Taxation (Consequential Rate Alignment and Remedial Matters) Bill

Commentary on the Bill

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First published in July 2009 by the Policy Advice Division of Inland Revenue, PO Box 2198, Wellington 6140.

Taxation (Consequential Rate Alignment and Remedial Matters) Bill; Commentary on the Bill.
ISBN 978-0-478-27170-6

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Policy and policy-related consequentials

AMENDMENTS TO RESIDENT WITHHOLDING TAX RATES ON INTEREST

(Clauses 45, 51 and 60)

Summary of proposed amendments

Tax cuts have been recently made to the individual and company tax rates. The bill introduces new resident withholding tax (RWT) rates on interest income to align them with the new tax rates.

The default rate of RWT which applies when an individual does not choose an RWT rate with his or her financial institution will also be changed from 19.5% to 38%. The reason for changing the default RWT rate to the highest income tax rate is to encourage individuals to select the rate that is consistent with their marginal tax rate.

Interest payers will be required at least once a year to remind recipients of interest to ensure that they are on the RWT rate that is consistent with their marginal tax rate.

Application date

Alignment of RWT rates with current tax rates generally applies from 1 April 2010.

However, in relation to the default rate, the change to a 38% rate applies to accounts opened from 1 April 2010 and from 2011 for people with bank accounts as at 1 April 2010.

As a transitional measure, individuals with bank accounts at 1 April 2010 who are on the current RWT rate of 19.5% will have their rate automatically shifted up to 21% for one year from 1 April 2010. If they do not confirm the 21% rate or choose another rate, their RWT default rate will rise to 38% from 1 April 2011.

A 30% RWT rate on interest income paid to companies will be optional from 1 April 2010 and compulsory from 1 April 2011.

Key features

Schedule 1, part D of the Income Tax Act 2007 contains the new RWT rates for interest in relation to individuals and companies. The current and proposed rate structure for RWT on interest is shown in the table below:

<table>
<tr><th>Marginal income tax rates</th><th>Present RWT rates</th><th>Proposed RWT rates</th><th>Proposed application date</th></tr>
<tr><td>12.5%</td><td rowspan="2">19.5%</td><td>12.5%</td><td>1 April 2010</td></tr>
<tr><td>21%</td><td>21%</td><td>1 April 2010</td></tr>
<tr><td>30%</td><td rowspan="2">33%</td><td>30%</td><td>1 April 2011, but at payer’s option earlier from 1 April 2010</td></tr>
<tr><td>33%</td><td>33%</td><td>No change</td></tr>
<tr><td>38%</td><td>38% or 39%</td><td>38%</td><td>1 April 2010</td></tr>
</table>

Application of 12.5% rate

The 12.5% rate will be available to recipients of interest who provide their tax file number and who have a reasonable expectation for the year of election that their income will be in the range of $0 to $14,000. This approach attempts to ensure that the 12.5% rate is applied correctly and that taxpayers who elect 12.5% actively consider whether their RWT rate is consistent with their personal tax rate.

Default RWT rate

Schedule 1, part D, table 2 and new section RE 12(6) contain the provisions relating to shifting the default rate to 38%.

The default rate will be set at 38%, the highest personal tax rate. It will apply from 1 April 2010 for individuals who open new bank accounts from that date and who do not choose an RWT rate with their bank or other financial institution.

As a transitional measure, individuals with bank accounts as at 1 April 2010 who are on the 19.5% tax rate, will have their rate changed to 21% from 1 April 2010. This is necessary to ensure consistency with the marginal tax rate structure in place since the recent personal tax changes, in which the 19.5% statutory tax rate was removed and a 21% rate was introduced. These individuals will have a year from 1 April 2010 to choose one of the other rates (12.5%, 33% or 38%) or confirm that 21% is the appropriate RWT rate with their bank. New section RE 12(6) specifies that any individuals remaining on the 21% rate after 31 March 2011 who have not chosen that rate with their financial institution will be moved to a 38% default rate after that date.

Non-declaration rate

The rate that applies when a recipient does not provide the interest payer with a tax file number will be lowered from 39% to 38% from 1 April 2010, to reflect the change in the highest tax rate.

Requirement that interest payers remind recipients to check their RWT rate

New section 26B of the Tax Administration Act 1994 provides that interest income payers must ask individual recipients their RWT rate, at least once a year as part of their normal correspondence, to ensure that their RWT rate is consistent with their personal tax rate.

RWT rate on interest income earned by companies

Section RE 12(5) provides for an optional 30% RWT rate to be available to payers of interest to companies for the 2010–11 income year. From 1 April 2011, that RWT rate will be mandatory. This will align the RWT rate on interest paid to companies with the company tax rate.

Background

RWT is a withholding tax based on the marginal tax rate of the recipient of interest income. Its purpose is to ensure that tax is paid at source on that income at a rate that closely approximates the recipient's actual tax liability. Compliance and administrative costs are therefore minimised as recipients are less likely to request a personal tax summary or file a return if tax is withheld at the correct rate.

Currently, if individual recipients of interest income provide a tax file number but do not choose an RWT rate, the default rate is 19.5% (formerly the lowest statutory tax rate). As a personal tax rate of 19.5% no longer exists, it is necessary to move these taxpayers to a new rate.

The reason for setting the default rate at 38% is to encourage individuals to consider what rate they should be taxed at and to choose the rate that is correct for them. An individual's compliance costs may be reduced if they choose a rate that is consistent with their personal tax rate, because they are less likely to be required to square up their tax obligations at the end of the year. Encouraging individuals to choose the correct rate also promotes the integrity of the tax system and reduces administrative costs for Inland Revenue, as fewer contacts with taxpayers are required.

Continuing the current approach of having the lowest tax rate as the default for RWT is not recommended, as the minimum statutory rate of 12.5% is considerably lower than the previous 19.5%. The majority of people using the default rate would have too little tax withheld, which would increase compliance and administrative costs. Additionally, there would be significant revenue implications.

AMENDMENTS TO TAX RATES ON PORTFOLIO INVESTMENT ENTITIES

(Clause 49)

Summary of proposed amendments

The bill introduces changes to the tax rates on portfolio investment entities (PIEs) so they align with the new personal tax rate structure that was enacted in 2008.

Currently, PIE tax rates are as follows:

Taxable income	Taxable + PIE income	PIE tax rate
$0 – $38,000	$0 – $60,000	19.5%
$38,001 +	Any	30%
Any	$60,001 and over	30%

These rates should be aligned with the new personal tax rates which are 12.5% for income $0 to $14,000, 21% for income $14,001 to $48,000, 33% for income $48,001 to $70,000, and 38% for income over $70,000. This is to ensure that investors are not disadvantaged if they invest in a PIE rather than investing directly. This is particularly important as the tax on PIEs is a final tax.

The PIE rates are capped at 30% so they align with the company tax rate of 30%. This alignment was necessary so that an investment in a PIE was not disadvantaged compared with an investment in, for example, an investment company that was not a PIE.

The proposed new rates from 1 April 2010 are as follows:

Taxable income	Taxable + PIE income	PIE tax rate
$0 – $14,000	$0 – $48,000	12.5%
$0 – $14,000	$48,001 – $70,000	21%
$14,001 – $48,000	$0 – $70,000	21%
$48,001 and over	Any	30%
Any	$70,001 and over	30%

Application date

The amendments will apply from 1 April 2010.

ALIGNMENT OF RETIREMENT SCHEME CONTRIBUTION TAX RATES

(Clauses 49(9), 51(2) and 61)

Summary of proposed amendments

Amendments are being made to align the retirement scheme contribution tax (RSCT) rates with the new personal tax rate structure from 1 April 2010.

Application date

The amendment applies from 1 April 2010.

Key features

The definition of "retirement scheme prescribed rate" in section YA 1 of the Income Tax Act 2007 will be replaced with the following:

- 0% if the person is a non-resident at the time and the contribution is non-resident passive income; or
- 12.5% if the person:
  - has, in either of the two income years immediately before the year in which the contribution is made, taxable income of $14,000 or less;
  - is a non-resident and the retirement scheme contributor is a Māori authority, and the distribution is $200 or less;
  - is a non-resident and the retirement scheme contributor is a Māori authority and the person supplies the Māori authority with a notice under section 28C of the Tax Administration Act 1994; or
- 21% if the person has, in either of the two income years immediately before the year in which the contribution is made, taxable income of $14,001 or more and less than or equal to $48,000; or
- 33% if the person has, in either of the two income years immediately before the year in which the contribution is made, taxable income of $48,001 or more and less than or equal to $70,000; or
- 38% in any other case.

The basic rates for RSCT in table 5 of schedule 1 will also be aligned with the new personal tax rate structure.

Section 28C of the Tax Administration Act 1994 currently requires a person who gives notice of a retirement scheme prescribed rate of less than 39% to include their Inland Revenue number in that notice. The bill replaces the 39% reference with 38%.

NEW SECONDARY TAX CODE

(Clauses 52(1), 58, 59 and 62(1))

Summary of proposed amendments

The bill amends the PAYE withholding tax rules to introduce a new 12.5% secondary tax code. The new code will be available for employees with secondary income who expect to earn under $14,000 per year. This brings the withholding rates on secondary employment income into line with the recent lowering of personal tax rates.

Application date

The changes will apply from 1 April 2010.

Key features

New section 24B(3)(bb) of the Tax Administration Act 1994 and schedule 2, part A, clause 8 of the Income Tax Act 2007 introduces the 12.5% secondary tax code. Employees may choose the "SB" code for secondary employment earnings if their annual income is not more than $14,000.

Section 24C of the Tax Administration Act 1994 is being amended to ensure that people who receive income-tested benefits can choose the 12.5% tax code for any employment income if that is their correct code, and to clarify that employees who receive an income-tested benefit can choose their correct secondary tax code for their employment income.

Background

Employees who receive secondary employment income (or those receiving income-tested benefits or student allowances who are also in employment) must choose a secondary tax code for their secondary source of employment income, based on the marginal tax rate they expect to be on for that year.

In 2008 the government introduced a new set of personal income tax rates. This new tax scale included a 12.5% rate for income of $14,000 and below. Currently, the lowest rate for withholding tax on secondary employment income is 21%. This means there is the potential for lower-income individuals to have excess tax withheld on their secondary income.

A new 12.5% code will be introduced to more accurately withhold tax on secondary income.

PERSONAL TAX SUMMARIES AUTOMATICALLY ISSUED

(Clauses 62(2), 63 and 64)

Summary of proposed amendments

The bill removes the current requirement for the Commissioner of Inland Revenue to issue personal tax summaries (PTSs). This will give Inland Revenue flexibility in selecting who PTSs should be issued to.

Application date

The amendments will apply from 1 April 2010.

Key features

Amendments to sections 33A(5), 80C and 80D of the Tax Administration Act 1994 give the Commissioner of Inland Revenue discretion over which groups of taxpayers PTSs should be issued to.

Background

Currently, Inland Revenue is required to issue PTSs to several categories of individual taxpayers. Current categories of taxpayers who automatically receive PTSs include those with over $200 of employment income withheld using certain tax codes. However, issuing PTSs may not be necessary for all of these groups, particularly when the correct amount of tax is likely to have been withheld during the year. Because issuing PTSs imposes compliance and administrative costs for taxpayers and Inland Revenue, legislative changes have been made to give Inland Revenue flexibility in selecting who PTSs should be issued to. Taxpayers will continue to be able to request a PTS from Inland Revenue.

TAX TREATMENT OF EXTRA PAYS

(Clauses 42, 43 and 52(2))

Summary of proposed amendments

The bill introduces a new 12.5% withholding tax rate for extra pays to align them with the new personal tax rate structure, and makes a remedial amendment to the extra pay rules to more accurately tax extra pays earned in a job where a secondary tax code is used.

Application date

The amendments will apply from 1 April 2010.

Key features

An amendment to section RD 17(2) and schedule 2, part B, table 1 introduces a new bottom rate of 12.5% for extra pays, to align with the new personal tax rate structure. It ensures that if a low-income earner receives a lump sum payment and their total annual income is $14,000 or less, they will be taxed correctly.

Extra pay in secondary jobs

New section RD 17(3) and (4) will more accurately tax extra pays earned in a job where a secondary tax code is used. It will result in people who receive an extra pay for their secondary income being taxed on that income at a rate which reflects their extra pay income, their secondary income and a proxy for their primary income.

Employee's option to choose rate

An amendment to section RD 10 allows an employee to choose a 21% rate for extra pays if they expect their taxable income to be no more than $48,000.

Background

Lump sum payments made to employees in relation to their employment are known as "extra pays". These are payments that are not related to overtime worked and are not regularly included in a pay period. They include bonuses, gratuities, back-pay and profit shares, redundancy payments and retiring allowances. Tax on extra pays is currently withheld at a flat rate of 21%, 33% or 38%. These rates are intended to reflect the employee's marginal tax rate.

In 2008 a new rate of 12.5% was introduced as the bottom personal tax rate. Before 1 April 2008, when the bottom personal tax rate was 15%, there was no corresponding rate for extra pays. Because the threshold at which the 21% rate applied was raised to $14,001 from 1 April 2009, a rate reflecting the lowest tax rate is necessary.

Another problem is the tax treatment of extra pays earned in secondary jobs. The current treatment withholds tax on extra pays earned in relation to a secondary job on the basis that the income earned on the secondary job is the person's total income. This can often result in insufficient tax being withheld.

An amendment to section RD 17 addresses this problem by requiring the deducting employer to approximate the person's primary income when calculating the deduction that is made on the extra pay. The approximation is equal to the income threshold at which the employee's secondary tax code starts to apply. For example, if an employee has chosen a secondary code of 21% the secondary employer assumes that the person has primary employment income of $14,001.

ELECTRONIC COMMUNICATIONS

(Clause 57)

Summary of proposed amendment

The bill contains an amendment that ensures that Inland Revenue can issue notices and other information electronically in a broader range of circumstances, and makes the tax administration rules for sending information electronically more consistent with the rules for sending information via post.

Application date

The amendment will apply from the date of enactment.

Key features

The amendment to section 14(7) of the Tax Administration Act 1994 replaces the current requirement that a person must consent to Inland Revenue communicating electronically, with a requirement that Inland Revenue can provide information electronically if there are no reasonable grounds to believe that the communication will not be received by the person.

Background

Currently, Inland Revenue issues many of its notices and other information to taxpayers by post.

As part of a long-term project, Inland Revenue intends to provide more information electronically. However, the current tax rules require a taxpayer's consent for Inland Revenue to provide a communication electronically (the consent can be implied or inferred). The requirement for consent is impractical in some circumstances and inconsistent with the tax administration rules applicable to sending notices via post.

PERMANENT FOREST SINK INITIATIVE AND FORESTERS

(Clauses 49, 54, 82 and 83)

Summary of proposed amendments

Amendments are being made to make it clear that expenses incurred by a person deriving Permanent Forest Sink Initiative (PSFI) emissions units are treated as forestry business expenses.

Application date

The amendments will apply from the 2005–06 income year.

Background

The PFSI is a climate change initiative under which a person who owns land that has been reforested, or which the person intends to reforest, can enter into a covenant with the government, and in exchange for meeting certain conditions, receive emission units.

The earning of these units may not always constitute a forestry business under the Income Tax Acts. Forestry businesses are entitled under the Act to more favourable tax treatment than other businesses. Since PFSI foresters should receive the same treatment as foresters who carry on a forestry business, the amendment defines "forestry business" in section YA 1 of the Income Tax Act 2007 to include PFSI activities.

Section OB 1 of the Income Tax Act 2004 is also correspondingly amended.

TAX RECOVERY ARRANGEMENTS

(Clause 56 and 68)

Summary of proposed amendment

The bill introduces changes to the Tax Administration Act 1994 so New Zealand can meet its treaty obligations to provide collection assistance to certain countries for amounts of unpaid tax before the time limit for objection rights has expired. This amendment will resolve an inconsistency between New Zealand's treaty obligations and the wording of part 10A of the Tax Administration Act 1994, which currently prohibits the Commissioner from providing collection assistance over unpaid tax until the time limit for objection rights has expired.

Application date

The amendment will apply from the date of enactment.

Key features

The proposed amendments repeal the definition of "contested tax" in part 10A of the Tax Administration Act 1994 and replace it with a definition of "uncontested tax". The new definition of "uncontested tax" under section 173B clarifies the circumstances in which New Zealand can provide collection assistance under a tax recovery arrangement.

Background

Part 10A of the Tax Administration Act 1994 authorises entering into a collection assistance arrangement. It also sets limits on the collection assistance that New Zealand can provide. Specifically, part 10A prohibits the Commissioner of Inland Revenue from providing collection assistance in relation to an amount of unpaid tax if the time limit for objection rights has not expired. This is inconsistent with Article 4(2) of the Netherlands Tax Recovery Convention, which generally imposes an obligation on the requested State to collect unpaid taxes unless the tax assessment is actually subject to an objection.

Part 10A was enacted with the specific purpose of authorising the entering into of the Netherlands Tax Recovery Convention. Part 10A was framed with a view to also contemplate future collection assistance arrangements with other countries. Similar arrangements have now also been concluded with Australia, Poland and the United Kingdom.

TIMING OF ALLOCATION OF BENEFICIARY INCOME

(Clause 18)

Summary of proposed amendment

The bill removes a timing problem for tax agents who administer trusts, in particular, to allow them more time to allocate beneficiary income. Currently, beneficiary income must be allocated within an arbitrary six months of a trust's balance date. This creates undue pressure for tax agents at a time when clients' business tax requirements must also be met.

Application date

The amendment will apply for income derived in the 2009–10 income year.

Background

Under current tax law trustees must allocate beneficiary income within six months of the trust's balance date. However, this does not fit well with tax agents' work schedules as frequently they have to give priority to trust accounts to ensure the six-months rule is met. This can conflict with the more commercial requirements of tax agents' clients.

Section HC 6(1) is being amended to allow the income allocation to be made in the longer of the following periods:

- six months after balance date; or
- the shorter of:
  - the time in which the tax return is due; or
  - the time it is filed.

Also, subsections HC 6(3) and (4) concerning which year the beneficiary returns the income have been combined and their application is clarified.

GST TREATMENT OF WASTE DISPOSAL LEVY PAYMENT

(Clause 71)

Summary of proposed amendment

An amendment is being made to clarify the tax treatment of the waste disposal levy which was introduced on 1 July 2009, as part of the Waste Minimisation Act 2008. The amendment specifies the treatment of payments of this levy as consideration for a supply of services in furtherance of a taxable activity which are subject to goods and services tax (GST).

Application date

The amendment will apply retrospectively from 1 July 2009 to align with the date on which the levy applies.

Key features

The amendment made to the Goods and Services Tax Act 1985 clarifies that the three central payments made in relation to the waste disposal levy are consideration for a supply of services made in the course or furtherance of a taxable activity and those supplies are therefore subject to GST. These payments will give rise to input tax credits when they are made in the course or furtherance of a taxable activity. The three payments are:

- payment of the levy from the user of a waste disposal facility to the operator of that waste disposal facility;
- payment of the levy from the waste disposal facility operator to the Secretary for the Ministry of the Environment, represented by the levy collector; and
- payment made from the Secretary for the Ministry of the Environment to funding recipients or territorial authorities and for other payments described in section 30 of the Waste Minimisation Act 2008.

Background

The activities of public and local authorities are included within the scope of New Zealand's GST rules to ensure that consumers of goods and services supplied by the public sector on a commercial basis (in competition with the private sector) are neither advantaged nor disadvantaged by their choice of supplier.

It also avoids the complexities experienced in other jurisdictions:

- in determining whether the activities undertaken by the public sector are commercial or non-commercial; and

- provides a basis for apportioning GST charged and input tax deductions between the two activities.

For these reasons most levies (for example, road user charges and fire service levies) are subject to GST.

CORRECTION OF MINOR ERRORS IN SUBSEQUENT RETURNS

(Clause 66)

Summary of proposed amendment

The amendment clarifies the Commissioner's discretion to allow taxpayers who have made minor errors in a return (involving $500 or less in tax) to correct them in a subsequent return. The amendment is aimed at reducing compliance costs and the taxpayer's exposure to use-of-money interest and penalties.

Application date

The amendment will apply from the day after the bill receives Royal assent.

Key features

New section 113A of the Tax Administration Act 1994 gives the Commissioner the discretion to allow taxpayers to correct minor errors made in income tax, fringe benefit tax or goods and services tax returns in the next subsequent return after discovering the error(s).

A minor error is defined as an error (or errors) that was caused by a clear mistake, simple oversight, or mistaken understanding on the taxpayer's part, and for a single return, causes a total reduction in the resulting assessment of $500 or less. For this purpose, errors the taxpayer may have made for income tax, fringe benefit tax or goods and services tax are treated separately.

In these circumstances the Commissioner may allow the person to correct the error(s) in the next income tax, fringe benefit tax or goods and services tax return that is due after discovery of the error.

Background

Taxpayers are required to correctly determine the amount of tax payable under tax laws. If an amount is not correctly calculated or not paid on time, penalties can apply. Use-of-money interest also generally applies if the correct amount of tax is not paid when due.

Currently, for GST returns, registered persons are sometimes able to correct minor errors in a subsequent return-period. For other tax types, however, errors are generally required to be corrected in the returns in which they arose. This involves (in addition to the penalty and interest implications noted above) further compliance costs for the taxpayer.

By giving the Commissioner the discretion to allow taxpayers to correct minor errors in previous returns by including them in current returns, taxpayers and their agents will have a greater level of comfort in making changes. This will also reduce the number of interactions taxpayers need to have with Inland Revenue.

The amendment is largely aimed at helping to reduce tax compliance costs for small and medium-sized enterprises and individuals, although it will apply to taxpayers generally. It was first outlined in the government discussion document, *Reducing tax compliance costs for small and medium-sized enterprises*, released in December 2007.

Remedial matters

COST OF TIMBER

(Clauses 11, 49, 77 and 81)

Summary of proposed amendment

Changes are being introduced to part of the forestry rules consequent to the introduction of new generally accepted accounting principles (IFRS or International Financial Reporting Standards GAAP) which values growing trees at value rather than cost.

Application date

The amendment will apply from taxpayers' 2007–08 income year, or an earlier year if they were an early adopter of GAAP.

Background

The main purpose of section DP 11 of the Income Tax Act 2007 (section DP 10 of the Income Tax Act 2004) was to allow a deduction of certain forestry expenditure that might not otherwise be deductible. It also quantifies and times this deduction. Given the newer revenue account property rules, arguably its main purpose falls away. However, it still allows some amounts to be deducted that otherwise might not be deductible. Also it points into the relevant Part E timing rules when the amounts are deductible. However, it is linked to the accounting treatment of expenditure that should be capitalised as part of the "cost of bush" under GAAP.

The section has been amended to reflect the introduction of IFRS GAAP which values biological assets, such as growing trees, at value, not cost. Thus GAAP is not now referred to.

For clarity, section DP 11(4) of the Income Tax Act 2007 (section DP 10(4) of the Income Tax Act 2004) makes it clear that if restoration expenditure is dealt with under section DB 46 of the Income Tax Act 2007 (section DB 37 of the Income Tax Act 2004), it is not deductible under this section.

ATTRIBUTION RULE AND COMPANY INTERMEDIARIES

(Clause 16)

Summary of proposed amendments

Changes are being introduced to facilitate amendments enacted in 2007 regarding the attribution rule and the new 30% company tax rate.

Application date

The amendment will apply from the 2008–09 income year, the date of the company tax rate change.

Background

The attribution rule is an anti-avoidance rule that aims to prevent employees using an intermediary (usually a company or a trust) to avoid paying income tax at the top individual marginal rate. When the rule applies, the income of the intermediary is attributed to the individual who provided the services.

To prevent double taxation where the company is an intermediary, it receives deemed imputation credits.

The Income Tax Act 2007 allows certain companies which are not qualifying companies (QCs) to use the QC fully imputed/exempt qualifying company income distribution mechanism. This was to prevent double taxation that could arise with the attribution rule when the new 30% company tax rate was introduced.

However, the deemed imputation credits were not cancelled at that time. New section GB 27(5) solves this problem by cancelling the deemed credits immediately before they are distributed.

RESEARCH AND DEVELOPMENT AND TWO GAAPS

(Clauses 8, 9, 49, 52, 74, 75, 78 and 79)

Summary of proposed amendments

The bill introduces changes to the research and development (R&D) rules to allow for the fact that New Zealand currently operates two forms of generally accepted accounting principles (GAAP).

Application date

The amendments are backdated to the introduction of the International Financial Reporting Standards (IFRS) GAAP amendments – generally from the 2007–08 income year.

Background

Certain R&D deductions that are determined with reference to specific GAAP rules are allowed.

In 2007 the Tax Acts were modified to allow for the introduction of IFRS GAAP. For R&D this involved changing the references into the specific GAAP R&D rules.

At this stage it was thought that old GAAP would not continue to be used. However, for compliance cost reasons a decision was subsequently made that certain non-large or non-reporting entities could, at least temporarily, continue to use old GAAP. Therefore, the old GAAP R&D deductions need to be reinstated for taxation purposes.

Amendments to clauses 8 (amending section DB 34, Income Tax Act 2007) and 74 (amending section DB 26, Income Tax Act 2004) allow for this. The other clauses amend “associated persons” definitions.

THE DEFINITION OF "ASSOCIATED PERSONS" IN THE GST ACT FOR CHARITABLE BODIES

(Clause 70)

Summary of proposed amendment

An amendment is being made to the definition of "associated persons" in the Goods and Services Act 1985 to ensure that donations made to and by charitable and non-profit bodies are not subject to GST if the donor or donee is associated with the charitable or non-profit body.

Application date

The amendment will apply from the date of enactment.

Key features

Two amendments to section 2A of the GST Act are proposed:

- Section 2A(1)(f) associates a trustee and a beneficiary of a trust, unless the trustee is a charitable or non-profit body and the supply is made while carrying out the charitable purpose. The charitable and non-profit body exemption does not, however, extend to situations where the beneficiary is the charitable or non-profit body. The amendment will ensure that a trustee and a beneficiary of a trust are not associated persons if the beneficiary is a charitable or non-profit body.
- Section 2A(1)(h) associates a trustee of a trust and a trustee of another trust if the same person is a settlor of both trusts. There is no exclusion for charitable and non-profit bodies. The amendment will ensure that two trustees with a common settlor are not associated when one of those trusts is a charitable or non-profit body.

Background

GST charged on a supply of goods and services is calculated on the value of that supply, which is normally the consideration paid for the goods and services in question. There is, therefore, a risk that two associated persons may agree to enter into a transaction with each other in order to reduce the GST charged on the transaction when the consideration charged for the goods or services is either reduced or is nil. To counter this the GST Act provides a special valuation rule so that the consideration for a supply is treated as being the open market value of the supply when the supply is made between associated persons. However, the special valuation rule applies to any supply made for nil value, including the donated goods and services made by or to a charitable or non-profit body.

Section 2A of the GST Act contains the definition of "associated persons". A number of concerns have been identified with the current wording of the definition as it applies to charitable and non-profit bodies. The combined effect of the current wording of the "associated persons" definition and the special valuation rule noted above is that certain donations made to and by charitable and non-profit bodies could be subject to GST on the full open market value because they were made by or to an associated person.

Activities of charitable and non-profit bodies do not involve the supply of goods and services in exchange for payment in the course or furtherance of a taxable activity but are performed in carrying out the principal purposes for which such bodies are established (such as collecting donations or making donations). As a result, these activities should be treated as being outside the GST base and should not be subject to GST, even if activities involve transacting with associated persons. The proposed amendments to the definition of "associated persons" are intended to achieve this policy outcome.

BINDING RULINGS ON THE INCOME TAX ACT 2004

(Clause 65)

Summary of proposed amendment

Currently Inland Revenue cannot make a binding ruling for the period before the Income Tax Act 2007 came into effect if the application for the ruling is received by Inland Revenue after the commencement of the 2008–09 income year.

An amendment is being made to the Tax Administration Act 1994 to allow Inland Revenue to make binding rulings for this period.

Application date

The amendment will apply from the date of enactment.

MAKING THE REQUIREMENT TO PAY TAX IN DISPUTE A NON-DISPUTABLE DECISION

(Clause 67)

Summary of proposed amendment

The bill introduces an amendment making the exercise of the Commissioner's discretion to require payment of all tax in dispute a non-disputable decision.

Currently, a decision of the Commissioner to require full payment is a disputable decision. This was not intended. Therefore, section 138I(2B) will be added to section 138E, which sets out the provisions where there is no right of challenge, making the exercise of the discretion a non-disputable decision.

Application date

The amendment will apply from the date of enactment.

Background

Section 138I of the Tax Administration Act 1994 concerns payment of tax in dispute. Since 2003 the Commissioner has been able to require that a disputant pay all of the tax in dispute if the Commissioner considers that there is a significant risk that the tax in dispute will not be paid should the disputant's challenge not be successful (section 138I(2B)). This discretion is exercised in exceptional circumstances only, for example, where the Commissioner considers there is a flight risk.

It was not intended that a decision of the Commissioner to require full payment should be a disputable decision.

RESIDENT WITHHOLDING TAX AND INTERMEDIARIES OR AGENTS

(Clauses 44, 48 and 81)

Summary of proposed amendments

The amendments clarify the application of the tax credit and RWT rules for intermediaries or agents acting on behalf of New Zealand residents with foreign investment fund (FIF) interests.

Application date

The amendment applies to distributions made via intermediaries or agents from the beginning of the 2008–09 income year.

The amendment providing for a resident withholding tax credit to be available to a New Zealand resident applies from the beginning of the 2008–09 income year for the 2007 Act and from the beginning of the 2005–06 income year for the 2004 Act.

Key features

Sections RE 10B of the 2007 Income Tax Act and NF 2E of the 2004 Act apply if:

- an intermediary or agent receives a distribution from a FIF on behalf of a New Zealand resident; and
- section CD 36 applies to treat the distribution as not being a dividend; and
- the intermediary has withheld an amount from the distribution under the resident withholding tax rules.

Section RE 10B provides that for the purposes of the tax credit rules and for refunds of tax, the amount withheld is treated as resident withholding tax. This amendment is necessary because a consequence of section CD 36 applying to treat the distribution from the FIF as not being a dividend, is that a tax credit may not be available for the amount withheld.

In addition, a minor amendment to section RM 8 clarifies that an intermediary or agent who has determined that the resident owning the FIF interest has exceeded the $50,000 threshold for FIF interests and has applied for a refund of the amount withheld may also request the Commissioner to apply the refund against other tax types.

Background

A submission was made on the Taxation (International Taxation, Life Insurance, and Remedial Matters) Bill 2008 that no tax credit is available for a New Zealand resident when an intermediary or agent for the resident:

- received distributions from attributing interests in foreign investment funds owned by the New Zealand resident, and
- withheld an amount on account of resident withholding tax in the belief the resident was covered by the $50,000 threshold rule in section CQ 5(1)(d) or (e); and
- subsequently on-paid the dividend to the New Zealand resident.

Under the 2007 Act, provided the New Zealand resident owning the FIF interests falls within the threshold of $50,000, the dividend received by the intermediary or agent on behalf of the New Zealand resident is resident passive income of the resident. In these circumstances, the intermediary or agent is normally required to account for resident withholding tax on the dividend.

However, if the New Zealand resident exceeds the threshold of $50,000, the resident is no longer exempt from most FIF income calculation methods. Consequently, section CD 36 provides that all distributions paid during the income year from the resident's attributing interests are not dividends for income tax purposes. Instead, the resident must determine their income from all of the person's FIF interests using one of the FIF income calculation methods.

There are likely to be a number of cases where the intermediary or agent will not necessarily be aware of the change in circumstances of the New Zealand resident at the time the withholding is made. In these circumstances, the intermediary or agent will normally withhold an amount on account of resident withholding tax from the actual dividend on-paid to the New Zealand resident.

These amendments clarify that, in these circumstances, if an intermediary withholds an amount on account of RWT, the amount withheld is treated as RWT for the purposes of the tax credit rules and the RWT rules. This amendment applies retrospectively to the beginning of both the 2007 Act and the 2004 Act.

In addition, section RM 8 of the 2007 Act is amended to address a potential unintended change in law from the 2004 Act. Section NF 7(5) was intended to permit an intermediary or agent who applied for a refund of an amount withheld on account of RWT to also request that the Commissioner apply the refund against other tax obligations of the payer. This amendment to section RM 8 applies from the date the 2007 Act came into force.

GIFTS OF MONEY MADE BY COMPANIES

(Clause 72)

Summary of proposed amendment

An amendment restores the position under the Income Tax Act 2004 in relation to deductions for gifts of money made by companies. The amendment ensures that the removal of the 5 percent limit on deductions for charitable donations made by companies applies from the 2008–09 income year.

Application date

The amendment applies from 19 December 2007.

Rewrite Advisory Panel recommendations

Consequential to the rewrite of income tax legislation, the following remedial amendments are being made to correct identified unintended changes in law or to clarify the law arising from recommendations made by the Rewrite Advisory Panel.

Capital gain amounts
(Clauses 5 and 73)

The amendment ensures that a capital gain amount can be passed through a corporate chain and distributed to shareholders of a company (who are not associated persons) as a capital gain amount on the liquidation of the company.

This amendment applies from the beginning of the 2008–09 income year (2007 Act) and the 2005–06 income year (2004 Act).

Dividend under the dividend stripping rules
(Clause 53)

The amendment clarifies that section GB 1 contains an intended change in law.

This amendment applies from the beginning of the 2008–09 income year (2007 Act). However, a savings provision applies to certain taxpayers so they are not adversely affected for decisions made on the basis of the unclarified view.

Branch equivalent income of a CFC carrying on the business of life insurance
(Clauses 14 and 78)

The amendment restores the 1994 Act position that the branch equivalent income for a CFC carrying on the business of life insurance is the part of the accounting profit or loss that is actuarially determined to relate to the shareholders of CFC.

This amendment applies from the beginning of the 2005–06 income year.

Meaning of settlor
(Clauses 19, 20 and 53)

The amendment clarifies that the rewrite of the definition of "settlor" contains an intended legislative change.

The amendment applies from the beginning of the 2008–09 income year. However, a savings provision applies to certain taxpayers and to some binding rulings to ensure taxpayers are not aversely affected for decisions made on the basis of the unclarified view.

Date of debit for loss of continuity – imputation rules
(Clauses 41 and 53)

The amendment clarifies that an intended legislative change has been made in the imputation rules, FDP rules and the branch equivalent tax account rules in relation to a loss of shareholding continuity.

The amendment applies from the beginning of the 2008–09 income year. However, a savings provision in section OZ 18 applies to certain taxpayers to ensure they are not adversely affected for decisions made on the basis of the unclarified view.

Natural resources and non-resident withholding tax
(Clause 47)

The amendment provides that the non-resident withholding tax rules do not apply to income in the nature of rents derived from land to which both section CC 1(2)(a) to (d) and section CC 9 applies. The amendment does not apply to consideration derived from the exploitation of (including the right to exploit), or the removal of (including the right to remove), any plants or naturally occurring materials or minerals from the land.

The amendment applies from the beginning of the 2008–09 income year.

Nominal settlements
(Clause 50)

This amendment clarifies that a person making a nominal settlement is treated as a nominee of the person in relation to the nominal settlement.

The amendment applies from the beginning of the 2008–09 income year.

Other remedial measures arising from the rewrite of income tax legislation

Election to use simplified method for determining a person's income interest in a FIF
(Clauses 15 and 79)

The amendment restores the requirement that a person must have held their income interest in a FIF for at least 12 months before they may elect to apply the simplified method for determining their income interest in the FIF.

The amendment is retrospective to the beginning of the 2005–06 income year. However, a savings provision applies to certain taxpayers to ensure they are not adversely affected for decisions made on the basis of the unclarified view.

Family scheme income
(Clause 38)

This amendment ensures that the Family Scheme Income is correctly adjusted for depreciation recovery income relating to depreciation deductions allowed in the 2002–03 or earlier income years.