Fisher & Paykel Healthcare Corporation Limited
Paykel Building
15 Maurice Paykel Place, East Tamaki
P O Box 14 348, Panmure
Auckland, New Zealand
Telephone: +64 9 574 0100
Facsimile: +64 9 574 0158
Website: www.fphcare.com

10 November 2016

Addressing hybrid mismatch arrangements
C/- David Carrigan, Acting Deputy Commissioner
Policy and Strategy
Inland Revenue Department
PO Box 2198
WELLINGTON 6140

Dear David

ADDRESSING HYBRID MISMATCH ARRANGEMENTS

We are writing to submit on the discussion document *"Addressing hybrid mismatch arrangements"* (the "Discussion Document"). We are members of the Corporate Taxpayers Group (CTG), who is also making a submission on this topic; however, given the importance of this matter we are making a separate submission in respect of submission point 8 – foreign branches.

We have previously advocated for and continue to be supportive of an active income exemption for foreign branches. Extending the active income exemption for branches was on the Government's Tax Policy Work Programme from 2010-2015 and was first referred to in the December 2006 International Tax Review discussion document. Although we understand why this reform was deferred, we consider the deferral to be disappointing and are pleased it is again being considered.

Regardless of whether the proposals to adopt the deductible hybrid payment responses proceed, a foreign active branch exemption should be enacted. As we have noted previously (in submissions to Inland Revenue policy officials and the Minister of Revenue) we believe the treatment of branches should, where possible, mirror the treatment of CFCs. In our view, businesses that operate as subsidiaries or branches are no different from an operational view point and should be treated as such.

We understand the connection between the active income exemption for branches and BEPS, and that the introduction of such an exemption would restrict the flow through of foreign losses against the New Zealand tax base. We believe it is more appropriate that reforms should be shaped as an extension of the active income exemption for CFCs (which already contains robust base protection measures). This would result in a comprehensive international tax framework that is equally applicable to branches and subsidiaries and ensure tax consequences do not distort business structure decisions. We also consider this critical to reducing the current compliance costs that arise when operating offshore through a foreign branch.

The extension of the active income exemption to branches would materially assist in eliminating the potential for inappropriate outcomes without detailed hybrid rules applying to foreign branch structures. This should reduce compliance costs that will likely arise as a result of the implementation of the proposals.

We understand that there are currently concerns around the timing of when the hybrid mismatch proposals should be adopted and the consensus appears to be that New Zealand should align timing with other relevant jurisdictions. We understand that adoption in Australia is currently being delayed

until the treatment of regulatory capital is considered further and this may delay implementation in New Zealand. Implementation of the active foreign branch exemption in New Zealand in the meantime could demonstrate that policy officials are actively taking steps to address BEPS concerns. Australia has had an active foreign branch exemption for some time and therefore there is no reason to delay reform to New Zealand's foreign branch rules.

We set out below the background on our business and we reiterate and expand on the comments above.

Background

Fisher & Paykel Healthcare Corporation Limited (and its branches and subsidiaries) is a leading designer, manufacturer and marketer of products and systems for use in respiratory care, acute care and the treatment of obstructive sleep apnea.

Our headquarters, research and development facilities and New Zealand manufacturing operations are located in East Tamaki, Auckland, with products sold in over 120 countries worldwide. We currently have close to 30 offshore entities (subsidiaries and branches), nearly all of which sell and distribute our products. Principal sales and distribution sites are located in the United States, the United Kingdom, Europe, Asia and Australia.

Our competitors are predominantly headquartered in the United States or Europe with operations in multiple jurisdictions. We are therefore typically competing against companies which have enjoyed the benefits of an active income exemption for subsidiaries and branches or something similar for some time.

Comments

Extending the active income exemption to foreign branches **with minimal further delay** would, in our view:

- help ensure that the momentum generated from the CFC/FIF reforms is not lost;
- materially reduce the compliance costs that New Zealand based multi-nationals incur in relation to foreign branch activities;
- improve New Zealand's international competitiveness with our major trading partners and competitors, including Australia;
- with respect to our business, represent New Zealand taking another step forward in levelling the playing field between ourselves and our foreign headquartered competitors.
- would demonstrate that policy officials are actively taking steps to address BEPS concerns.

As noted previously, we believe the treatment of branches should, where possible, mirror the treatment of CFCs. The OECD/G20 Base Erosion and Profit Shifting (BEPS) Project *Designing Effective Controlled Foreign Company Rules* ACTION 3: 2015 Final Report contemplates the application of CFC rules focussing on the attribution of income that gives rise to BEPS concerns (i.e. passive income) to foreign branches. The application of an active income exemption to branches is consistent with the recommendations in the report. We support the view that the relevant focus area is on the type of income rather than the type of entity and believe the most coherent legislative solution is to extend the current CFC treatment.

The introduction of the proposals contained in the Discussion Document would restrict the flow through of foreign losses against the New Zealand tax base and there are concerns about the impact on taxpayers of removing this flow through of losses from foreign branches (especially for small start-up type businesses). While this is generally only a timing benefit as future income arising from the foreign branch should also be recognised in New Zealand, it is possible for taxpayers to structure their arrangements such that this is not necessarily the case. Therefore, in some situations tax consequences are currently distorting business structure choices.

The potential issues with use of foreign branch losses against New Zealand income are detailed in the Discussion Document. The general principle is that foreign branch losses should only be able to be used against foreign branch income which is also taxable in New Zealand (referred to as "dual inclusion income") unless there is no ability to otherwise utilise the losses in the foreign jurisdiction. The

extension of the active income exemption to branches would materially assist in eliminating the potential for inappropriate outcomes without the need for the application of detailed hybrid rules.

If the proposals in the Discussion Document do not proceed we consider the active branch exemption should still be enacted. If there is concern about denying the flow through of losses from foreign branches (especially for small start-up type businesses), we suggest introducing an elective regime under which taxpayers could choose to make an irrevocable election into an active exemption regime for foreign branches. This would provide the necessary compliance relief and alignment with CFC/FIF treatment for taxpayers that make the election, but would retain the status quo for those that do not make the election. We see merit in an elective regime with appropriate base maintenance protection measures to prevent the potential opportunities that exist for inappropriate outcomes even within the current regime.

Finally, we note that we are a New Zealand business employing a large and growing number of New Zealanders. We want to continue to be based in New Zealand and pay the majority of our tax here. We encourage officials to ensure we and other New Zealand headquartered businesses have access to international tax legislation we deserve to assist (or at the least not inhibit) this intention and our competitive position.

We appreciate the opportunity to provide a submission on the paper and we would be happy to be contacted to discuss any points raised in this submission. In the first instance, please contact Rachael Bull.

Yours faithfully

Tony Barclay
Chief Financial Officer

Direct Tel: 9(2)(a)
Direct Fax: +64 9 574 0176
Email: tony.barclay@fphcare.co.nz

Rachael Bull
Head of Group Tax

Direct Tel: 9(2)(a)
Direct Fax: +64 9 574 0176
Email: rachael.bull@fphcare.co.nz