of the person's interest in the FIF at the end of the previous income year. (The value is zero if the person did not hold the interest then or was then applying another calculation method to it).

Costs

(6) **Costs** is the total of all expenditure that the person incurs during the income year in acquiring or increasing the interest.

Conversion of foreign currency amounts

(7) If an amount is derived from, or incurred on, the interest in a foreign currency during the year, the person must choose either—

(a) for each foreign currency amount in the year to be converted into New Zealand dollars using the exchange rate on the day the amount is derived or incurred; or

(b) for all foreign currency amounts in the year to be converted into New Zealand dollars at the average of the close of trading spot exchange rates for the fifteenth day of each month that falls in the year.

Origin:	(1) CG 18. (2) CG 18. (3) CG 18. (4) CG 18. (5) CG 18. (6) CG 18. (7) CG 16(11)(b), (12).
Defined terms:	amount, attributing interest, calculation method, close of trading spot exchange rate, comparative value method, derived, FIF, FIF income, income year, loss, New Zealand, person, tax.

EI 45 Deemed rate of return method

Calculation formula changes if interest changes

(1) If a person is using the deemed rate of return method to calculate FIF income or loss from an attributing interest in a FIF for an income year, the FIF income or loss is calculated—

(a) by the standard formula in subsection (3) if the person has held the interest unchanged throughout the year; and

(b) by totalling the amounts calculated by the part-year formula in subsection (5) for each part of the income year during which the interest is unchanged, in any other case.

When an interest changes

(2) A person's attributing interest in a FIF changes during an income year if the person—

(a) acquires or increases the interest; or

(b) disposes of or reduces the interest (but merely receiving an annuity payment from the interest is not a disposal or reduction).

Standard formula

(3) The standard formula is—

$$\text{opening book value} \times \text{deemed rate.}$$

Definition of items in standard formula

(4) In the standard formula,—

(a) **opening book value** is the book value of the interest at the end of the previous year, calculated under subsection (7) or subsection (8):

(b) **deemed rate** is the rate set by the Governor-General by Order in Council for this section for the relevant income year.

Part-year formula

(5) The part-year formula is—

$$(\text{opening book value} + \text{costs}) \times (\text{deemed rate} \times \frac{\text{days})}{365.}$$

Definition of items in part-year formula

(6) In the part-year formula,—

(a) **opening book value** is the book value (if any) of the interest at the end of the period before the part-year, calculated under subsection (7) or subsection (8):

(b) **costs** is the total of all expenditure (if any) that the person incurs in acquiring or increasing the interest during the part-year:

(c) **deemed rate** is the rate set by the Governor-General by Order in Council for this section for the relevant income year:

(d) **days** is the number of days in the part-year, (for this purpose, an acquisition or increase is treated as occurring at the start of a day and a disposition or reduction is treated as occurring at the end of a day).

Closing book value formula if not changing

(7) Subject to subsection (9), the book value, at the end of an income year or (in a case in which subsection (5) applies) a part-year, of an

attributing interest of a person in a FIF under the deemed rate of return method is calculated using the formula—

(opening book value + costs + deemed income + top-up amounts) - gains.

Definition of items in closing book value formula

(8) In the closing book value formula,—

(a) **opening book value** is the book value (if any) of the interest at the end of the previous year or part-year, calculated under subsection (7) or subsection (8):

(b) **costs** is the total of all expenditure (if any) that the person incurs in acquiring or increasing the interest during the year or part-year:

(c) **deemed income** is the FIF income from the interest for the year or part-year calculated under subsection (3) or subsection (5):

(d) **top-up amounts** is amounts (gains from holding or disposing of the interest) that are top-up FIF income in the year under section EI 48 or section EI 49:

(e) **gains** is the total of all amounts that the person derives during the year or part-year from holding or disposing of the interest, (the amounts include any foreign withholding tax or other tax that the person is allowed as a credit under section LC 1 (Credits in respect of tax paid in a country or territory outside New Zealand)).

Closing book value zero if changing to another method

(9) The closing book value is always zero if the person is using a calculation method for the interest different from the deemed rate of return method at the end of the year or (in a case to which subsection (5) applies) the part-year.

Top-up income if deemed rate inadequate

(10) If the closing book value of a person’s attributing interest in a FIF at the end of a year or part-year is below zero, the person has additional FIF income equal to the deficit for the relevant income year.

Exemption from subsection (10)

(11) Subsection (10) does not apply if—

(a) the person is a natural person; and

(b) at all times during the income year the total value of the person’s attributing interests in FIFs is not more than $250,000, the value of each interest being—

(i) its book value (calculated under subsection (7) or subsection (8)) at the end of the previous income year, if the person held the interest then and used the deemed rate of return method to calculate FIF income for all attributing interests in the previous year:

(ii) its market value, in any other case; and

(c) the deficit in closing book value arises only because the person disposed of some or all of the interest; and

(d) the gain that the person derived from disposing of the interest or part-interest is not income, except to the extent to which it gives rise to FIF income.

Top-up income if gains more than deemed income

(12) A person calculating FIF income under the deemed rate of return method can also have additional FIF income under section EI 48.

FIF income reduced on disposal if deemed rate excessive

(13) If a person has disposed of the whole of an attributing interest in a FIF and the closing book value for the relevant year or part-year is more than zero, the excess is subtracted when the person's FIF income under the deemed rate of return method for the year is calculated.

When subsection (13) does not apply

(14) Subsection (13) does not apply if—

(a) the person is a natural person; and

(b) at all times during the income year the total value of attributing interests in FIFs held by the person is not more than $250,000, the value of each interest being—

(i) its book value (calculated under subsection (7) or subsection (8)) at the end of the previous income year, if the person held the interest then and used the deemed rate of return method to calculate FIF income for all attributing interests in the previous year:

(ii) its market value, in any other case; and

(c) the gain that the person derived from disposing of the interest or part-interest is not income, except to the extent to which it gives rise to FIF income.

Conversion of foreign currency amounts

(15) If an amount is derived from, or incurred on, the interest in a foreign currency during the year, the person must choose either—

(a) for each foreign currency amount in the year to be converted into New Zealand dollars using the exchange rate on the day the amount is derived or incurred; or

(b) for all foreign currency amounts in the year to be converted into New Zealand dollars at the average of the close of trading spot exchange rates for the fifteenth day of each complete month that falls in the year.

Origin:	(1) CG 19(1). (2) CG 19(4). (3) CG 19(1). (4) CG 19(1). (5) CG 19(4). (6) CG 19(4). (7) CG 19(5). (8) CG 19(5). (9) CG 19(5). (10) CG 19(2). (11) CG 19(2). (12) new. (13) CG 19(3). (14) CG 19(3). (15) CG 16(11)(b), (12).
Defined terms:	amount, attributing interest, calculation method, close of trading spot exchange rate, deemed rate of return method, derived, FIF, FIF income, income, income year, loss, New Zealand, payment, person.
Comment:	Current section CG 19 (6) and (7) are not rewritten as they appear to be adequately covered by section 225 of the Tax Administration Act 1994.

Additional FIF income or loss if CFC owns FIF

EI 46 Additional FIF income or loss if CFC owns FIF

When this section applies

(1) This section applies if—

(a) a person has an income interest of 10% or more in a CFC for an accounting period, under the rules in sections EI 8 to EI 17; and

(b) because section EI 21 (33) applies, FIF income and FIF loss is not taken into account in calculating the branch equivalent income or loss of the CFC for the period for the person.

FIF income or loss formula

(2) The person instead has FIF income or loss, for the income year in which the period ends, calculated using the formula—

$$\text{income interest} \quad x \quad \text{CFC's FIF income or loss.}$$

Definition of items in formula

(3) In the formula,—

(a) **income interest** is the person's income interest in the CFC for the period under the rules in sections EI 8 to EI 13:

(b) **CFC's FIF income or loss** is the CFC's FIF income or loss for the period calculated under subsections (4) and (5).

Application of FIF rules to choice of method

(4) The person must—

(a) choose, under the rules in sections EI 38 to EI 41, the calculation method for calculating the CFC's FIF income or loss; and

(b) otherwise apply the calculation rules in sections EI 38 to EI 49 as if the person directly held the attributing interest; and

(c) apply the FIF loss ring-fencing rules in section DN 8 (Ring-fencing cap on deduction: not branch equivalent method) and section DN 9 (Ring-fencing cap on deduction: branch equivalent method) as if the person directly held the attributing interest.

Exclusion of policyholder entitlements

(5) Despite subsection (4), the CFC's FIF income or loss does not include any amount actuarially determined to be attributable to policyholders in the CFC or another company as a result of applying the rules in section EI 21 (25) and (26) to the CFC.

Unqualified grey list CFCs still subject to rule

(6) This section applies whether or not the CFC is an unqualified grey list CFC under the rules in section EI 22 for the period.

Origin:	(1) CG 7(5). (2) CG 7(5). (3) CG 7(5). (4) CG 11(25)(b). (5) CG 11(25)(c). (6) CG 13(1).
Defined terms:	accounting period, amount, attributing interest, branch equivalent income, calculation method, CFC, company, FIF income, FIF loss, FIF rules, grey list, income interest, income year, loss, person, policyholder.

Relationship with other provisions in Act

EI 47 Codes: comparative value and deemed rate methods

When this section applies

(1) This section applies when a person has an attributing interest in a FIF and calculates their FIF income or loss from the interest for a period using the comparative value method or the deemed rate of return method.

No income other than FIF income

(2) The person is treated as not having any income from the interest for the period other than FIF income and, in particular, any dividends derived in the period from the interest and any income gain from disposing of the interest in the period are disregarded.

No deductions other than FIF loss

(3) The person is not allowed a deduction for any amount incurred in the period on acquiring some or all of the interest, except to the extent to which the amount is taken into account under the relevant calculation method in calculating FIF income or loss for the period.

Application of trading stock rules

(4) The interest is not trading stock in the period and accordingly the rules in subpart EC (Valuation of trading stock (including dealer's livestock)) do not apply.

Origin:	(1) CG 16(6). (2) CG 16(6)(a). (3) CG 16(6)(b). (4) CG 16(6)(c).
Defined terms:	amount, attributing interest, calculation method, comparative value method, deduction, deemed rate of return method, derived, dividend, FIF, FIF income, FIF loss, income, loss, person.
Comment:	A reference to this draft section will be placed in draft subpart CQ (Attributed income from foreign equity) and draft subpart DN (Attributed losses from foreign equity).

EI 48 Top-up FIF income: deemed rate of return method

When this section applies

(1) This section applies at any time when a person—

(a) has an attributing interest in a FIF for a period; and

(b) is calculating the FIF income or loss from the interest using the deemed rate of return method; and

(c) derives in the period, from holding or disposing of the interest, an amount that would have been income if section EI 47 (2) had not applied.

Gain income if deemed rate inadequate

(2) The gain is FIF income to the extent to which the amount calculated using the following formula is positive:

$$\text{total income gains} \quad - \quad \text{total FIF income.}$$

Definition of items in formula

(3) In the formula,—

(a) **total income gains** is the total of amounts (including the amount in question) derived by the person until that time from holding or disposing of the interest that would have been income if section EI 47 (2) had not applied:

(b) **total FIF income** is the total of FIF income (reduced by the total of any FIF losses) derived by the person from the interest until (and including) the relevant period.

Consequence of partial sale

(4) If the person disposes of part of the interest, this section applies to the part disposed of and the part retained as if they were separate interests. If this means that an apportionment is necessary, it must be done on the basis of the respective market values at the time the part interest is disposed of.

Origin:	(1) CG 22(1). (2) CG 22(1). (3) CG 22(1). (4) CG 22(2).
Defined terms:	amount, attributing interest, deemed rate of return method, derived, FIF, FIF income, FIF loss, income, loss, person.

EI 49 Top-up FIF income: 1 April 1993 uplift interests

When this section applies

(1) This section applies at any time if a person—

(a) has an attributing interest in a FIF for a period; and

(b) held the interest on 2 July 1992; and

(c) calculated their FIF income from the interest in the period starting on 1 April 1993 under the comparative value method or the deemed rate of return method; and

(d) was treated as having reacquired the interest on 1 April 1993 for an uplifted cost under section CG 23 (1)(d) (as it applied then); and

(e) derives in the period, from holding or disposing of the interest, an amount that would have been income if section EI 47 (2) had not applied.

Gain income if FIF income accrual inadequate

(2) The gain is FIF income to the extent to which the amount calculated using the following formula is positive:

$$\text{total income gains} \quad - \quad \text{total FIF income.}$$

Definition of items in formula

(3) In the formula,—

(a) **total income gains** is the total of amounts (including the amount in question) that the person derived until that time from holding or disposing of the interest that would have been income if section EI 47 (2) had not applied:

(b) **total FIF income** is the total of FIF income (reduced by the total of any FIF losses) that the person derived from the interest until (and including) the relevant period.

Consequence of partial sale

(4) If the person disposes of part of the interest, this section applies to the part disposed of and the part retained as if they were separate interests. If this means that an apportionment is necessary, it must be done on the basis of the respective market values at the time the part interest is disposed of.

Origin:	(1) CG 22(1). (2) CG 22(1). (3) CG 22(1). (4) CG 22(2).
Defined terms:	amount, attributing interest, comparative value method, deemed rate of return method, derived, FIF, FIF income, FIF loss, income, person.

Changing calculation method

EI 50 Limits on change of method

No change unless allowed

(1) Once a person uses a particular calculation method to calculate FIF income or loss for an attributing interest in a FIF for a particular period, they must use the same method for interests in the FIF for the next period unless they are allowed to change under subsections (2) to (7).

Change on practical grounds

(2) The person may change if it is not practical to continue with the same method because—

(a) in the case of the accounting profits method, section EI 40 (2) prevents its continued use or it is impossible to obtain enough information to continue to use it:

(b) in the case of the branch equivalent method, it is impossible to obtain enough information to continue to use it:

(c) in the case of the comparative value method, it is impossible to find out the end-of-year market value of the interest:

(d) in the case of the deemed rate of return method, if the person was entitled to use that method only by falling under the $250,000 threshold in section EI 40 (4)(b), the threshold is exceeded:

(e) in the case of the deemed rate of return method, if it was the default method under section EI 41, it ceases to be the default method.

Choosing to change

(3) The person may also change by notice to the Commissioner if—

(a) the notice complies with subsection (4); and

(b) either—

(i) the person is a natural person and the $250,000 threshold in subsection (5) is not exceeded; or

(ii) the change is to, or from, the branch equivalent method and within the rules in subsections (6) and (7).

Notice of election

(4) The notice of an election to change under subsection (3) must—

(a) give the reasons for the change; and

(b) comply with the Commissioner's notice requirements; and

(c) be given before the end of the first income year or accounting period for which the change is to take effect, unless the Commissioner agrees to a retrospective notice; and

(d) in the case of a natural person relying on the $250,000 threshold test in subsection (3)(b)(i), be given before the end of the year or period that is before the one from the end of which the change takes effect.

Natural person: $250,000 threshold

(5) A natural person may make an election under subsection (3) if the total market value of their attributing interests in FIFs is not more than $250,000 at the end of the income year or accounting period before the year or period from the end of which the change takes effect.

Changes to or from branch equivalent method

(6) A person may make an election under subsection (3) to change—

(a) to the branch equivalent method if—

(i) this is the first time they have chosen to change to the branch equivalent method for an attributing interest in the FIF; or

(ii) subsection (7) allows them to make another election:

(b) from the branch equivalent method if—

(i) they are changing back to a calculation method that they used for attributing interests in the fund before they used the branch equivalent method; and

(ii) this is the first time they have chosen to change from the branch equivalent method, unless subsection (7) allows them to make another election.

Repeated change to or from branch equivalent method

(7) A person may change more than once to, or from, the branch equivalent method if—

(a) there has been a change in circumstances (such as a significant change in shareholding) that significantly changes their ability to obtain enough information to use the branch equivalent method; and

(b) altering their income tax liability is not the principal purpose or effect of the change.

Origin:	(1) CG 17(8). (2) CG 17(8)(a), (b). (3) CG 17(9). (4) CG 17(9)(a), (b)(iii)(B). (5) CG 17(9)(b)(iii)(A). (6) CG 17(9)(b)(i), (ii). (7) CG 17(10).
Defined terms:	accounting period, accounting profits method, attributing interest, branch equivalent method, calculation method, Commissioner, comparative value method, deemed rate of return method, FIF, FIF income, income tax liability, income year, loss, notice, person.
Comment:	Draft subsection (4)(c) (current section CG 17 (9)(b)(iii)(B)) requires notice to be given before the date on which the $250,000 test is applied.

EI 51 Consequences of changes in method

Changes between cost-based methods and look-through methods

(1) Subsection (2) applies if a person holding an attributing interest in a FIF changes the calculation method for calculating FIF income or loss from the interest—

(a) from either of the cost-based calculation methods (the comparative value method and the deemed rate of return method) to either of the look-through calculation methods (the accounting profits method and the branch equivalent method); or

(b) from either of the look-through methods to either of the cost-based methods.

Treatment as sale for market value

(2) The person is treated as having—

(a) disposed of the interest to an unrelated person immediately before the start of the first accounting period to which the new method applies; and

(b) reacquired it immediately after the start of the period; and

(c) received for the disposal and paid for the reacquisition an amount equal to the interest's market value at the time.

Change from comparative value method to deemed rate of return method

(3) If a person holding an attributing interest in a FIF changes from the comparative value method to the deemed rate of return method for calculating FIF income or loss from the interest, the person is treated as having—

(a) disposed of the interest to an unrelated person immediately before the start of the first income year to which the new method applies; and

(b) reacquired it immediately after the start of the year; and

(c) received for the disposal and paid for the reacquisition an amount equal to the interest's market value at the time.

Change from deemed rate of return method to comparative value method

(4) If a person holding an attributing interest in a FIF changes from the deemed rate of return method to the comparative value method for calculating FIF income or loss from the interest, the person is treated as having—

(a) disposed of the interest to an unrelated person immediately before the start of the first income year to which the new method applies; and

(b) reacquired it immediately after the start of the year; and

(c) received for the disposal and paid for the reacquisition an amount equal to the interest's closing book value (calculated under section EI 45 (7)) at the end of the previous income year.

Origin:	(1) CG 24(1). (2) CG 24(1). (3) CG 24(2). (4) CG 24(2).
Defined terms:	accounting period, accounting profits method, amount, attributing interest, branch equivalent method, calculation method, comparative value method, deemed rate of return method, FIF, FIF income, income year, loss, person.

Cases of entry into and exit from FIF rules

EI 52 Migration of person holding FIF interest

Person leaving New Zealand

(1) Subsection (2) applies if a person—

(a) ceases to be resident in New Zealand; and

(b) holds an attributing interest in a FIF at the time; and

(c) for the period before the change of residence, uses the comparative value method or the deemed rate of return method to calculate FIF income or loss from the interest.

Treatment as sale at market value

(2) The person is treated as—

(a) having sold the interest immediately before the change of residence for an amount equal to its market value at the time; and

(b) not holding the interest when not resident in New Zealand (unless they become resident again and subsections (3) and (4) apply).

Person coming to New Zealand

(3) Subsection (4) applies if a person—

(a) becomes a resident of New Zealand; and

(b) holds an attributing interest in a FIF at the time; and

(c) for the period after the change of residence, uses the comparative value method or the deemed rate of return method to calculate FIF income or loss from the interest.

Treatment as purchase at market value

(4) The person is treated as—

(a) having bought the interest immediately after the change of residence for an amount equal to its market value at the time; and

(b) not holding it when not resident in New Zealand (unless they had previously ceased being resident and subsections (1) and (2) applied).

Look-through calculation method: relevance of income interest rules

(5) Subsection (6) applies if a person—

(a) ceases to be or starts being resident in New Zealand; and

(b) holds an attributing interest in a FIF at the time; and

(c) for the accounting period in which the change occurs, uses the accounting profits method or deemed rate of return method to calculate FIF income or loss from the interest.

Income interest rules

(6) The income interest rule in section EI 16 is relevant to the calculation of the amount of FIF income or loss for the period.

Origin:	(1) CG 23(3). (2) CG 16(4); CG 23(3). (3) CG 23(2). (4) CG 16(4); CG 23(2). (5) CG 16(4). (6) CG 16(4).
Defined terms:	accounting period, accounting profits method, amount, attributing interest, calculation method, comparative value method, deemed rate of return method, FIF, FIF income, income interest, loss, market value, New Zealand, person, resident in New Zealand.
Comment:	In draft subsection (3) (current section CG 23 (2)), there is a circularity problem – one cannot, in some cases, determine whether the $50,000 threshold is breached without applying the deemed sale rule.

EI 53 Change in application of FIF exemptions

Exemptions ceasing to apply

(1) Subsections (2) and (3) apply if a person—

(a) holds rights in one of the categories of rights described in section EI 30 (2) to (4); and

(b) either—

(i) the rights become an attributing interest in a FIF because one of the exemptions in sections EI 32 to EI 37 ceases to apply; or

(ii) the person starts having FIF income or loss from the rights because they incur a cost on an attributing interest in a FIF and exceed the $50,000 threshold in section CQ 5 (1)(d) (When FIF income arises) and section DN 6 (1)(d) (When FIF loss arises).

Market value for cost-based methods

(2) If the person uses the comparative value method or deemed rate of return method to calculate FIF income or loss from the rights for the period following the change, the person is treated as having—

(a) disposed of the rights to an unrelated person immediately before the change; and

(b) reacquired them immediately after the change; and

(c) received for the sale and paid for the repurchase an amount equal to their market value at the time.

Pro-rating under look-through methods

(3) If the change occurs during an accounting period of the FIF and the person uses the accounting profits method or the deemed rate of return method to calculate FIF income or loss from the rights for that period, the FIF income or loss is reduced by subtracting the amount calculated using the formula—

$$\text{FIF income or loss} \quad x \quad \frac{\text{days before change}}{\text{days in period.}}$$

Definition of items in formula

(4) In the formula,—

(a) **FIF income or loss** is the FIF income or loss of the person from the rights for the period before allowing for the reduction:

(b) **days before change** is the number of complete days in the period before the change occurs:

(c) **days in period** is the number of days in the period.

Exemptions starting to apply

(5) Subsections (2) to (4) apply if a person—

(a) holds an attributing interest in a FIF; and

(b) either—

(i) the interest ceases to be an attributing interest in a FIF because one of the exemptions in sections EI 32 to EI 35 starts to apply; or

(ii) the person ceases having FIF income or loss from the interest because they dispose of an attributing interest in a FIF and fall below the $50,000 threshold in section CQ 5 (1)(d) (When FIF income arises) and section DN 6 (1)(d) (When FIF loss arises).

Market value for cost-based methods

(6) If the person uses the comparative value method or the deemed rate of return method to calculate FIF income or loss from the interest for the period before the change, the person is treated as having—

(a) disposed of the interest to an unrelated person immediately before the change; and

(b) repurchased it immediately after the change; and

(c) received for the sale and paid for the repurchase an amount equal to its market value at the time.

Pro-rating under look-through methods

(7) If the change occurs during an accounting period of the FIF and the person uses the accounting profits methods or the deemed rate of return method to calculate FIF income or loss from the interest for that period, the FIF income or loss is reduced by subtracting the amount calculated using the formula—

$$\text{FIF income or loss} \quad x \quad \frac{\text{days after change}}{\text{days in period.}}$$

Definition of items in formula

(8) In the formula,—

(a) **FIF income or loss** is the FIF income or loss of the person from the interest for the period before allowing for the reduction:

(b) **days after change** is the number of complete days in the period after the change occurs:

(c) **days in period** is the number of days in the period.

Origin:	(1) CG 23(7). (2) CG 23(7). (3) CG 23(7). (4) CG 23(7). (5) CG 23(8). (6) CG 23(8). (7) CG 23(8). (8) CG 23(8).
Defined terms:	accounting period, accounting profits method, amount, attributing interest, comparative value method, deemed rate of return method, FIF, FIF income, loss, market value, person.
Comment:	In draft subsection (1)(b)(ii) (current section CG 23 (7)(b)), there is no reference to the threshold being breached just because the market value uplift applies. As with section EI 52, the existing reference may create circularity.

EI 54 FIF migrating from New Zealand

When this section applies

(1) This section applies when a person holds rights that become an attributing interest in a FIF because an entity becomes a FIF.

Cost-based methods using market value

(2) If the person uses the comparative value method or deemed rate of return method to calculate the FIF income or loss from the interest for the period following the change, the person is treated as having—

(a) disposed of the interest immediately before the change to an unrelated person; and

(b) repurchased it immediately after the change; and

(c) received for the sale and paid for the repurchase an amount equal to the market value of the interest at the time of the change.

Pro-rating under look-through methods

(3) If the change occurs during an accounting period of the FIF and the person uses the accounting profits method or deemed rate of return method to calculate FIF income or loss from the rights for that period, section EI 25 does not apply and the FIF income or loss is reduced by subtracting the amount calculated using the formula—

$$\text{FIF income or loss} \quad x \quad \frac{\text{days before change}}{\text{days in period.}}$$

Definition of items in formula

(4) In the formula,—

(a) **FIF income or loss** is the FIF income or loss of the person from the rights for the period before allowing for the reduction:

(b) **days before change** is the number of complete days in the period before the change occurs:

(c) **days in period** is the number of days in the period.

Origin:	(1) CG 23(7A). (2) CG 23(7B), (7C). (3) CG 23(7D). (4) CG 23(7D).
Defined terms:	accounting period, accounting profits method, amount, attributing interest, comparative value method, deemed rate of return method, FIF, FIF income, loss, New Zealand, person.
Comment:	Reference to the branch equivalent method does not appear in current section CG 23 (7D) but it seems appropriate to add it to draft subsection (3). Again, with regard to the $50,000 threshold, there may be circularity because an uplift under draft subsection (2) may be the cause of the threshold being breached.

EI 55 Death of person holding FIF interest

When this section applies

(1) This section applies when—

(a) a person dies; and

(b) they hold an attributing interest in a FIF at the time; and

(c) the comparative value method or the deemed rate of return method is used to calculate their FIF income or loss for the period before the death.

Treatment as sale for market value

(2) The person is treated as having sold the interest immediately before death for an amount equal to its market value at the time.

Origin:	(1) CG 23(4). (2) CG 23(4).
Defined terms:	attributing interest, comparative value method, deemed rate of return method, FIF, FIF income, loss, person.

Measurement of cost

EI 56 Measurement of cost

When this section applies

(1) This section applies when the cost of a person's attributing interest in a FIF is being measured for the purposes of—

(a) the natural person $50,000 exemption in section CQ 5 (1)(d) (When FIF income arises) and section DN 6 (1)(d) (When FIF loss arises); and

(b) the comparative value method; and

(c) the deemed rate of return method.

FIFO cost flow identification

(2) If it is not possible to specifically identify the cost of the interest, because of multiple acquisitions or dispositions or both by the person, the first-in-first-out (FIFO) method of identifying cost flows is applied.

Share splits or similar

(3) If the person acquires the interest as the result of a share split, non-taxable bonus issue, or similar event, and the acquisition is not income for the person, subsections (4) and (5) apply.

Allocation of original cost

(4) The cost of the interest is a fair allocation (based on market values at the time of the split) of the cost of the original property that is split.

Allocation replacing original cost

(5) For the income year in which the split occurs and later,—

(a) the cost allocated to the interest is no longer the cost of the original property that was split; and

(b) the person is treated as having incurred the allocated cost amount on acquiring the interest when the original property was acquired; and

(c) the person is treated as not incurring any other cost on the interest merely because the original property ceases to exist.

Non-monetary cost

(6) If any cost is incurred in kind and not in money, the amount of the cost is equal to the market value of the cost incurred in kind, measured as at the time incurred.

Exclusion of term life insurance element of premiums

(7) If the interest is an entitlement to benefit under a life insurance policy, the cost of the interest excludes a premium incurred in a previous income year (or accounting period) to the extent to which the premium relates only to term life insurance for the previous period and does not increase the policy's surrender value.

Exclusion of holding costs

(8) The cost of the interest does not include any expenditure under the financial arrangements rules or interest on money borrowed to acquire it, or other holding costs, incurred after its acquisition.

Origin:	(1) CG 14(1). (2) CG 14(1)(a). (3) CG 14(1)(b). (4) CG 14(1)(b). (5) CG 14(1)(b). (6) CG 14(1)(c). (7) CG 14(1)(d). (8) CG 14(1)(e).
Defined terms:	accounting period, attributing interest, amount, comparative value method, deemed rate of return method, FIF, financial arrangements rules, income, income year, life insurance, non-taxable bonus issue, person, premium, share.
Comment:	Current section CG 14 (1)(ca) is not rewritten on the basis that it seems to duplicate the rules for migration in current section CG 23, which involve a deemed sale and reacquisition at market in any event.

Change of FIF's balance date

EI 57 Change of FIF's balance date

When this section applies

(1) This section applies if a person—

(a) has an attributing interest in a FIF; and

(b) calculates their FIF income or loss from the FIF using the accounting profits method or the branch equivalent method; and

(c) has calculated FIF income or loss from the FIF on the basis of one accounting year (the old accounting year); and

(d) wants to change to use a different accounting year (the new accounting year) for the calculations.

Commissioner's consent

(2) The person may make the change only if the Commissioner agrees.

Commissioner's reasons

(3) The Commissioner may take into account any relevant factors when making the decision, including—

(a) whether the change is sought because ownership of the FIF has changed:

(b) whether the change is sought because of taxation or other legal requirements in a country where the FIF is resident or does business:

(c) whether the change would postpone liability to income tax on FIF income.

New accounting year if change approved

(4) If the change is approved, the person may use the new accounting year.

Limit on transitional deferral

(5) If, in order to make the transition, the transitional accounting period is more than 12 months and ends in a later income year than the old accounting year ends in, and that would result in an amount of FIF income being derived in the later income year, subsection (6) applies and section CQ 5 (1)(f) (When FIF income arises) does not.

Income pro-rated over whole period

(6) For the transitional accounting period, the FIF income is divided by the number of days in the period and the resulting amount is FIF income of the person derived on each day in the period.

Origin:	(1) CG 16(8). (2) CG 16(8). (3) CG 16(10). (4) CG 16(8). (5) CG 16(9). (6) CG 16(9).
Defined terms:	accounting period, accounting profits method, accounting year, amount, attributing interest, branch equivalent method, business, Commissioner, derived, FIF, FIF income, income tax, income year, loss, person, tax.

Market value rules

EI 58 Market value of life policy and superannuation entitlements

When this section applies

(1) This section applies when, in order to calculate a person's FIF income or loss, it is necessary to calculate the market value of a person's

entitlement under a life insurance policy or as a beneficiary under a superannuation scheme.

Life insurance policy value

(2) The market value of an entitlement to benefit under a life insurance policy is equal to its surrender value.

Superannuation scheme entitlement value

(3) The market value at any time of a person's entitlement to benefit under a superannuation scheme is equal to the total of costs incurred up to that time by the person (or on their behalf) on acquiring the entitlement if—

(a) it is not reasonably practicable to work out the actual market value; and

(b) they have not derived any material gain from the entitlement up to that time.

Origin:	(1) CG 23(9). (2) CG 23(9). (3) CG 23(9).
Defined terms:	derived, FIF income, life insurance policy, loss, market value, person, superannuation scheme.
Comment:	Current section CG 23 (9) is limited to apply only for certain purposes in the FIF rules, but it seems logical that it should apply more broadly.

EI 59 Non-market transactions in FIF interests

Section GD 14 (Attributing interests in FIFs (foreign investment funds)) applies to acquisitions and dispositions of attributing interests in FIFs when the comparative value method or the deemed rate of return method is used.

Origin:	CG 23(5), (6).
Defined terms:	attributing interest, comparative value method, deemed rate of return method, FIF.
Comment:	Draft section GD 14 is in the consequential amendments in volume 3.

Commissioner's default assessment power

EI 60 Commissioner's default assessment power

When this section applies

(1) This section applies if—

(a) a person has failed to disclose their control interest or income interest in a CFC or attributing interest in a FIF, under section 61 of the Tax Administration Act 1994; or

(b) a person has failed to disclose information regarding their control interest or income interest in a CFC or attributing interest in a FIF, under section 17 of the Tax Administration Act 1994; or

(c) a person cannot obtain enough information to calculate their attributed CFC income or loss, FIF income or loss or attributed repatriation for a period.

Commissioner's power

(2) The Commissioner may make an assessment of the amount of attributed CFC income or loss, FIF income or loss or attributed repatriation for the relevant period.

Examples of methods

(3) Without limiting the Commissioner's discretion, the assessment may be based on any of the following:

(a) the accounts of the CFC or FIF for the relevant period prepared for tax authorities, creditors, shareholders, or others:

(b) the application of a rate of presumed increase of 10% or more (compounding annually) to the CFC's or FIF's branch equivalent income calculated under section EI 21 for a previous period:

(c) the application of a rate of presumed increase of 10% or more (compounding annually) to the CFC's or FIF's accounting profits as shown in its accounts for a previous period:

(d) an imputed rate of return on the market value of the interest at the start of the period:

(e) the actual gains or losses of the person in the period from holding or disposing of the interest:

(f) the change in the market value of the interest over the period.

Origin:	(1) CG 25(1). (2) CG 25(1). (3) CG 25(1); CG 25(2).
Defined terms:	amount, attributed CFC income, attributed repatriation, attributing interest, branch equivalent income, CFC, Commissioner, control interest, FIF, FIF income, income interest, loss, person, shareholder.
Comment:	Does this provision materially add to the Commissioner's default assessment power under section 106 of the Tax Administration Act 1994? In other words, can it be omitted?