



*Tax facts &
figures*
New Zealand

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Liability to income tax

Imposition of income tax

The worldwide income of New Zealand residents, whether they are companies, individuals or other entities, is generally subject to New Zealand income tax. Non-residents are subject to tax on New Zealand sourced income, although a double tax agreement may reduce the tax liability.

A New Zealand resident's taxable income is computed as follows:

	\$
Gross income from all sources	100
Less: Exempt income	(10)
	90
Less: Allowable deductions	(50)
Net income	40
Less: Losses	(20)
Taxable income	20

Income tax is calculated using a graduated scale (for individuals) or a flat tax rate (for companies and trusts). Refer Personal income tax rates, page 12 and Company tax rate, page 17.

A taxpayer's residual income tax (RIT) liability is determined after deducting any domestic tax credits, foreign tax credits and dividend imputation credits to which they are entitled from the income tax payable on their taxable income.

Gross income

Gross income includes business income, employment income, rents, interest, dividends, royalties, allowances, bonuses, some annuities and pensions, attributed income and services-related payments.

Exempt income

Exempt income includes:

- alimony or maintenance received from a spouse or former spouse
- dividends received by New Zealand resident companies from foreign companies or from resident companies with 100% common ownership
- scholarships and bursaries except student allowances
- income earned by a non-resident in respect of personal services performed for, or on behalf of, a person who is not resident in New Zealand, in the course of a visit not exceeding 92 days, subject to certain provisos, including the imposition of tax in the recipient's country of residence (refer Non-resident contractor's tax, page 43)
- annuities paid under insurance policies offered or entered into in New Zealand by a life insurer or offered or entered into outside New Zealand by a New Zealand resident life insurer
- distributions from superannuation schemes registered under the Superannuation Schemes Act 1989
- distributions from a superannuation scheme that is registered under the KiwiSaver Act 2006
- money won on horse races and dog races.

Allowable deductions

Allowable deductions include depreciation and expenditure incurred in deriving gross income or in carrying on a business for the purpose of deriving gross income subject to specific limitations (eg limitations for capital and private expenditure).

Income year

The income year generally consists of the 12-month period ending 31 March.

When a taxpayer has a balance date other than 31 March, they can elect, with the consent of the Commissioner of Inland Revenue (the Commissioner), to file returns to their annual balance date. In such cases income derived during the year ending with the annual balance date is treated as being derived during the year ending on the nearest 31 March.

In this publication, references to the 2011/2012 or 2012 income year are references to the income year ending on 31 March 2012.

Taxation of individuals

Residence

An individual is a New Zealand tax resident if he or she:

- has a permanent place of abode in New Zealand, even if they also have a permanent place of abode overseas; or
- is personally present in New Zealand for more than 183 days in total in any 12-month period; or
- is absent from New Zealand in the service of the New Zealand Government.

A New Zealand resident will cease to be a tax resident only if he or she:

- is absent from New Zealand for more than 325 days in any 12-month period; and
- at no time during that period maintains a permanent place of abode in New Zealand.

A permanent place of abode is determined with reference to the extent and strength of the attachments and relationships that the person has established and maintained in New Zealand.

Tie-breaker provisions often apply to relieve individuals ordinarily resident in a country with which New Zealand has a double tax agreement from any potential double taxation (refer Double tax agreements, page 37).

However, individuals ordinarily resident in non-treaty countries, who take up a permanent place of abode, or who are personally present, in New Zealand for more than 183 days in any 12-month period, are subject to tax on their worldwide income during the period of deemed residence. In such cases, the residence test applies from the first day of the individual's presence in New Zealand, even when that pre-dates the individual's move to New Zealand. The individual may be able to offset credits for tax paid in foreign jurisdictions against tax payable in New Zealand.

Non-resident individuals working in New Zealand are subject to the same marginal rates of tax as residents.

A temporary (48-month) exemption from income tax applies to the foreign income (other than employment income or income from the supply of services) of individuals who become New Zealand tax residents on or after 1 April 2006. Returning residents who have been non-resident for 10 years or more are entitled to the same exemption. New migrants who became tax residents before 1 April 2006 are not eligible for the exemption.

Gross income

Each individual is separately assessed. There is no joint assessment of the income of spouses. The gross income of a taxpayer includes salary and wages, employment-related allowances, bonuses, other emoluments, expenditure by an employer on account of an employee, interest, dividends (including attached imputation credits and withholding tax), certain trust distributions, partnership income, shareholder salary, rents, services-related payments (such as exit inducement and restraint of trade payments), attributed personal services income and income from self-employment.

Employee remuneration

The gross income of an employee includes:

- all cash receipts in respect of the employment or service of the employee
- expenditure incurred by the employee but paid for by the employer. However, cash allowances which are intended merely to reimburse the employee for work-related expenditure incurred on behalf of the employer are generally not treated as part of the employee's gross income
- the value of any benefit an employee receives from any board and lodging or the use of any house or quarters, or an allowance paid in lieu of board, lodging, housing or quarters, provided in respect of a position of employment
- the value of the benefit gained by an employee from an employee share option or share purchase scheme
- certain payments for loss of earnings payable under various accident insurance statutes
- retiring allowances
- director's fees
- redundancy payments
- restraint of trade and exit inducement payments.

Fringe benefits

Fringe benefit tax (FBT) is payable by employers on non-cash or in-kind benefits provided to employees (refer Fringe benefit tax, page 53).

Payments from superannuation funds

Payments from a New Zealand superannuation fund, whether in the form of an annuity, lump sum or pension, are not taxable in the hands of the recipient.

KiwiSaver

KiwiSaver is a voluntary savings scheme available to individuals who are either New Zealand citizens or permanent residents.

Since 1 April 2009 the default contribution rate for new employees has been 2%. The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill proposes to raise the minimum employee and employer contribution rates to 3% of an employee's gross salary or wages (refer New developments – KiwiSaver, page 63).

A tax credit is available for a member's contributions to KiwiSaver (capped at \$521.43 per year).

Employers must contribute to KiwiSaver for those of their employees who are KiwiSaver members. Compulsory employer contributions are capped at 2% of an employee's gross salary or wages.

Employer contributions to KiwiSaver (or other qualifying registered superannuation schemes) were previously exempt from employer superannuation contribution tax (ESCT), capped at the 2% compulsory employer contribution. This exemption is removed from 1 April 2012. From 1 April 2012, the ESCT default deduction rate (a flat rate of 33%) is also removed and ESCT must be calculated at a rate equivalent to an employee's marginal tax rate.

Subject to certain narrow exceptions, KiwiSaver contributions are locked in until the later of the member becoming entitled to New Zealand Superannuation (currently at age 65) or for five years.

Generally KiwiSaver schemes are 'portfolio investment entities' (PIEs) and can take advantage of the favourable tax rules for PIEs (refer Portfolio investment entities, page 28).

Trans-Tasman superannuation portability

The Taxation (Annual Rates, Trans-Tasman Savings Portability, KiwiSaver, and Remedial Matters) Act 2010 introduced significant changes to the treatment of retirement savings transferred between Australia and New Zealand.

New Zealanders with retirement savings from certain Australian superannuation funds will be able to transfer their funds into KiwiSaver when they return home permanently. Similarly, KiwiSaver members who are moving to Australia will be able to transfer all of their savings in KiwiSaver, including Government contributions and any member tax credits, to an Australian complying superannuation scheme.

Portability will be voluntary for retirement savings providers and members. The portability arrangement will come into force when both countries have given it legal effect.

Overseas investments

Investments in foreign companies or other foreign entities may be taxable even if the taxpayer does not receive any dividends or other income. In some circumstances attributed income can arise if the taxpayer has an investment in a controlled foreign company or a foreign investment fund (refer Controlled foreign companies, page 38, and Foreign investment funds, page 39).

Individuals who benefit from certain pensions or annuities provided by foreign entities may be exempt from the foreign investment fund rules but may be subject to tax on distributions on a receipts basis.

An individual's interest in an Australian superannuation scheme is exempt from the foreign investment fund rules when the scheme is subject to preservation rules that lock in the benefit until the member reaches retirement age.

Individuals who maintain foreign currency bank accounts, loans and mortgages are liable to tax on exchange rate fluctuations (refer The financial arrangements rules, page 29).

Overseas pension plans

The taxation of such plans (with respect to the entitlement balance, the transfer amount, and the withdrawal amount) is under review. We expect a discussion paper to be released in mid 2012.

Deductions

The only deductions that employees may claim against employment income are professional fees for preparing their income tax returns and certain premiums for loss of earnings insurance.

Individuals in business are entitled to a wide range of deductions (refer Deductions and valuation issues, page 29).

Personal income tax rates

The basic rates of tax (before allowing for credits and excluding ACC earner premiums) that apply to individuals for the 2011/2012 and subsequent income years are:

Taxable income \$	Tax rate %	Cumulative tax \$
0 – 14,000	10.5	1,470
14,001 – 48,000	17.5	7,420
48,001 – 70,000	30.0	14,020
over 70,000	33.0	

Individual tax tables

The table below sets out tax payable on taxable income (before deducting rebates and credits and excluding ACC levies) based on the above tax rates:

Taxable income \$ 2011/2012 and subsequent income years	Tax \$
5,000	525
10,000	1,050
20,000	2,520
30,000	4,270
40,000	6,020
50,000	8,020
60,000	11,020
100,000	23,920
150,000	40,420
200,000	56,920

Tax credits

Credits reduce income tax otherwise payable. For the 2011/2012 and subsequent income years individual taxpayers can claim a number of credits including:

	Maximum credit \$
Child taxpayer credit	245.70 (Note 1)
Housekeeper credit	310.00 (Note 2)
Transitional tax allowance	611.52 (Note 3)
Redundancy tax credit	3,600.00 (Note 4)
Independent earner tax credit	520.00 (Note 5)

Note 1. Available to children under 15 years of age and to children under the age of 19 still at school. Claim the lower of \$245.70 or 10.5% of net income (excluding interest and dividends subject to resident withholding tax).

Note 2. Claim the lower of \$310 or 33% of qualifying payments for the year. This credit generally applies to childcare costs incurred by working parents and the costs of employing a housekeeper incurred by a taxpayer who is disabled or whose partner is disabled.

Note 3. Available to full-time earners (working 20 hours or more per week). Claim \$611.52 and deduct 16.8 cents for every dollar of net income over \$6,240. The credit is not available if a person's net income exceeds \$9,880. If the taxpayer works for fewer than 52 weeks of the year, the credit reduces further.

Note 4. Individuals are entitled to a redundancy payment credit of 6 cents per dollar of redundancy payment, capped at \$3,600 for redundancy payments paid before 1 October 2011.

Note 5. Individuals whose annual income is between \$24,000 and \$44,000 and who meet certain requirements qualify for an independent earner tax credit of \$520.00. For eligible individuals who earn over \$44,000 the annual entitlement decreases by 13 cents for each additional dollar earned up to \$48,000, at which point the credit is fully abated.

An individual is able to claim a 33.3% tax credit for charitable donations up to their taxable income. If an employer offers 'payroll giving', the employee can receive the tax credit immediately as a reduction in PAYE paid.

Individual taxpayers may also be eligible for the following tax credits:

- 'Working for Families' tax credits, a form of income support for families
- imputation credits
- credits for tax paid on overseas income subject to tax in New Zealand.

PAYE (Pay As You Earn)

Employers are required to withhold tax from employee remuneration paid and must account to the Commissioner for the amounts withheld. This procedure is known as 'pay as you earn' (PAYE). The tax withheld is offset against the employee's income tax liability.

Schedular payments

Withholding tax deductions are generally required from schedular payments.

These include:

Type of schedular payment	Withholding tax rate (%)
• Directors' fees	33
• Honoraria (payments to members of Councils, boards, committees, societies, clubs, etc)	33
• Salespersons' commissions	20
• Primary production contractors	15
• Contractors in the television, video and film industries	20
• Non-resident contractors (including companies) where payments exceed \$15,000 in a 12 month period	15

To apply the above rates the payer must receive a withholding declaration from the taxpayer. Where this is not received the above rates increase by 15 cents in every \$1. The tax withheld is an interim tax credited against the taxpayer's ultimate income tax liability.

Resident withholding tax (RWT)

Subject to certain exemptions, interest and dividend income is subject to RWT unless the recipient holds a valid certificate of exemption.

Interest income

The RWT rates on interest income for individuals are 10.5%, 17.5%, 30% and 33%. The applicable rate of RWT on interest income depends on whether the recipient has supplied an IRD number to the payer and whether an election has been made to apply a certain rate to a particular source of interest income. The recipient can elect which of the four RWT rates applies if they have supplied their IRD number. If the recipient has supplied their IRD number but no election has been made, the default RWT rate is 33% on all new bank accounts opened after 31 March 2010 and 17.5% for all existing bank accounts. The non-declaration rate (ie when the IRD number is not supplied) is 33%.

Dividend income

The withholding tax rate on dividend income is 33%.

Following the reduction in the company tax rate from 33% to 30%, the imputation credit ratio changed to 30/70 when New Zealand resident companies pay dividends to shareholders. When a dividend is fully imputed at 30%, RWT is payable at 3%.

With the reduction in the corporate tax rate to 28% with effect from the 2011/2012 income year, the imputation credit ratio changed to 28/72 when New Zealand resident companies pay dividends to shareholders. When a dividend is fully imputed at 28%, RWT is payable at 5% (refer Dividend imputation – Attaching credits to dividends (page 20).

Dividend imputation credits

New Zealand resident individual shareholders receiving dividends from New Zealand and certain Australian companies must:

- include net dividends and taxable bonus issues received (including bonus shares in lieu) in gross income;
- add imputation and resident withholding tax credits to income (refer Dividend imputation, page 19);
- calculate their total tax; and
- deduct imputation credits and resident withholding tax from tax payable.

Excess imputation credits that exceed a natural person shareholder's tax liability are carried forward.

Restrictive covenant and exit inducement payments

Restrictive covenants and exit inducement payments are taxable.

Attributed personal services income

Individuals subject to the 33% tax rate cannot divert personal services income into entities taxed at lower rates. The rules attribute the personal services income of any interposed entity (after deduction of expenses) to the individual who provides the services. The rules apply when:

- the entity and the individual service provider are associated;
- the entity derives 80% or more of its service income from one recipient (or associates);
- 80% or more of the entity's service income relates to services provided by one service provider (or relatives);
- the service provider's net income in the year in which an attribution would occur exceeds \$70,000; and
- substantial business assets do not form a necessary part of the process of deriving the interposed entity's income from services.

Income without tax deducted at source

Provisional tax (refer Provisional tax, page 47) is levied on income (excluding income from which tax has been deducted at source at the correct rate) to ensure, as far as possible, that all income is taxed in the year in which it is earned.

Tax returns

The requirement to file a tax return has been removed for certain individuals (refer Returns, page 46). The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill proposes changes to the requirements for returns filing and record keeping (refer New developments – returns filing requirements, page 62).

Taxation of companies

Residence

A company is deemed to be resident in New Zealand if:

- it is incorporated in New Zealand; or
- it has its head office in New Zealand; or
- it has its centre of management in New Zealand; or
- directors exercise control of the company in New Zealand, whether or not the directors' decision-making is confined to New Zealand.

For companies resident in a country with which New Zealand has a double tax agreement (refer Double tax agreements, page 37), tie-breaker provisions often apply to relieve any potential double taxation.

Company tax rate

All companies, whether resident or non-resident, are taxed at the same rate. This tax rate also applies to certain savings vehicles, including unit trusts, widely held superannuation funds, some group investment funds and life insurance shareholder income. The top tax rate for portfolio investment entities (PIEs) is also capped at the same rate as the corporate tax rate.

The company tax rate reduced from 30% to 28% with effect from the 2011/2012 income year. This resulted in the imputation credit ratio changing to 28/72 (refer Dividend imputation, page 19).

Taxable income

Generally, taxable income is determined after adjustments to accounting income for:

- depreciation (refer Depreciation, page 31);
- trading stock (refer Trading stock, page 36);
- financial arrangements (refer The financial arrangements rules, page 29);
- legal and other expenses on capital account;
- entertainment expenses (refer Entertainment expenditure, page 33);
- leases; and
- provisions and reserves.

Dividends

Dividend income generally forms part of gross income. Dividend income derived from a New Zealand resident company by another New Zealand resident company is subject to tax in the hands of the recipient, except where paid between 100% commonly owned companies (prior to 29 August 2011 the companies also needed to share a common balance date).

The definition of dividend for tax purposes extends beyond company law concepts, catching virtually every benefit provided by a company to shareholders (or associates thereof). The definition excludes certain benefits provided to downstream associate companies or between sister companies in a wholly owned group of companies.

Interest

Interest incurred by most companies is deductible, subject to the thin capitalisation regime (refer Thin capitalisation, page 44).

Losses

In calculating taxable income, losses from prior years may be carried forward and deducted when, in broad terms, at least 49% continuity of ultimate ownership has been maintained.

Specific regimes

Special rules apply in calculating taxable income for businesses such as life insurance companies, group investment funds, non-resident insurers, ship-owners, mining, forestry and some film rental companies.

Grouping of losses

Companies are assessed for income tax separately from other companies included in the same group (exception - refer Consolidation, page 20).

To share losses between group companies, certain requirements must be satisfied:

- 49% continuity of ownership in the loss company; and
- 66% commonality of ownership in the group companies.

Continuity and commonality are measured based on a shareholder's minimum voting and market value interests held at a particular time or over a particular period, tracing through intermediate shareholders. Special rules apply to ensure that a subsidiary does not forfeit losses when the shares in that subsidiary are transferred to the shareholders of its parent company, providing there is no change in the underlying economic ownership because of the 'spinout'.

Group companies may share losses by the profit company making a subvention payment to the loss company or by simple loss offset election. The payment or offset is deductible to the profit company and taxable to the loss company.

Losses cannot be transferred to natural person shareholders except historically in the case of loss attributing qualifying companies. Legislation enacted in December 2010 removed the ability for loss attributing qualifying companies to attribute losses to their shareholders with effect from the 2011/2012 income year. That legislation also introduced a new 'look-through company' vehicle (refer Qualifying companies, page 21 and Look-through companies, page 22).

Dividend imputation

The dividend imputation system applies to all dividends paid by New Zealand resident companies. It allows tax paid by resident companies to flow through to shareholders in the form of credits attaching to dividends paid and taxable bonus issues (including bonus shares in lieu).

Resident individual shareholders in receipt of dividends with credits attached may offset these credits against their personal tax liability. Resident corporate shareholders in receipt of dividends with credits attached may offset credits against their tax liability except where the dividend is exempt from income tax.

Specific rules allow trans-Tasman groups of companies to attach both imputation credits (representing New Zealand tax paid) and franking credits (representing Australian tax paid) to dividends paid to shareholders. Under these rules, dividends paid by an Australian resident company with a New Zealand resident subsidiary can have imputation credits attached that the New Zealand resident shareholders can offset against their New Zealand tax liability. In the same manner, a New Zealand resident company with an Australian resident subsidiary can attach franking credits to dividends. Australian resident shareholders can offset the franking credits against their Australian tax liability.

Imputation credit account (ICA)

Generally, New Zealand resident companies must maintain an ICA, a memorandum account which records tax paid and the allocation of credits to shareholders. A company must maintain an ICA on a 31 March year-end basis irrespective of its balance date.

Credits arise in the ICA in a number of ways, including from:

- payments of income tax including payments made into a tax pooling account
- imputation credits attached to dividends received
- tax on amounts attributed under the attributed personal services income rules.

Debits arise in the ICA in a number of ways, including from:

- the allocation of credits to dividends
- refunds of income tax including refunds from a tax pooling account
- penalties (allocation debit) when a company fails to meet the allocation requirements
- a breach of shareholder continuity requirements
- an adjustment to a company's ICA for the tax effect of an amount attributed under the attributed personal services income rules.

Company refunds of income tax are limited to the credit balance in the ICA at the previous 31 March, or in certain circumstances, the credit balance in the ICA most recently filed with Inland Revenue. Inland Revenue will not refund the balance of any tax refund in excess of the ICA credit balance but the taxpayer can offset it against future tax obligations.

When an ICA has a debit balance at 31 March the company must pay income tax equal to the debit balance plus a 10% imputation penalty tax by the following 20 June. The income tax can be offset against future income tax obligations. The imputation penalty tax cannot be offset.

Attaching credits to dividends

When a company pays a dividend it may, at its own election, attach an imputation credit to the dividend. The maximum amount of credits that a company can attach to the dividend is calculated using the following ratio:

$$\frac{a}{1 - a}$$

Where a = resident company tax rate for the income year in which the dividend is paid.

Therefore, in the 2011/2012 imputation year, the ratio cannot generally exceed \$28 of credits for every \$72 of net dividend paid. This gives a gross dividend of \$100. There are rules to prevent companies streaming credits selectively to particular dividends or to particular shareholders.

Prior to the 2011/2012 income tax rate reduction, the ratio could not generally exceed \$30 of credits for every \$70 of net dividend. Under a transitional rule, the 30/70 ratio is available until 31 March 2013 for the distribution of profits taxed at 30%.

Dividend statements

If a company pays a dividend with an imputation credit attached, it must provide each shareholder with a shareholder dividend statement showing the amount of credit and other prescribed information. The company must also produce a company dividend statement showing the prescribed information and provide this to the Commissioner.

Consolidation

A 100% commonly owned group of companies has the option of consolidating and being recognised as one entity. Consolidation allows it to file a single consolidated tax return. Generally, relevant elections must be made prior to the start of the income year in which consolidation is sought.

Consolidation offers tax relief on intra-group transactions, including asset transfers, dividend and interest flows, and it simplifies tax filing and provisional tax calculations.

However, it requires:

- all companies within the consolidated group to be jointly and severally liable for the group's income tax liabilities; and
- increased tax record keeping (eg individual and group ICAs, loss carry forward records and property transfer records).

Amalgamation

Companies are able to amalgamate under the Companies Act 1993. An amalgamation occurs when two or more companies amalgamate and continue as one company, which can be one of the amalgamating companies or a new company. On amalgamation, the old companies cease to exist.

For tax purposes, when the amalgamation is a 'qualifying amalgamation' certain concessionary tax rules apply.

Qualifying companies

Prior to 1 April 2011, certain closely held companies could elect to become qualifying companies.

The qualifying company regime is closed for new entrants with effect from the 2011/2012 income year. Existing qualifying companies at 31 March 2011 have the option of continuing to be taxed as qualifying companies or to transition into 'look through companies' (refer Look through companies, page 22), a partnership or a sole trader or to elect out of the qualifying company rules and into the tax rules that apply to companies.

For tax purposes, qualifying companies are treated in a similar manner to partnerships.

This allows for the:

- single taxation of revenue earnings by exempting distributions made to New Zealand resident shareholders to the extent that those distributions are not fully imputed.
- tax-free distribution of capital gains without requiring a winding-up.
- preservation of shareholders' limited liability, except in relation to income tax.

Prior to 1 April 2011, a company could have elected to become a qualifying company if:

- it was not a unit trust nor a foreign company;
- it did not derive more than \$10,000 in foreign sourced non-dividend income;
- it was effectively owned by 5 or fewer natural persons; and
- corporate shareholders were also qualifying companies.

In addition when the company's shares all carried equal rights, shareholders could elect for it to be a loss attributing qualifying company (LAQC). Historically, shareholders in LAQCs have been able to deduct losses at their marginal tax rate with profits being taxed in the company at the company tax rate. The ability to attribute losses to shareholders has been removed with effect from 1 April 2011.

Look-through companies

Legislation effective from 1 April 2011 introduced a new entity called a 'look-through company' (LTC). An LTC is a flow-through vehicle with all profits and losses being allocated to the shareholders in proportion to their shareholding on an annual basis, subject to the application of a loss limitation rule. An LTC will be treated as a company for company law purposes.

Existing QCs and LAQCs can elect to be subject to the LTC rules without incurring a tax cost up to 31 March 2013.

Life insurance and general insurance companies

From 1 July 2010, income from a life insurer's business is separated into shareholder income (income earned by the equity owners in the company) and policyholder income (income earned for policyholders from life insurance products).

Shareholder base income is taxed at the corporate tax rate in a similar manner to other businesses. The portfolio investment entity (PIE) rules apply to policyholder income. This means that the tax treatment of those who save through life insurance policies is consistent with that which applies to other investment products.

Transitional rules apply to life insurance policies existing when the new regime commenced (1 July 2010).

General insurance companies are taxed as other companies but are subject to industry specific rules. New Zealand resident general insurance companies are subject to tax on offshore branch insurance business. Offshore reinsurance premiums are deductible and any recoveries made under that reinsurance are taxable.

An effective 2.8% tax is imposed on insurance premiums and reinsurance premiums paid offshore.

Mineral and petroleum mining

Mineral and petroleum mining companies are generally taxed in the same way as other companies but are subject to industry specific rules. Specific provisions apply for the deductibility of development and exploration expenditure.

Income derived in New Zealand by a non-resident company from the operation of seismic survey vessels and offshore drilling rigs is exempt from income tax. The exemption applies to income earned between 1 January 2004 and 31 December 2014. Despite the exemption, non-residents may still have other New Zealand tax obligations such as goods and services tax and employee taxes.

Unit trusts

Unit trusts are deemed to be companies for tax purposes. Accordingly, the corporate tax model applies to distributions of income and redemption gains paid by the unit trust to unit holders. For these transactions, the unit holder is deemed to derive dividends, which are usually accompanied by imputation credits representing tax paid by the unit trust.

A concession exists for qualifying (widely held) unit trusts. For shareholder continuity purposes unit holders in qualifying unit trusts are treated as a notional single person. This ensures the unit trust is able to carry forward losses and imputation credits.

Other entities

Partnerships

Legislation enacted in 2008 codified the tax rules that apply to general partnerships and introduced new rules for limited partnerships. The limited partnership rules effectively replace the earlier special partnership regime. There are two types of partnership – general partnership and limited partnership.

General partnerships

A general partnership is a flow-through entity for New Zealand income tax purposes (ie partners are attributed profits or losses directly). The partnership is required to file a tax return but this is for information purposes only. The individual partners include their share of the profit or loss of the partnership in their individual tax returns and the individual partners pay tax at their marginal tax rates.

Limited partnerships

A limited partnership is also a flow-through entity but has separate legal status from the individual partners in the partnership (in the same way as a company has a separate legal status from its shareholders).

A limited partnership must have at least one general partner and one limited partner who is not the same person. Any 'person' can be a partner in a limited partnership including a natural person, a company, a partnership and another unincorporated body. General partners manage the business and are jointly and severally liable for all the debts and liabilities of the partnership. Limited partners are usually passive investors whose liability is limited to their capital contribution to the partnership.

Limited partners can only participate in restricted decision making in respect of the business otherwise they risk losing their limited status. Loss limitation rules ensure that losses claimed by a limited partner reflect the level of that partner's economic loss (ie any tax loss claimed by a limited partner is limited to the amount that the limited partner has at risk in the partnership).

There are anti-streaming provisions in the legislation for both general and limited partnerships to ensure that partners are allocated income, tax credits, rebates, gains, expenditure and losses in the same proportion as each partner's share in the income of the partnership.

Joint ventures

A joint venture itself is not subject to income tax and is not required to file an income tax return. However, it is treated as a separate entity for GST purposes and must file GST returns on its own account. Participants in joint ventures include their individual share of the proceeds from the sale of the output or production in their own tax returns and claim a deduction for their individual share of the revenue expenditure. A joint venture may elect into the partnership regime for income tax purposes.

Trusts

There are three classes of trust:

Complying trusts

A complying trust is one that has satisfied the New Zealand tax liabilities on its worldwide trustee income since settlement. New Zealand family trusts established by a New Zealand resident settlor with New Zealand resident trustees generally fall within this class.

Trustee income is subject to tax at 33%. With the exception of beneficiary income, all other distributions from a complying trust are tax-free in the hands of the beneficiary. Beneficiary income consists of income derived by a trustee that vests absolutely in the interest of a beneficiary during the same income year in which the trustee derived it, or within six months after the end of that income year. Tax agents who administer trusts can make beneficiary distributions up to the later of:

- (i) 6 months after balance date; and
- (ii) the earlier of the time in which the tax return is due or filed.

Beneficiary income is taxable in the hands of the beneficiary at their marginal tax rate, except when the 'minor beneficiary' rule applies (refer Trust distributions to minor beneficiaries, page 27).

Foreign trusts

A trust is a foreign trust if none of its settlors has been resident in New Zealand between the later of 17 December 1987 and the date of first settlement of the trust, and the date the trustees make a taxable distribution. This class includes offshore trusts with New Zealand resident beneficiaries.

A trust ceases to be a foreign trust if it makes any distribution after a settlor becomes a New Zealand resident, or if a New Zealand resident makes a settlement on the trust.

Only New Zealand sourced trustee income is subject to tax. Beneficiaries are subject to tax at their respective marginal tax rates on all distributions received from the trust except:

- distributions of certain property settled on the trust;
- distributions of certain capital profits/gains;
- income derived by a trustee prior to 1 April 1988; and
- distributions after 1 April 2001 subject to the minor beneficiary rule.

New Zealand resident trustees of foreign trusts are subject to information disclosure and record keeping requirements. They are required to provide certain information to Inland Revenue and to keep financial records for the trusts in New Zealand. If a New Zealand resident trustee knowingly fails to disclose information or to keep or provide the requisite records to Inland Revenue the trustee will be subject to sanctions, including prosecution. In certain circumstances, the foreign trust will be subject to New Zealand tax on its worldwide income until the information is provided to Inland Revenue.

Non-complying trusts

A non-complying trust is any trust that is neither a complying trust nor a foreign trust. This class generally covers a trust with New Zealand resident settlors, non-resident trustees and actual or potential New Zealand resident beneficiaries.

It also includes a trust where the trustee income has been liable to full New Zealand tax but the trustees have not paid the tax.

Generally, trustee income comprises only New Zealand sourced income, except for years in which a settlor is resident in New Zealand, in which case worldwide income is taxable. Beneficiary income is taxed in the hands of the beneficiary at their marginal rate (subject to the minor beneficiary rule) while most other distributions are taxed at 45%.

The wide definition of a settlor includes a person who:

- makes a settlement of property to or for the benefit of a trust for less than market value; or
- makes property available, including a loan or guarantee, to a trust for less than market value; or
- provides services to or for the benefit of the trust for less than market value; or
- acquires or obtains the use of property of the trust for greater than market value.

For trusts with New Zealand settlors, who are not permanently New Zealand resident, there is effectively a choice between being a complying or non-complying trust. Only New Zealand sourced income of a non-complying trust is subject to tax, except for years in which the settlor is resident in New Zealand. However, most distributions to New Zealand resident beneficiaries are subject to tax at 45%. If the trust elects to be a complying trust, the trustees are subject to tax on their worldwide income, with a credit for foreign tax paid. The rules for complying trusts then apply to distributions of such income.

Trust distributions to minor beneficiaries

In certain circumstances trust distributions to minor beneficiaries (ie beneficiaries younger than 16) are subject to tax at the trustee tax rate of 33% rather than the beneficiary's marginal tax rate. This is the 'minor beneficiary' rule. This income is subject to tax as trustee income and is not included in the minor beneficiary's gross income.

The minor beneficiary rule applies to distributions to minors when the income is derived from property settled on the trust by the minor's relative or guardian, or their associates. The intent of the regime is to limit the tax benefits of using trusts to split income, on the basis that the income distributed to many minor beneficiaries is, in substance, 'family income' rather than income of the minor beneficiary.

Superannuation funds

Superannuation funds are taxed as complying trusts. However, investment income is generally subject to tax at a rate of 28%. Member contributions received by the superannuation fund are tax-free and no deduction is allowable for any benefit paid out of the scheme.

As the fund pays the tax, all distributions, whether provided in lump sum or pension form, are tax-free in the hands of the members.

Employer contributions to superannuation funds are deductible but are subject to employer superannuation contribution tax (ESCT). The ESCT rates are 10.5% on contributions made on behalf of employees earning no more than \$16,800, 17.5% on earnings between \$16,801 and \$57,600, 30% on earnings between \$57,601 and \$84,000 and 33% thereafter. ESCT is calculated using the sum of an employee's gross salary or wages and their employer superannuation contributions.

The rules applying to foreign superannuation schemes are more complex. Employer contributions are liable to FBT but both the contribution and the FBT are deductible to the employer. While investment income of the scheme may be taxed as trustee income, any increase in the value of an entitlement of any member may also be taxable under the foreign investment fund regime (refer Foreign investment funds, page 39). Distributions may be taxable in the hands of the recipient.

KiwiSaver

KiwiSaver is a Government-initiated savings scheme open to all individuals (with minor exceptions) who are New Zealand citizens or permanent residents. From 1 April 2012 employer contributions to employees' KiwiSaver schemes are no longer exempt from ESCT (refer to New developments – employer superannuation contribution tax, page 63). KiwiSaver schemes are likely to be 'portfolio investment entities' (PIEs) and take advantage of the tax rules for Portfolio investment entities, page 28.

Fund withdrawal tax (FWT)

Fund withdrawal tax was repealed with effect from 1 April 2011.

Portfolio investment entities (PIEs)

A collective investment vehicle (eg a managed fund) that meets the eligibility requirements and elects to become a portfolio investment entity (PIE) is subject to the PIE rules.

A PIE is taxed on its investment income at the elected prescribed investor rates (PIRs) of its investors. The prescribed investor rates are 0%, 10.5%, 17.5% and a capped rate of 28%. Eligibility for any given rate depends on a number of factors including the investor's PIE and non-PIE income earned in the previous two years. PIE tax deducted at a rate greater than 0% is a final tax for an individual who selects a rate to which they are entitled.

The rules align the tax treatment of investments made through PIEs with the tax treatment of direct investments made by individuals. PIEs are not taxable on capital gains and losses they make on New Zealand shares and certain Australian shares.

Charities and donee organisations

Income derived by an organisation that has a charitable purpose is exempt from income tax. Until 30 June 2012 charities must register with the Charities Commission to be eligible for tax-exempt status. From 1 July 2012 the Charities Commission will be disestablished and charities must register with the Department of Internal Affairs to be eligible for tax-exempt status.

Charitable organisations are eligible for various tax benefits, including exemptions:

- from income tax for non-business income.
- for business income derived by, or in support of, charities.

Charities can also be eligible for donee status. Inland Revenue administers donee status.

An individual can claim a tax credit equal to 1/3 of all donations made to organisations with donee status, up to the donor's taxable income. Some employers offer 'payroll giving' where the employee can receive the tax credit immediately as a reduction of PAYE paid (see Tax credits, page 13). Companies and Maori authorities may deduct all donations to organisations with donee status, up to the donor's net income (calculated prior to taking the deduction for the donations).

Deductions and valuation issues

The financial arrangements rules

Financial arrangements

The taxation of debt and debt instruments is governed by the financial arrangements rules.

The financial arrangements rules are specific timing rules which determine the recognition (for income tax purposes) of income and expenditure in relation to financial arrangements. The financial arrangements rules apply only to New Zealand residents or entities carrying on business in New Zealand. The effect of the rules is to require the spreading of income and expenditure under a financial arrangement and to eliminate the capital/revenue distinction for financial arrangements.

Financial arrangements are broadly defined to include any arrangements whereby a person obtains money or money's worth in consideration for a promise to provide money or money's worth at some future time. Common examples of financial arrangements are loans, bonds, government stock, mortgages, bank accounts, swaps and options.

Exceptions include interests in group investment funds, partnerships and joint ventures, certain private or domestic agreements, warranties, employment contracts, life insurance policies, superannuation schemes and hire purchase agreements. A hire purchase agreement is treated as two separate transactions – a sale of goods and a loan. The loan is subject to the financial arrangements rules.

Special rules apply to financial arrangements entered into before 20 May 1999.

Cash basis persons

When the total value of the person's income and expenditure from the financial arrangement does not exceed \$100,000 in an income year or the total value of financial arrangements at any time does not exceed \$1 million, income or expenditure on financial arrangements held by that person can be returned on a cash basis. However, a person is not a cash basis person if the difference between the income which would be deemed to be derived on an accruals basis and the income derived on a cash basis exceeds \$40,000.

Non cash basis persons

International Financial Reporting Standards (IFRS) users

Taxpayers who use IFRS to prepare their financial statements may use spreading methods that rely on accounting practice. There are a number of compulsory methods and elective methods for IFRS taxpayers. The application of the methods is both prescribed and limited, depending on the type of financial instrument held and subject to the taxpayer satisfying certain criteria. Elective methods include the expected value method and the modified fair value method, which assist in reducing exposure to volatility that might otherwise arise under IFRS fair value accounting for financial arrangements.

Non-IFRS users

Generally income and expenditure from financial arrangements is returned for tax purposes using the yield-to-maturity method. However, when the total value of all financial arrangements held at any time in the year does not exceed \$1.85 million the straight line method is acceptable. In certain circumstances the market valuation method can be used. When it is not possible to use any of these methods, income or expenditure from the financial arrangement may be returned on the basis of a determination made by the Commissioner. An alternative method may be adopted if it meets certain criteria.

Foreign exchange

Foreign exchange gains arising from financial arrangements denominated in a foreign currency (whether realised or unrealised, capital or revenue) are included as gross income. Foreign exchange losses (realised and unrealised) are deemed to be interest and, provided the losses meet the interest deductibility criteria, a tax deduction should be available. In some circumstances foreign exchange income or expenditure will be taxed based on the expected value of the financial arrangement. Any unexpected portion will be taxed upon realisation of the gain or loss.

Deferred settlements

Deferred settlements of real and other property can give rise to deemed interest in the sale price, resulting in gross income for the vendor and a potential interest deduction for the purchaser. However, private or domestic agreements with deferred settlements are an exception to the definition of financial arrangement, subject to certain conditions. Agreements must be entered into for a private or domestic purpose, and the monetary value of the settlement must be less than \$1 million if it relates to real property, or \$400,000 if it relates to any other property or services. Settlement must take place within 365 days of the agreement.

Base price adjustment

Upon maturity or disposal of a financial arrangement, a base price adjustment is performed to 'wash up' final amounts of income and expenditure. Discounts realised on redemption are taxable. The base price adjustment applies regardless of the calculation method used in prior periods and applies to both cash basis and non cash basis persons.

Interest deductibility

Interest incurred by most companies is automatically deductible subject to the thin capitalisation rules (refer Thin capitalisation, page 44).

The Taxation (Tax Administration and Remedial Matters) Act 2011 clarifies that use of money interest (UOMI) is deductible for both companies and individuals (refer Use of money interest, page 52). The amendment applies retrospectively from the 1997–98 income year (the start of the UOMI rules) for taxpayers who have claimed UOMI deductions in returns filed before the Act was introduced.

Depreciation

Taxpayers have the choice of using the diminishing value (DV) or straight line (SL) method of depreciation with a pooling option for assets with a cost or book value below \$2,000. Generally, annual deductions are calculated in accordance with the formula:

$$a \times b \times c / 12$$

where

a = the depreciation rate applying for the asset

b = the cost price (SL) or book value (DV) of the asset

c = the number of months (or part months) during the year in which the property was owned and used or available for use by the taxpayer

Depreciation rates (DV and SL equivalents) are determined by the Commissioner pursuant to a statutory formula which takes account of the expected economic life and residual value of assets. In special circumstances taxpayers may ask the Commissioner to prescribe a special depreciation rate.

The double declining balance (accelerated) method for depreciating plant and equipment was introduced in 2006. Under the double declining balance method equipment with an estimated useful life of 10 years results in DV depreciation deductions of 20% per annum ie double the straight line rate of 10% over the equipment's 10 year life. Buildings, certain motor vehicles, high residual value property, fixed life intangible property and property acquired prior to the introduction of the new rules cannot be depreciated under the double declining balance method.

The actual depreciation rate to be applied is dependent on the date of acquisition of the relevant asset by the taxpayer:

- assets acquired prior to 1 April 1993 – apply ‘old’ rates previously allowed by the Commissioner, plus a 25% loading for qualifying assets acquired on or after 16 December 1991
- assets acquired between 1 April 1993 and 31 March 1995 (or equivalent balance date) – choose between applying ‘old’ rates, inclusive of any loading, and ‘new’ economic rates
- assets acquired between 1 April 1995 and the end of the 2004/2005 income year apply ‘new’ economic rates plus a 20% loading for qualifying assets
- assets acquired in the 2005/2006 income year – choose between applying ‘new’ economic rates plus a 20% loading for qualifying assets and, in the case of plant and equipment, double declining balance rates plus a 20% loading for qualifying assets
- buildings acquired on or after 19 May 2005 must apply a 2% SL rate or equivalent 3% DV rate, with application to the 2005/2006 and subsequent income years
- assets acquired in the 2006/2007 and subsequent income years – apply double declining balance rates to plant and equipment (where applicable) plus a 20% loading for qualifying assets
- assets acquired after 20 May 2010 – do not use the 20% loading for qualifying assets (except when the decision to obtain the asset was made on or before 20 May 2010).

Buildings with an estimated useful life of 50 years or more are subject to a depreciation rate of 0% from the start of the 2011/2012 income year.

Assets costing up to \$500 may be expensed on acquisition rather than capitalised and depreciated provided certain criteria are met.

The classes of depreciable property include certain land improvements and some types of intangible property. Computer software must be depreciated.

Depreciation recovered is taxable in the year of sale. Taxpayers are not able to offset depreciation recovered against the cost of replacement assets.

Specific new rollover relief provisions have been introduced to provide relief from depreciation recovered for assets affected by the Canterbury earthquakes.

Entertainment expenditure

Generally 50% of entertainment expenditure is non-deductible for tax purposes.

The entertainment tax regime applies to specified types of entertainment, namely:

- corporate boxes
- holiday accommodation
- yachts and pleasure craft
- food or beverages
 - provided as part of the above; or
 - provided or consumed off the taxpayer's business premises; or
 - provided or consumed on the taxpayer's business premises, at a party or social function, or in an exclusive area of the premises reserved for employees of a certain level of seniority.

Exclusions from the entertainment regime include:

- food or beverages consumed while travelling on business, except where entertaining business contacts
- food or beverages consumed at a conference which lasts over four hours
- certain overtime meal allowances
- 'light meals' provided to employees while working
- entertainment at trade displays and other promotional activities
- entertainment enjoyed or consumed outside of New Zealand.

Legal expenditure

Businesses with \$10,000 or less of business-related legal expenditure can claim a full deduction in the year the expenditure is incurred, regardless of whether the expenditure is capital or revenue in nature.

Farming, agriculture and forestry expenditure

Provisions exist for the deduction of specified development expenditure against income derived from such ventures.

Farming and agriculture

Taxpayers engaging in farming or agricultural businesses in New Zealand may take an immediate deduction for the following classes of development expenditure (ordinarily classified as capital and accordingly non-deductible):

- destruction of weeds, plants or animal pests detrimental to the land
- clearing, destruction and removal of scrub, stumps and undergrowth
- repair of flood or erosion damage
- planting and maintaining trees for the purpose of preventing or combating erosion or for the purpose of providing shelter
- construction of fences for agricultural purposes, including rabbit-proofing of new or existing fences
- regrassing and fertilising of all kinds of pasture, provided the expenditure is not incurred in the course of a significant capital activity.

Development expenditure not eligible for immediate write-off is capitalised and depreciated together with similar development expenditure from earlier income years on a diminishing value basis. Depreciation rates generally range from 6% to 12%.

In addition to detailed records of direct capital expenditure, farmers are required to keep details of indirect costs incurred in relation to farm development, such as labour and motor vehicle expenses.

Forestry

Taxpayers engaging in a forestry business may take an immediate deduction for expenditure incurred in:

- planting and maintaining forests
- construction of temporary access tracks
- administration of the forestry business (ie interest, rates, insurance premiums and administrative overheads).

Forest land development expenditure not eligible for immediate write-off is capitalised and depreciated, together with similar development expenditure from earlier income years, on a diminishing value basis. Depreciation rates range from 6% to 24%.

Expenditure incurred in relation to the purchase of an existing forest must be capitalised to a 'cost of timber' account and is only deductible in the year the relevant timber is sold.

Livestock valuation options

'Specified livestock' (sheep, beef cattle, dairy cattle, deer, goats (meat and fibre), goats (dairy) and pigs) may be valued using one of four methods of valuation:

- national standard cost scheme
- the herd scheme
- cost, market value or replacement price
- self-assessed cost scheme.

Special valuation rules apply for bailed or leased livestock, non-specified livestock and bloodstock.

Motor vehicle deductions

Self-employed taxpayers using a motor vehicle partially for business and partially for other purposes are required to maintain either:

- complete and accurate records of the reasons for and distance of journeys undertaken for business purposes; or
- a motor vehicle logbook for a three month test period every three years to establish a business mileage pattern. When no records or logbooks are maintained, the tax deduction is limited to the lesser of the percentage of actual business use or 25% of the total operating expenditure and depreciation.

Research and development expenditure

Research expenditure (which does not include feasibility expenditure, such as costs incurred to perform initial research into starting a business) is always deductible.

Development expenditure is deductible until the product or process is clearly defined and the costs attributable to the product or process can be separately identified and measured. Development expenditure not immediately deductible must be analysed to determine whether a depreciable asset is created. When annual development expenditure is less than \$10,000 it is automatically deductible. For tax purposes the definitions of research and development expenditure mirror those in the relevant accounting standards. Special rules govern the deductibility of software development expenditure.

In certain circumstances companies are able to defer deductions for research and development expenditure to reduce tax losses which would otherwise be forfeited on the introduction of new equity investors. This rule removes a barrier to investment in research and development by allowing deductions for research and development expenditure (including depreciation) to be matched against income arising from that expenditure.

Businesses that met certain criteria were eligible for a 15% tax credit for qualifying research and development expenditure in the 2008/2009 income tax year. The 15% tax credit was repealed for later income tax years.

Trading stock

Trading stock may be valued at either cost or market selling value, if this is lower. Cost is determined by reference to generally accepted accounting principles. Market selling value must be demonstrated generally based on actual sales. Replacement price or discounted selling price may be used to approximate cost if these methods are used for financial reporting purposes. Shares which are trading stock must be valued at cost.

Business environmental expenditure

Taxpayers can deduct certain expenditure incurred in avoiding the discharge of contaminants and in remedying or mitigating the effect of such discharges. An 'environmental restoration account' is used to match site restoration expenditure against prior business income.

International

Double tax agreements (DTAs)

DTAs are designed to provide relief from double taxation and thereby to offer more certainty of tax treatment for people and entities carrying on business in foreign jurisdictions.

DTAs are bilateral and provide that only one country has priority taxing rights. When both countries impose tax, generally the taxpayer is allowed a credit against tax paid in the other country.

DTAs are in force between New Zealand and the following countries:

- Australia*
- Austria
- Belgium
- Canada*
- Chile*
- China
- Czech Republic
- Denmark
- Fiji
- Finland
- France
- Germany
- Hong Kong*
- India
- Indonesia
- Ireland
- Italy
- Japan
- Korea
- Malaysia
- Mexico*
- Netherlands
- Norway
- Philippines
- Poland
- Russia
- Singapore*
- South Africa
- Spain
- Sweden
- Switzerland
- Taiwan
- Thailand
- Turkey*
- United Arab Emirates
- United Kingdom
- United States of America*

*New Zealand has renegotiated its DTAs with Australia, Singapore and Canada, amended its DTAs with the United States, Mexico and Chile (by Protocol) and negotiated new DTAs with Hong Kong and Turkey. The renegotiated DTAs allow for lower withholding rates (refer NRWT, page 43). Refer New developments - double tax agreements (DTAs), page 63, for details of the new DTAs with Hong Kong, Turkey and Canada and the updated DTAs with Mexico and Chile.

Tax information exchange agreements (TIEAs)

A TIEA enables the tax authority of one country to access information about any persons that the tax authority of another country may hold. Inland Revenue can use the information to identify income or assets that are unreported in the person's home country and that may give rise to the evasion of tax.

TIEAs allow the exchange of information:

- on beneficial ownership of companies
- on settlors, trustees and beneficiaries of trusts
- held by banks and financial institutions.

In addition to the information exchange arrangements included in the 37 DTAs listed above, New Zealand has entered into TIEAs with:

- Anguilla*
- Bahamas*
- Bermuda*
- British Virgin Islands*
- Cayman Islands
- Cook Islands
- Curacao
- Dominica*
- Guernsey
- Gibraltar
- Isle of Man
- Jersey
- Marshall Islands*
- Netherlands Antilles
- Samoa*
- Saint Maarten
- St Christopher and Nevis*
- St Vincent and the Grenadines*
- Turks and Caicos Islands*
- Vanuatu*

*As at the date of publication, these TIEAs are not yet in force.

Taxing offshore investments

Controlled foreign companies (CFCs)

The CFC regime imposes New Zealand tax on the notional share of income attributable to residents (companies, trusts and individuals) with interests in certain CFCs.

Central to the regime is the definition of a CFC. When five or fewer New Zealand residents directly or indirectly control more than 50% of a foreign company, or when a single New Zealand resident directly or indirectly controls 40% or more of a foreign company (unless a non-associated non-resident has equal or greater control) that company is a CFC. For interests of less than 10% the investment may be taxed under the foreign investment fund regime (refer Foreign investment funds, page 39).

For income years starting on or after 1 July 2009 new rules apply to the taxation of foreign companies controlled by New Zealand residents. Under the new rules, a person with an income interest of 10% or more in a CFC does not have attributed CFC income or losses if:

- the Australian exemption applies; or
- the CFC passes an active business test.

If the exemptions do not apply, only the CFC's passive (attributable) income is subject to tax on attribution (on an accruals basis).

Active business test

A CFC passes the active business test if it has passive (attributable) income that is less than 5% of its total income. For the purposes of the test, taxpayers measure passive and total income, using either financial accounting (audited IFRS or NZ GAAP accounts) or tax measures of income.

CFCs in the same country may be consolidated for calculating the 5% ratio, subject to certain conditions.

The active exemption test may also be available to investors with less than 10% interest income in a CFC if certain criteria are satisfied.

Australian exemption

A person with an income interest of 10% or more in a CFC does not have attributed CFC income or a loss if the CFC is a resident in, and subject to income tax in, Australia and meets certain other criteria.

Passive (attributable) income

Attributable, or passive, income is income that is highly mobile and not location-specific ie income where there is a risk that it could easily be shifted out of the New Zealand tax base.

The broad categories of attributable income are as follows:

- certain types of dividend that would be taxable if received by a NZ resident company
- certain interest
- certain royalties
- certain rents
- certain amounts for financial arrangements
- income from services performed in New Zealand
- income from offshore insurance business and life insurance policies
- personal services income
- income from the disposal of revenue account property
- certain income related to telecommunications services.

Taxpayers must disclose interests in CFCs in their annual tax returns. Failure to disclose CFC interests can result in the imposition of penalties.

Foreign investment funds (FIFs)

The FIF regime is an extension of the CFC regime (refer Controlled foreign companies, page 38), which subjects persons with interests in certain foreign entities (which are not CFCs) to New Zealand tax. It also applies when the investor does not have a sufficient interest in a CFC to be taxed under that regime.

Common examples of investments classified as FIFs include foreign companies, unit trusts, foreign superannuation schemes and life insurance policies issued by foreign entities not subject to New Zealand tax.

The FIF rules can be split into two regimes:

- the portfolio FIF rules – which apply to interests of less than 10% in a FIF
- the non-portfolio FIF rules - which apply to interests of 10% or more that are outside the CFC rules.

Portfolio FIF rules

The portfolio FIF rules underwent significant reform in 2006. The new rules have applied from 1 April 2007. The portfolio FIF rules apply to interests of less than 10% in foreign companies, foreign superannuation schemes and foreign life insurance policies issued by non-resident life insurers (if the CFC rules do not apply). However, a New Zealand resident does not generally have FIF income when:

- the total cost of FIF interests held by the individual does not exceed \$50,000
- the income interest is less than 10% in certain ASX-listed companies or certain Australian unit trusts
- the CFC rules apply.

There are also exemptions for interests in certain foreign employment-related superannuation schemes. These include interests held by returning residents and new migrants acquired before the person became a New Zealand resident or within the first five years of New Zealand residence.

When an interest is exempt from the FIF rules, distributions are subject to tax on a receipts basis in accordance with normal principles.

The taxable income of a New Zealand resident with an interest in a FIF that does not qualify for one of the exemptions is calculated using one of the following methods:

- the fair dividend rate (FDR)
- the comparative value
- the cost
- the deemed rate of return.

The nature of the interest held and the availability of information restrict the choice of method.

Taxpayers must disclose interests in certain FIFs in their annual tax returns. Failure to disclose can result in the imposition of penalties.

Non-portfolio FIF rules

The Taxation (International Investment and Remedial Matters) Act 2012 reforms the non-portfolio FIF rules significantly. The new rules apply to income years starting on or after 1 July 2011. A key feature of the new rules is to extend the active income exemption (which applies for CFCs) to certain non-portfolio FIFs. If the FIF fails the active business test, passive income will be attributed to the New Zealand shareholders. The new rules also repeal the grey list exemption from the FIF rules and replaces it with an exemption for shareholders with a 10% or greater interest in a FIF that is resident and subject to tax in Australia.

When investors do not have sufficient information to perform the calculations required under the active business test (or choose not to apply the active business test) they will be able to use one of the attribution methods for portfolio FIF investments (refer page 40). The accounting profits and branch equivalent methods, which were previously available to calculate FIF income, have also been repealed under the new rules for both non-portfolio and portfolio FIF interests.

Dividends from a foreign company

For income years starting on or after 1 July 2009, a dividend derived by a company resident in New Zealand from a foreign company is treated as exempt income unless it is:

- a dividend on a fixed rate share or a dividend for which the foreign company has received a tax deduction in its home jurisdiction; or
- a dividend from a FIF that is not a 10% or greater interest in a company resident and subject to tax in Australia but is otherwise exempt from the FIF rules (eg an interest in an Australian listed company).

Dividends from foreign companies derived by taxpayers other than companies are taxable (generally with a credit for any foreign withholding taxes). However, where FIF income in respect of the investment in the foreign entity has been calculated under the FDR, cost, comparative value or deemed rate of return methods, any dividends received from the foreign company will not be subject to tax in NZ.

Branch equivalent tax account (BETA)

Previously, taxpayers who were subject to tax on attributed foreign income under the CFC or FIF regimes and also taxed or liable to pay foreign dividend payments on dividends could elect to maintain a BETA. A BETA operates in a similar manner to an Imputation Credit Account (refer Dividend imputation, page 19) and helps avoid the double taxation of attributed foreign income and foreign dividend income.

As most foreign dividends received by New Zealand companies are now exempt from tax, most companies no longer need to maintain BETAs. The Taxation (International Investment and Remedial Matters) Act abolishes BETAs from the income year beginning on or after 1 July 2012.

Payments to non-residents

Non-resident withholding tax (NRWT)

NRWT is imposed on the gross amount of dividends, interest (including redemption payments, such as discounts on commercial bills and bills of exchange) and royalties derived from New Zealand and paid or credited to companies and individuals not resident in New Zealand.

Payers of dividends, interest and royalties must deduct NRWT at source and pay it to the Commissioner by the 20th of the month following the month of deduction.

In some cases, NRWT is a minimum tax and the non-resident's net income may be subject to tax at full rates unless a DTA limits the liability.

NRWT is imposed on dividends at the following rates regardless of the jurisdiction to which the dividends are paid:

- 0% – Fully imputed dividends paid to a shareholder holding 10% or more of the direct voting interests in the company and fully imputed non-cash dividends; fully imputed dividends paid to a shareholder holding less than 10%, if subject to a reduced NRWT rate under a DTA
- 15% – Fully imputed cash dividends paid to a shareholder holding less than 10%
- 30% – In most other cases, subject to any relief available under a DTA.

Most interest payments are subject to NRWT at either 10% or 15%. NRWT is imposed on royalties at either 5%, 10% or 15%.

The new DTAs with Australia, Hong Kong, Singapore and the United States allow NRWT to be deducted at the following rates⁽¹⁾:

	Australia, USA and Hong Kong	Singapore
Dividends		
• less than 10% voting power	15%	15%
• 10% to 80% voting power	5%	5%
• over 80% voting power***	0%*	5%
Interest		
• paid to government	0%	0%
• paid to financial institution	0%**	10%
• other interest payments	10%	10%
Royalties	5%	5%

* The shares must be held for over 12 months and the shareholder company must meet certain other conditions.

** The 0% rate is only available for interest paid from NZ if AIL is paid (refer Approved issuer levy, page 43).

*** For the Hong Kong DTA, the threshold is 50%

(1) A revised DTA with Canada lowers rates as well. However, the treaty is not yet in force.

Foreign investor tax credit (FITC)

Previously, the FITC regime ensured that foreign investors were not taxed at more than the New Zealand corporate tax rate by effectively rebating the New Zealand withholding tax to the extent that the dividend was fully imputed. As NRWT rates have been reduced to nil on most fully imputed dividends FITC is generally no longer required.

From 1 February 2010, the FITC regime applies only to fully imputed dividends paid to shareholders holding less than 10% of the shares in the company on NRWT rates of at least 15%.

Approved issuer levy (AIL)

NRWT does not need to be deducted from interest paid on borrowings when:

- the New Zealand borrower and overseas lender are not associated persons
- the borrower is recognised as an 'approved issuer' by the Commissioner
- the debt instrument is registered with the Commissioner
- the borrower pays a tax deductible levy (AIL), equal to 2% of the interest paid, by the appropriate date.

Any late payment of AIL is subject to the compliance and penalties regime.

Taxpayers with annual AIL liabilities of less than \$500 are able to make six-monthly, rather than monthly, payments.

The Taxation (International Investment and Remedial Matters) Act 2012 introduces a new approved issuer levy rate of 0%, which applies to interest paid on bonds that meet certain requirements.

Non-resident contractor's tax (NRCT)

New Zealand imposes an obligation to deduct NRCT on those making contract payments to non-residents in relation to certain contract activities undertaken in New Zealand. Contract activities generally relate to services but also include the granting of a right to use property in New Zealand. The NRCT rate is 15% (or 30% for individuals and 20% for companies if the relevant paperwork is not provided). Some contractors are eligible to apply for a certificate of exemption or a reduced rate certificate.

Non-resident contractors do not have to apply for a certificate of exemption from withholding tax if they:

- are eligible for total relief under a double tax agreement; and
- are in New Zealand for less than 92 days in any 12 months.

In addition, payments for contract work amounting to less than \$15,000 in a 12-month period are exempt from NRCT. In such cases contractors themselves are responsible for paying any New Zealand tax owing at the end of the year.

Base protection

Thin capitalisation

'Inbound' thin capitalisation rules apply to New Zealand taxpayers controlled by non-residents, including branches of non-residents. The aim of the rules is to ensure that New Zealand entities or branches do not deduct a disproportionately high amount of the worldwide group's interest expense. This is achieved by deeming income in New Zealand when, and to the extent that, the New Zealand entities in the group are thinly capitalised (ie excessively debt funded).

From 1 July 2009, the thin capitalisation regime was extended to New Zealand companies controlled by New Zealand residents that have interests in CFCs (outbound thin capitalisation). The outbound thin capitalisation rules are further extended from 1 July 2011 to include NZ companies controlled by New Zealand residents that have interests in FIFs and that apply either the active income exemption or the exemption for Australian resident FIFs. The outbound thin capitalisation rules are intended to operate as a base protection measure to prevent New Zealand residents with CFC and FIF investments from allocating an excessive portion of their interest cost against the New Zealand tax base.

In conjunction with the introduction of the 'outbound thin capitalisation' rules, the definitions of 'debt' and 'assets' for thin capitalisation purposes were also amended. Equity investments in CFCs are excluded from 'assets'. 'Fixed rate shares' issued by a New Zealand company to New Zealand taxpayers and stapled debt securities are treated as debt. Payments made on fixed rate shares are included in interest when determining a taxpayer's additional income adjustment under the thin capitalisation rules.

Equity investments in FIFs (where the active business exemption or Australian exemption is being applied) are also excluded from 'assets' from 1 July 2011.

To reduce taxpayer compliance costs the outbound thin capitalisation rules do not apply when the New Zealand taxpayer has 90% or more of their assets in New Zealand.

When the taxpayer has total interest deductions of less than \$1 million, the interest adjustment under the 'outbound' thin capitalisation rules will be reduced to zero.

An apportionment of deductible interest is required under the thin capitalisation rules when the debt percentage (calculated as total group debt/total group assets of a New Zealand entity or group) exceeds both:

- 60% for 'inbound' thin capitalisation, (the 60% threshold was reduced from 75% from the beginning of the 2011/2012 income year) or 75% for 'outbound' thin capitalisation
- 110% of the worldwide group's debt percentage.

The use of the debt to asset ratio differs from most thin capitalisation models, which apply to an entity's debt to equity ratio. All interest (both related and unrelated party) is subject to apportionment.

The Taxation (International Investment and Remedial Matters) Act 2012 introduces a new 'interest cover' based thin capitalisation test. This new test applies to the outbound thin capitalisation rules and gives certain New Zealand-based groups the option of using a ratio of net interest expense to net income, rather than the debt to asset ratio under the existing test.

Foreign-owned banks operating in New Zealand are subject to specific thin capitalisation rules that deem income if the bank does not hold a level of equity equivalent to 4% of their New Zealand banking risk-weighted assets. In addition, banks are required to have sufficient equity to equity fund offshore investments that do not give rise to New Zealand taxable income in full. Refer to New developments – thin capitalisation, page 63 for proposed changes to the thin capitalisation rules for foreign-owned banks.

Transfer pricing

The transfer pricing rules are based on OECD principles and require taxpayers to value for tax purposes all cross-border transactions with associates on an arm's length basis.

The transfer pricing rules apply to arrangements for the acquisition or supply of goods, services, money, intangible property and anything else (other than non-fixed rate shares), when the supplier and acquirer are associated persons. Similar rules apply to the apportionment of branch profits.

Various methods are available for determining the 'arm's length consideration'. The taxpayer is required to use the method that produces the most reliable measure of the amount that independent parties would have paid or received in respect of the same or similar transactions. Inland Revenue has published guidelines that make it clear that documentation is required to support a taxpayer's transfer prices.

Tax administration and payment of tax

Returns

Generally the following persons and entities are liable to lodge an income tax return:

- individuals who derive income not taxed at the time of payment unless that income is less than \$200
- individuals who are in business or engaged in a profession
- all companies, societies, clubs and some public authorities
- all partnerships, trusts and superannuation funds
- absentees deriving income from New Zealand.

Returns are not required for individuals who receive only:

- income from employment that is subject to PAYE
- interest and dividends that are subject to RWT or do not have a New Zealand source.

At the end of the year, Inland Revenue prepares personal tax summaries for certain individuals based on information provided by employers. This group includes individuals with incorrect or special deduction rates, student loans or Working for Families tax credits. Other taxpayers may request a personal tax summary from Inland Revenue.

Housekeeper/childcare and donations credits are claimed using a separate form, (unless, for the latter, the new payroll giving system is used). The PAYE rates build in some credits removing the need for taxpayers to make a separate claim.

Inland Revenue sends individuals who file IR3 returns and receive source deduction payments a summary of earnings containing income and tax deduction information from their employer. Taxpayers can use this to prepare the IR3.

Lodgement date (final date without penalty):

- when linked to a chartered accountant or other tax agent – 31 March of the following income year.

Otherwise:

- i) taxpayers with balance dates 1 October to 31 March – the following 7 July
- (ii) taxpayers with balance dates 1 April to 30 September – 7th day of fourth month after balance date.

Taxpayers have four years in which to claim a refund of overpaid tax. However, when there has been a clear mistake or simple oversight or in the case of credits, the Commissioner may extend the period to eight years.

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill proposes changes to the requirements for returns filing and record keeping for businesses (refer New developments – returns filing requirements, page 62).

Assessments and disputes

The Commissioner may adjust a return by way of a notice of proposed adjustment. A taxpayer who disagrees with the notice will need to begin the disputes resolution process.

This process aims to resolve disputes as quickly as possible by early identification of all issues, full disclosure of the facts and evidence and consultation between the taxpayer and Inland Revenue.

There are strict limits (generally two monthly intervals) built into the process which apply to both the taxpayer and the Commissioner. A taxpayer who does not respond in the required manner and within the time limit will be deemed to accept Inland Revenue's position and generally will not be able to challenge the adjustment further. Except in limited specific circumstances, the Commissioner is required to follow the full disputes process before issuing an assessment.

The Commissioner has four years in which to amend an assessment unless the taxpayer's return is fraudulent or wilfully misleading or excludes amounts of gross income.

The Taxation (Tax Administration and Remedial Matters) Act 2011 amended the disputes resolution process. The changes include:

- limiting the application of the evidence exclusion rule to issues and propositions of law. Previously a taxpayer and the Commissioner were limited in Court proceedings to the facts, evidence, issues and propositions of law disclosed in their respective statements of position.
- introducing an 'intention to dispute' test for late notices to allow the Commissioner to accept late documents if the taxpayer has demonstrated an intention to enter into or continue the disputes process.
- repealing a taxpayer's ability to opt out of the disputes process where the taxpayer has initiated the dispute to ensure that there is consistency between taxpayer and Commissioner initiated disputes.
- removing the small claims jurisdiction, with application to disputes where no election to the small claims jurisdiction has been made before 29 August 2011.

Provisional tax

Every taxpayer who is liable to pay residual income tax exceeding \$2,500 for the 2012/2013 income year is a 2012/2013 provisional taxpayer. Residual income tax is the amount of income tax payable by a taxpayer after deducting tax credits but before deducting any provisional tax paid. Provisional tax is generally payable in three equal instalments (refer Payment dates for the 2012/2013 income year, page 49 - 50).

Tax pooling

Taxpayers may reduce their exposure to use of money interest on provisional tax by using an Inland Revenue approved tax pooling intermediary. Tax pooling intermediaries facilitate the trading of under- and over-payments of provisional tax and typically save taxpayers 2% – 3% on the official rates.

Calculating provisional tax

Provisional taxpayers have three options available for calculating their provisional tax for the 2012/2013 income year (ie year ending 31 March 2013).

These options are:

- the standard uplift method
- the estimate method
- the GST ratio method.

Standard uplift method

Under the standard uplift method the general rule is that provisional tax payable is 105% of the residual income tax for the previous income year. However, if the prior year tax return has not been filed due to an extension of time for filing (refer Returns, page 46), the provisional tax payable can be based on 110% of the residual income tax for the income year before the previous income year (ie two years ago), but only for the first two instalments. The final instalment must be calculated based on 105% of the previous income year's residual income tax.

The changes in personal and company income tax rates from 1 October 2010 affect the rates used to calculate provisional tax for the 2012/2013 income year as follows:

	General rule	2012/13 income year
Individuals		
Uplift based on prior year RIT	RIT * 105%	RIT * 105%
Uplift based on year preceding prior year RIT	RIT * 110%	RIT * 100%
Companies and other entities taxed as companies (e.g. PIEs)		
Uplift based on prior year RIT	RIT * 105%	RIT * 105%
Uplift based on year preceding prior year RIT	RIT * 110%	RIT * 105%
Other entities (e.g. trusts)		
Uplift based on prior year RIT	RIT * 105%	RIT * 105%
Uplift based on year preceding prior year RIT	RIT * 110%	RIT * 110%

Estimate method

Provisional tax can be based on an estimate of the income year's residual income tax. A taxpayer who chooses to estimate residual income tax is required to take reasonable care when doing so.

GST ratio method

The GST ratio method enables smaller taxpayers to align their provisional tax payments with their cash flow and reduce their exposure to use of money interest. The option benefits those taxpayers with declining, seasonal or fluctuating income. This option calculates provisional tax by reference to the taxpayer's GST taxable supplies in the relevant provisional tax instalment period.

Taxpayers can also make voluntary payments. Such payments can minimise exposure to use of money interest (refer Use of money interest, page 52).

When the taxpayer files their tax return for the year, the provisional tax paid for that year is credited against the tax assessed. This results in either a refund or further tax to pay by way of terminal tax.

Tax discount in first year of business

Although individual taxpayers are not required to pay provisional tax in their first year of business, they are still required to pay income tax on any income derived in the first year. Generally, this income tax is payable at about the same time as the third instalment of provisional tax for the next year is due. Individuals who begin receiving self-employed or partnership income are eligible for a 6.7% discount. Essentially, the discount operates so that an eligible taxpayer who pays income tax prior to the end of an income tax year receives a credit for the lesser of 6.7% of the amount paid or 6.7% of 105% of the residual income tax for that income tax year. The discount is designed to relieve eligible taxpayers of the financial strain of making two years' worth of tax payments at the same time.

Payment dates for the 2012/2013 income year

The provisional tax payment dates depend on the frequency with which a taxpayer files their GST returns. Generally provisional tax payments are due on the following dates:

Month of Balance Date	First Provisional Tax Instalment (one-third)	Second Provisional Tax Instalment (one-third)	Third Provisional Tax Instalment (one-third)	Terminal Tax Instalment (payable subsequent to balance date)
October	28 March	28 July	28 November	7 September
November	7 May	28 August	15 January	7 October
December	28 May	28 September	28 January	7 November
January	28 June	28 October	28 February	7 December
February	28 July	28 November	28 March	15 January
March	28 August	15 January	7 May	7 February
April	28 September	28 January	28 May	7 February
May	28 October	28 February	28 June	7 February
June	28 November	28 March	28 July	7 February
July	15 January	7 May	28 August	7 February
August	28 January	28 May	28 September	7 February
September	28 February	28 June	28 October	7 February

The terminal tax due date is extended by 2 months for taxpayers linked to a tax agent.

Late payment and shortfall penalties

An initial late payment penalty of 1% applies if the taxpayer does not pay tax by the due date. A further 4% late payment penalty applies if the tax is still not paid within 7 days of the due date. An incremental late payment penalty of 1% is then imposed monthly until payment is made.

Inland Revenue is required to notify a taxpayer the first time their payment is late rather than imposing an immediate late payment penalty. If the taxpayer does not make payment by a certain date, Inland Revenue will impose a late payment penalty. Taxpayers are entitled to one notification every two years. After receiving a first warning, Inland Revenue will not send further notifications for two years and will impose an initial late payment penalty in the normal manner.

Shortfall penalties, calculated as a percentage of the tax shortfall resulting from the action or position taken by the taxpayer in a tax return, may also apply. These are:

Penalty – percentage of tax shortfall

Action subject to penalty	Standard rate	Reduced by 100% / 75% for disclosure before audit or timing error only	Reduced by 40% for disclosure during audit	Reduced by 75% for disclosure when filing	Increased by 25% for obstruction
Lack of reasonable care	20%	0%	12%	n/a	25%
Unacceptable tax position	20%	0%	12%	5%	25%
Gross carelessness	40%	10%	24%	n/a	50%
Abusive tax position	100%	25%	60%	25%	125%
Evasion	150%	37.5%	90%	n/a	187.5%

There is a 50% discount on certain penalties when the taxpayer has a past record of good behaviour and, in certain circumstances, a cap of \$50,000 on shortfall penalties for not taking reasonable care or for taking an unacceptable tax position.

When a taxpayer discloses a tax shortfall voluntarily before notification of a tax audit or investigation penalties imposed for lack of reasonable care and for taking an unacceptable tax position are reduced by 100%.

Use of money interest (UOMI)

Taxpayers are required to pay interest when taxes are not paid by the due date for payment. There is a corresponding requirement for the Commissioner to pay interest to the taxpayer when the taxpayer has overpaid tax. UOMI applies to most tax obligations eg income tax, PAYE, FBT and GST.

All provisional taxpayers, other than individuals who were not liable to pay residual income tax exceeding \$50,000 and who did not pay their provisional tax on the estimation basis, are subject to the 'use-of-money' interest regime. When residual income tax exceeds provisional tax paid, the taxpayer is liable to pay interest on the underpayment. Interest is payable regardless of culpability. When provisional tax paid exceeds residual income tax, the taxpayer is entitled to receive interest on the overpayment.

UOMI rates

From 16 January 2011 the rate for overpaid tax is 2.18% and the rate for underpaid tax is 8.89%. Interest is generally calculated from the due date for the first instalment of provisional tax. Interest paid is deductible for both companies and individuals, while interest received is taxable.

The UOMI rates will decrease from 8 May 2012. The rate for overpaid tax will decrease to 1.75%. The rate for underpaid tax will fall to 8.4%.

Binding rulings

The Commissioner is able to make binding public rulings and, at a taxpayer's request, private and product rulings on specific tax issues. Rulings bind the Commissioner on the application of the law to which the rulings relate.

Other taxes

Capital gains tax

New Zealand does not have a capital gains tax as such. However, gains from the sale of real property (land and buildings) and personal property (including shares) acquired for the purpose of resale, or as part of a dealing operation, are subject to income tax at normal rates. Profits on the sale of real property may be taxable in other circumstances also.

Specific regimes such as the financial arrangements rules, foreign investment fund rules and the services-related payments rules also effectively blur the capital/revenue distinction.

Fringe benefit tax (FBT)

FBT is payable by employers on the value of fringe benefits provided to employees and shareholder/employees. The value of fringe benefits provided is not included in the gross income of employees.

The FBT quarters end with the last day of June, September, December and March. Within 20 days of the end of the first, second and third quarter, any employer who has provided a fringe benefit is required to file a return setting out the fringe benefits received or enjoyed by employees in the quarter and a calculation of the amount of FBT payable on those benefits. The due date for filing the fourth (March) quarter return is 31 May.

Employers with PAYE and employer superannuation contribution tax deductions (refer PAYE and employer superannuation contribution tax, page 56) not exceeding \$500,000 per annum can pay FBT on an annual basis. An income year basis is also available for shareholder-employees.

FBT rates

Employers can pay FBT at either 43% or 49.25% of the taxable value of fringe benefits provided for the first three quarters of the tax year.

If the 43% rate is used in any one of quarters 1 to 3, complete either the 'full' multi-rate calculation (also known as the full attribution option) or the 'short form' option in the fourth quarter.

If the 49.25% rate is used in the first three quarters, either complete the multi-rate calculation in the fourth quarter or pay FBT at 49.25%. Under the full attribution option, the applicable FBT rate depends on the net remuneration (including fringe benefits) paid to the employee. The attribution calculation, which is performed in the fourth quarter, treats the fringe benefit as if it was paid in cash and calculates FBT as the notional increase in income tax that would otherwise have arisen.

The 'short form' option applies the flat rate of 49.25% to all attributed benefits and 42.86% (or 49.25% for major shareholders and associates) to all non-attributed benefits.

The multi-rates for 2011/2012 and subsequent income years are:

Net remuneration	FBT rate %
\$12,530 or less	11.73
\$12,531 - \$40,580	21.21
\$40,580 - \$55,980	42.86
>\$55,980	49.25

Under the full attribution system, where possible, all benefits must be attributed to a particular employee. However, certain low value exemptions apply. The tax threshold for exempting unclassified benefits from FBT is \$300 per employee per quarter and \$22,500 per employer per annum.

All benefits not attributed to individuals are pooled and subject to FBT at 42.86% (or 49.25% for major shareholders and associates). A benefit is attributable to an individual if the asset or benefit is 'principally' assigned, used or available for use by that employee during the quarter or income year as appropriate.

Examples of the value on which FBT is to be calculated are as follows:

Fringe benefit	Taxable value of benefit
<ul style="list-style-type: none"> • Motor vehicle 	<p>Employers can value a vehicle on an annual basis either using 20% of the cost price or market value (GST inclusive) of the vehicle (depending on whether the vehicle is owned or leased by the employer) or 36% of the vehicle's tax written down value (GST inclusive). In each case, the FBT value must be reduced proportionately for whole days when the vehicle is not available for private use at any time.</p>
<ul style="list-style-type: none"> • Employment-related loan 	<p>The amount by which the interest payable on the loan is less than the interest that would be payable if calculated using the prescribed rate. The prescribed rate is determined on a quarterly basis. The rate from 1 July 2011 is 5.90%.</p> <p>Employers who are in the business of lending money to the public can elect to calculate FBT on employment-related loans using a market interest rate instead of the prescribed rate.</p>
<ul style="list-style-type: none"> • Employer contributions to medical insurance 	<p>The whole amount of the contribution.</p>
<ul style="list-style-type: none"> • Employer contributions to employee superannuation funds 	<p>Subject to employer superannuation contribution tax (ESCT).</p>
<ul style="list-style-type: none"> • Employer contributions to superannuation schemes 	<p>The whole amount of the contribution.</p>
<ul style="list-style-type: none"> • A benefit of any other kind received by an employee 	<p>The price that an independent third party would pay for the goods or services in the normal course of business.</p>

FBT also applies to benefits received by an employee from a third party when there is an arrangement between the employer and the third party and when the benefit would be subject to FBT if the employer had provided it. Generally FBT does not apply to discounted goods or services received by an employee from a third party, if the price paid by the employee is not less than the price that would be charged to other groups of people.

Benefits that are not subject to FBT include specified superannuation contributions (which are separately taxed), the provision of accommodation by an employer (which is subject to PAYE), and the use of a business tool such as a mobile telephone or laptop (provided the tool is used primarily for business purposes and the cost of the tool does not exceed \$5,000). FBT is generally a tax-deductible expense, so the effective FBT cost corresponds to the relevant employee's marginal tax rate.

PAYE and employer superannuation contribution tax (ESCT)

Employers are required to make PAYE tax deductions from employee remuneration (refer PAYE, page 14) and ESCT deductions from any employer superannuation contribution made to a superannuation fund.

Employers who made total deductions of \$500,000 or more in the preceding year must remit PAYE and ESCT deductions twice monthly. The payments are due on the 20th day of each month (for days 1 to 15 of the same month) and the 5th day of the following month (for days 16 to month-end of the preceding month).

Employers who made total deductions of \$500,000 or less in the prior year make one remittance of PAYE and ESCT deductions on the 20th of the month for deductions made in the previous month.

Employer contributions made to a KiwiSaver scheme or an employee superannuation scheme with similar lock-in requirements will no longer be exempt from ESCT from 1 April 2012 (refer to New developments – employer superannuation contribution tax, page 63).

An employer must withhold ESCT on contributions it makes to a superannuation fund on behalf of an employee. The rates of ESCT are 10.5%, 17.5%, 30% or 33% (depending on the employee's marginal tax rate).

Accident compensation insurance

All New Zealanders pay levies to fund a statutory scheme of accident insurance cover. These are paid by employers and self-employed people to cover work-related injuries and by earners to cover non-work injuries.

Motor vehicle accident cover is funded by a component of motor vehicle registration fees and a percentage of fuel sales. This covers claims for all injuries resulting from motor vehicle accidents on New Zealand public roads.

The Government funds the costs of cover for injuries to people who are not in the paid workforce, unless the injury is related to a motor vehicle accident on a public road.

The Accident Compensation Corporation (ACC) collects the employer levy, self employed levy, residual claims levy and earners' account levy by issuing an invoice to the relevant party. Employers generally deduct earner premiums, together with PAYE, from an employee's income and remit it to Inland Revenue (as agent for ACC).

Employer levies

The ACC is the sole provider of workplace accident insurance in New Zealand providing statutory minimum entitlements. The private sector can write accident insurance contracts only if they provide cover above the minimum entitlements.

As a result of a previous regime, private insurers remain responsible for the continuing cost of workplace accidents that occurred between 1 July 1999 and 30 June 2000 for which they have provided cover.

All employers are required to pay employer levies to cover workplace accidents (minimum entitlement cover). The employer levy payable is determined according to the industry or risk classification of the employer and the level of earnings of employees. The levy may be adjusted up or down following an audit of the safety practices of the employer.

Employers also have the option of becoming accredited under the ACC Partnership Programme. Under the Programme, the employer takes responsibility for managing their employees' workplace injuries. This is a self-insurance mechanism where the employer assumes liability for some, or all, of the costs of providing statutory entitlements directly to employees as agent for the ACC. In return, the ACC charges the employer reduced premiums.

Self-employed persons now have the option of purchasing the right to receive an agreed amount of compensation, rather than compensation calculated retrospectively after the injury and based on actual earnings.

Residual claims levy

In addition to work accident insurance cover, the residual claims levy is payable annually by employers and the self-employed. It funds the cost of claims outstanding from the 'old' ACC scheme ie the ongoing costs of:

- (i) work injury claims that occurred prior to 1 July 1999; and
- (ii) non-work injuries to earners that occurred prior to 1 July 1992.

This 'tail' of claims arises due to the 'old' ACC scheme being run on a 'pay as you go' system rather than fully funding all future claims.

The residual claims levy is risk-rated on individual employers' industrial classifications. The residual claims levy rate varies from year to year depending on the success of the ACC rehabilitation programme in managing claim costs. The objective of this levy is to establish reserves over a 15 year period to fully fund the 'tail'. The ACC collects residual claims levies from employers and self-employed directly.

The residual claims levy is a deductible expense to the employer or self-employed person in the income year it is due and payable. When a self-employed person's terminal tax date has been extended to 7 April (because they are linked to a tax agent) the residual claims levy is deemed to be deductible in the previous income year, as if the levy were payable on 7 February.

Earners levy

All earners (employees and self-employed persons) are liable for an 'Accident Compensation Earner Levy'. From 1 April 2012 the levy is payable at the rate of \$1.70 per \$100 of liable earnings, GST inclusive.

The earner levy on earnings from self-employment is a deductible expense to the self-employed person in the income year it is due and payable.

Earners levies payable by employees are deducted via the PAYE system (ie built into the PAYE deduction tables).

Earnings of the following nature are not liable for the earner levy:

- withholding payments
- retirement or redundancy payments
- student allowances

various benefits

- pensions and tax-free allowances.

The maximum amount of liable earnings in the 2012/2013 income year will increase to \$111,669 for self-employed persons and \$113,768 for other earners.

Liable earnings include both earnings as an employee and other earnings derived as a result of personal exertion.

Goods and services tax (GST)

GST is a consumption tax which is imposed under the Goods and Services Tax Act 1985. GST is imposed on the supply of goods and services in New Zealand and on goods imported into New Zealand (in addition to any customs duty).

GST is levied at the rate of 15% (prior to 1 October 2010 it was 12.5%), although some supplies are taxed at zero percent and certain specified supplies are exempt from the tax.

The tax is generally borne by the final consumer. Goods and services are taxed at each transaction stage, with a credit being given to registered persons for GST previously paid on goods or services.

Normally GST has no impact on business profits, except for additional administration and compliance costs and cash flow effects. However, there are instances where the tax falls on the business taxpayer as a final consumer eg GST on fringe benefits supplied to employees or GST on deemed supplies of non-deductible entertainment expenditure.

GST is normally accounted for on an accrual (invoice) basis but where turnover in a given 12-month period is less than \$2 million there is an option to account for GST on a cash basis.

Registered person

Any person who, in a given 12-month period, makes total taxable supplies in excess of \$60,000 in New Zealand in the course of all taxable activities is liable to be registered for GST. This is a turnover threshold – the level of profit/loss is irrelevant. Registered persons must generally file a GST return once every two months. However, a person may apply to file on a six-monthly basis if taxable supplies do not exceed \$500,000 in a given 12-month period. Where turnover exceeds \$24 million per annum registered persons are required to submit GST returns on a monthly basis.

Exempt supplies

Certain supplies, known as exempt supplies, are specifically excluded from the imposition of GST.

These include:

- supply of financial services (other than those which are zero-rated)
- letting of residential accommodation
- supplies of fine metal (except for those which are zero-rated).

Being exempt means that no GST is payable on such supplies. However, GST on associated costs is not recoverable as 'input tax'.

Zero-rated supplies

Certain supplies, known as zero-rated supplies, are taxed at the rate of zero percent. While no GST is payable on zero-rated supplies, in contrast to exempt supplies, GST on associated costs is recoverable as input tax. Zero-rated supplies include:

- exported goods
- services supplied to a New Zealand resident in connection with temporary imports
- goods situated overseas
- a taxable activity disposed of as a going concern
- certain 'exported' services including supplies in relation to exported goods where the services are supplied to a non-resident who is outside New Zealand at the time the services are performed
- business-to-business supplies of financial services
- certain transactions involving emissions units
- supplies that include land where the purchaser is GST-registered and acquires the goods with the intention of using them to make taxable supplies and is not intending to use the property supplied as their principal place of residence.

Imported services

A 'reverse charge' mechanism requires the self-assessment of GST on the value of services imported by some registered persons. The reverse charge applies to imported services that are not used for making taxable supplies and that would have been subject to GST if they had been provided in New Zealand.

Refer to New developments – GST (page 64) for proposed changes to GST.

Customs duty

Customs duty is levied on some imported goods at rates generally ranging from 0% to 10%.

Excise duty

Excise duty is levied, in addition to GST, on alcoholic beverages (eg wines, beers, and spirits), tobacco products and certain fuels (eg compressed natural gas and gasoline).

Gift duty

Gift duty has been repealed in respect of gifts made on or after 1 October 2011.

Estate duty

Estate duty has been abolished in respect of the estates of persons who die on or after 17 December 1992.

Stamp duty

Stamp duty has been abolished in respect of instruments executed after 20 May 1999.

Cheque duty and credit card transaction duty

Duty is payable at the rate of 5 cents per cheque transaction. Credit card transaction duty has been repealed.

New developments

Returns filing requirements

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill, introduced in September 2011, proposes changes to the requirements for returns filing and record keeping for businesses. The proposed changes are intended to reduce compliance costs for taxpayers and help Inland Revenue meet its objective to deliver the majority of its services electronically.

The proposals include:

- amalgamating the two main income tax return forms (the personal tax summary and IR 3 forms).
- removing the requirement for taxpayers to file an income tax return simply because they are receiving Working for Families tax credits.
- allowing the Commissioner to authorise data storage providers to store their clients' tax records offshore, and the power to revoke the authorisation.
- allowing taxpayers who submit their returns electronically to store them electronically.

The Bill also includes an amendment requiring individual taxpayers who choose to file a tax return to file returns for the previous four years as well as the current year. This amendment is designed to prevent taxpayers from 'cherry-picking' the years in which they are due a tax refund and then filing in those years only.

If enacted, the proposed amendments will apply from the 2014-2015 income year.

Unsuccessful software costs

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill introduces an upfront deduction for expenditure incurred on unsuccessful software development projects in the year that the development is abandoned. If enacted this amendment will apply retrospectively from the 2007-2008 and later income years.

Profit distribution plans

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill proposes to treat shares issued under profit distribution plans (PDPs) as taxable dividends from 1 July 2012. The changes follow the Government's announcement in April 2009 that it intended to tax bonus issues of shares distributed under PDPs in the same way as it taxes shares issued under other dividend reinvestment plans.

KiwiSaver

As announced in Budget 2011, the Taxation (Annual Rates and Budget Measures) Act 2011 reduces the maximum member tax credit from \$1 to 50c for every \$1 contributed by members up to a maximum of \$521.43 per year. This amendment will apply to member tax credits paid for the year ended 30 June 2012 and later years.

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill raises the minimum employee and employer contribution rates for KiwiSaver from 2% to 3% of an employee's gross salary or wages. If enacted, the new rates will apply from 1 April 2013.

Employer superannuation contribution tax (ESCT)

In conjunction with the KiwiSaver changes announced in Budget 2011, the Taxation (Annual Rates and Budget Measures) Act 2011 removes the current exemption from ESCT for an employer's superannuation contributions (up to 2% of salary and wages) to an employee's KiwiSaver and complying superannuation fund accounts from 1 April 2012.

From 1 April 2012, employers must calculate ESCT at a rate equivalent to an employee's marginal tax rate. The default deduction rate (a flat rate of 33%) is removed from 1 April 2012.

Thin capitalisation

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill proposes to increase the minimum equity threshold of a foreign held bank from 4% to 6% of the group's risk-weighted exposures from 1 April 2012.

Double tax agreements (DTAs)

Hong Kong - New Zealand DTA

A new DTA came into force on 9 November 2011. The DTA brings withholding tax rates into line with rates currently in operation with the US and Australia. The DTA applies in New Zealand for withholding taxes from 1 April 2012. In respect of all other taxes, the DTA applies in New Zealand for income years beginning on or after 1 April 2012.

Turkey – New Zealand DTA

A new DTA came into force on 28 July 2011. The DTA is effective in New Zealand for withholding taxes from 1 January 2012. In respect of all other taxes the DTA applies in New Zealand for income years beginning on or after 1 April 2012. In Turkey, the DTA is effective generally for taxable periods beginning on or after 1 January 2012.

Canada - New Zealand DTA

New Zealand and Canada have signed a new double tax agreement (DTA), which will replace the 1980 treaty. The updated agreement will come into force once both countries have given legal effect to it. In New Zealand, this will occur through an Order in Council.

The withholding rate on dividends will reduce from 15% to a maximum of 5% for an investor who holds at least 10% of the shares in the company that pays the dividend. The withholding rate on royalties will reduce from 15% to 10% generally, with a further reduced rate of 5% for royalties relating to copyright, computer software and others.

Changes to Mexico and Chile DTAs

Lower non-resident withholding tax rates on dividends and royalty payments under New Zealand's DTAs with Chile and Mexico apply retrospectively from 1 May 2010. The reciprocal withholding tax rate on royalties arising in New Zealand and Chile has decreased from 10% to 5%. The withholding tax rate for dividend payments arising in New Zealand and Mexico has decreased from 15% to either 5% or zero, depending on the size of the investor's shareholding in the company paying the dividend and certain other criteria.

DTAs under negotiation

New Zealand is currently negotiating DTAs with Papua New Guinea, Netherlands, Luxembourg, the United Kingdom and Vietnam.

GST

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill proposes an amendment to the Goods and Services Tax Act 1985 to provide that late payment fees are subject to GST.

Other proposed changes to the GST rules include:

- a new rule precluding liquidators, receivers and administrators from changing their GST accounting basis from payments to invoice basis to claim GST deductions (effective from the date of enactment).
- confirmation that an assignment of a commercial lease can be zero-rated under the compulsory zero-rating (CZR) regime.
- amendments to the nomination rules for non-land transactions to ensure a GST-registered contractual purchaser can claim a GST deduction even if the nominee is not GST-registered.

The Government has not yet confirmed when these proposed changes will apply from if enacted.

Earthquake relief measures

The Taxation (Canterbury Earthquake Measures) Act 2011 provides earthquake relief through the tax system for Canterbury residents and businesses. Relief measures include the following exemptions from:

- tax and gift duty on trading stock donated by businesses, effective 4 September 2010 to 31 March 2012.
- income tax and fringe benefit tax for welfare contributions (cash, goods and accommodation). This exemption applied to income other than normal pay/benefits provided by employers to employees within eight weeks of the 4 September 2010 and 22 February 2011 earthquakes.
- certain payments made to families who receive social assistance because of the earthquakes from counting as income for some benefit abatement purposes.

The redundancy payment tax credit was also extended to 30 September 2011.

Tax policy work programme

The focus of the Government's tax policy work programme for 2012 and 2013 is on increasing efficiency and fairness in the tax system. Specific areas of focus will include further simplification measures for small and medium businesses, deductibility of 'mixed-use assets', ensuring consistency in the tax treatment of employee benefits, reviewing the tax treatment of New Zealand residents' foreign superannuation and ensuring deductibility of certain 'black hole' expenditure. Extending the active income exemption to branches and seeking mutual recognition of imputation and franking credits is also on the Government's agenda for the next 18 months.

Inland Revenue's compliance management programme

In July 2011 Inland Revenue announced its key areas of focus for 2011-2012.

These include complex financing arrangements, loss generation and usage, diverting personal income and the 'hidden economy'.



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