GST Direct: Pointing the way

September 2012

Issue 14

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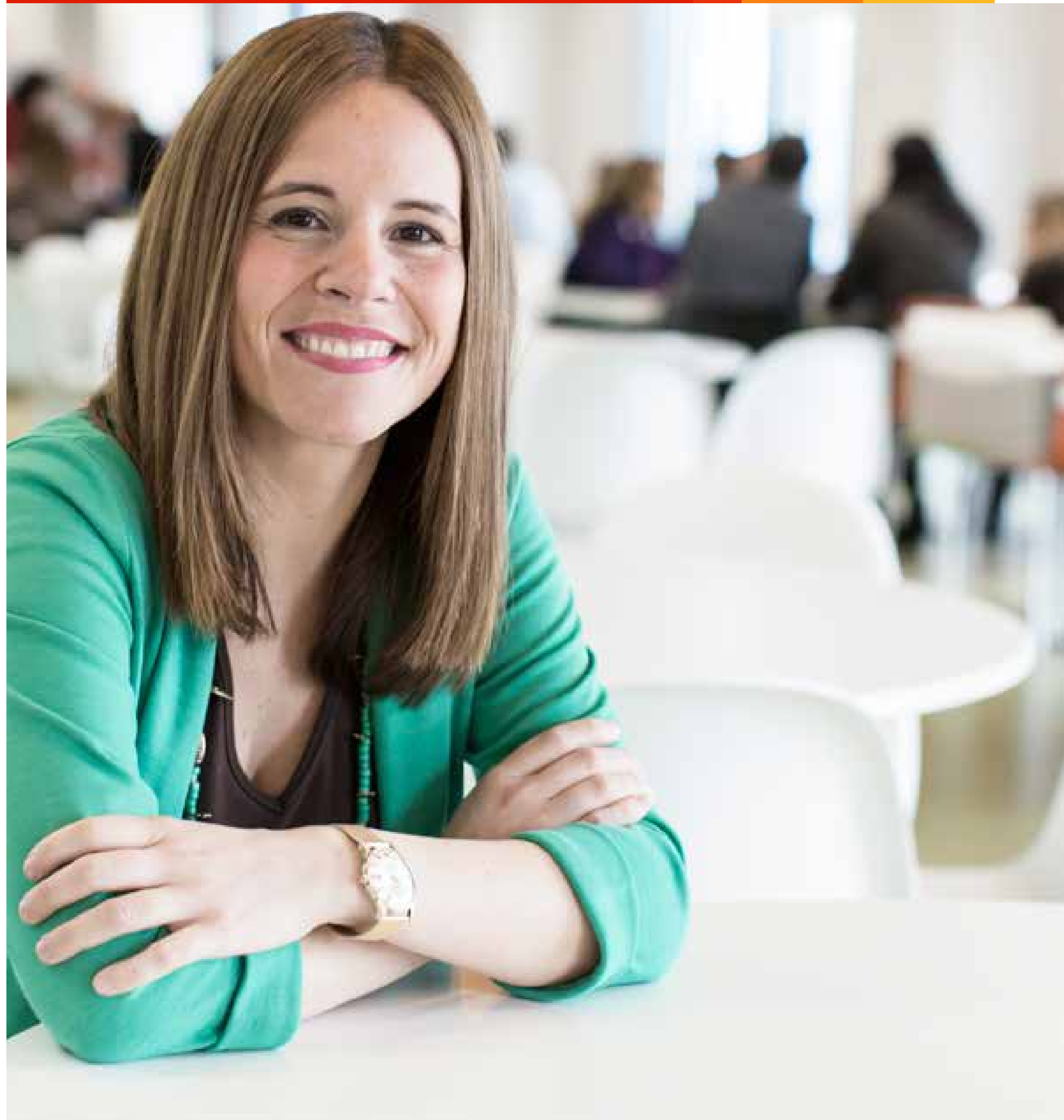

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New Bill introduces more GST changes

The Taxation (Livestock Valuation, Assets Expenditure and Remedial Matters) Bill was introduced to Parliament on 13 September 2012.

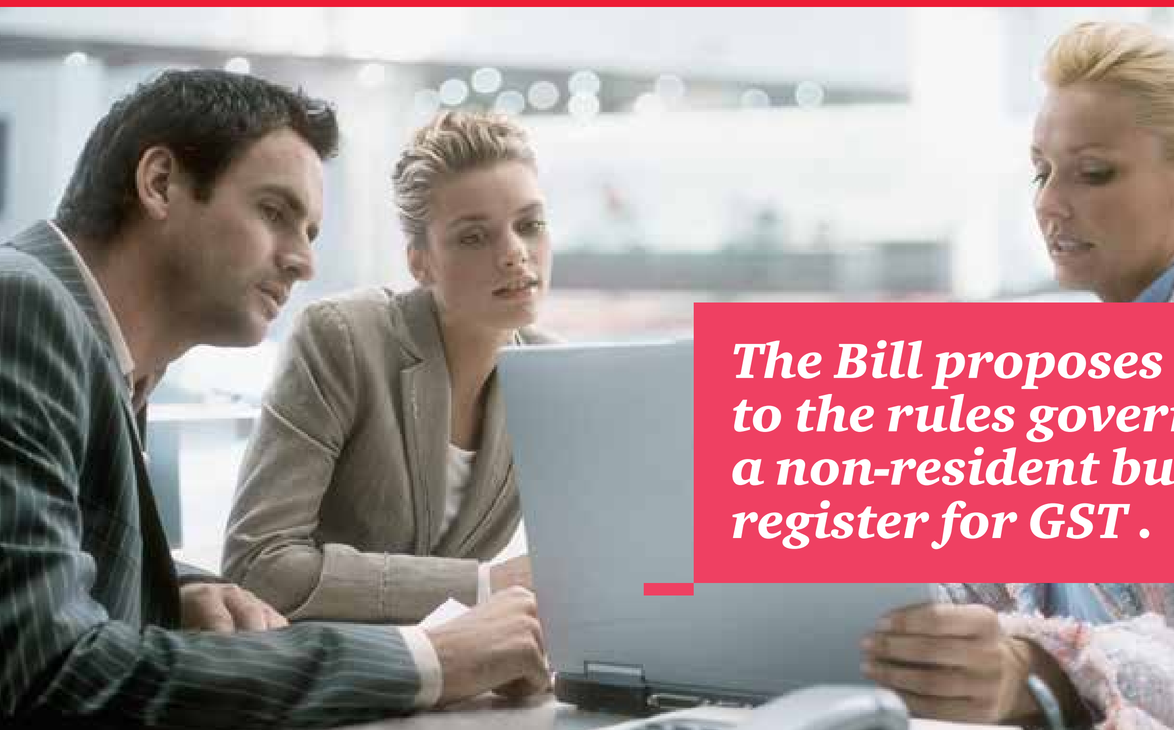
In a welcome development, the Bill proposes changes to the rules governing when a non-resident business can register for GST and claim input tax deductions. These changes are intended to allow non-residents to register and claim GST input tax in a manner comparable to New Zealand residents. Although non-residents must meet certain registration criteria and the Commissioner has the ability to deregister a non-resident in certain circumstances, this change is generally a positive one as it promotes cross-border business-to-business neutrality.

Another positive development is the introduction of a new zero-rating rule to allow taxpayers to zero-rate certain tooling costs charged to non-resident customers. Taking GST out of the equation will help New Zealand manufacturers and make them more competitive on the world stage.

If the Bill is enacted, both of the above amendments will have an application date of 1 April 2014.

Other changes include:

- Changes to the treatment of mixed-use assets to require owners to apportion their input deductions in a way which reflects their relative taxable to non-taxable use. This is expected to apply to taxable periods starting from 1 April 2013;
- Changes to allow organisers of prize competitions to deduct cash prizes from the total proceeds collected;
- Changes to allow principals and agents to agree to 'opt-out' of the agency rules;
- Amendments to align the record keeping requirements in the GST Act with proposed new record keeping provisions in the Tax Administration Act 1994 which allows the Commissioner to authorise the storage of tax records offshore in certain instances; and
- Changes to reflect the fact that certain local authorities will no longer be eligible to account for GST on a payments basis.



The Bill proposes changes to the rules governing when a non-resident business can register for GST .

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Property developer carrying on taxable activity

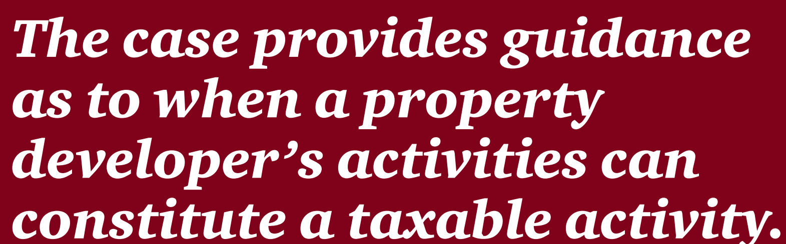
The Taxation Review Authority recently ruled on a case (TRA 009/11) involving a property developer and examined the question of whether the developer was conducting a taxable activity. The case will be of interest to many as it provides guidance as to when a property developer's activities can constitute a taxable activity.

Briefly, the developer was a trust and it acquired a property with the intention of subdivision and resale. The trust registered for GST on the basis that it was conducting a taxable activity involving the purchase, subdivision, refurbishment and sale of high-end residential properties. Due to a lack of working capital and a downturn in the property market the subdivision was eventually abandoned and the property was resold, undivided and undeveloped, back to the original vendor (and second mortgagee). The trust has not undertaken activity since the sale of the property.

Inland Revenue did not think the activities undertaken by the trust amounted to a taxable activity.

Although the property was eventually resold back to the original vendor undivided and undeveloped, the TRA held that the trust had been 'continuously' engaged in a taxable activity for the relevant period. In particular, it held the activities undertaken by the trust (such as consideration of the development potential, the purchase of the property, setting up the purchase and ownership structure, management time, dealings with real estate agents, refurbishment and surveying work) took the activities beyond the preparatory stage and amounted to a taxable activity. The level of activity carried out by the trust was sufficient for there to have been an activity that was carried on continuously for the relevant period.

An important point is that the TRA concluded the trust had commenced its taxable activity upon the purchase of the property. This is of interest as we are aware Inland Revenue has sometimes asserted the purchase of a property with the intention to conduct a taxable activity does not amount to a taxable activity.



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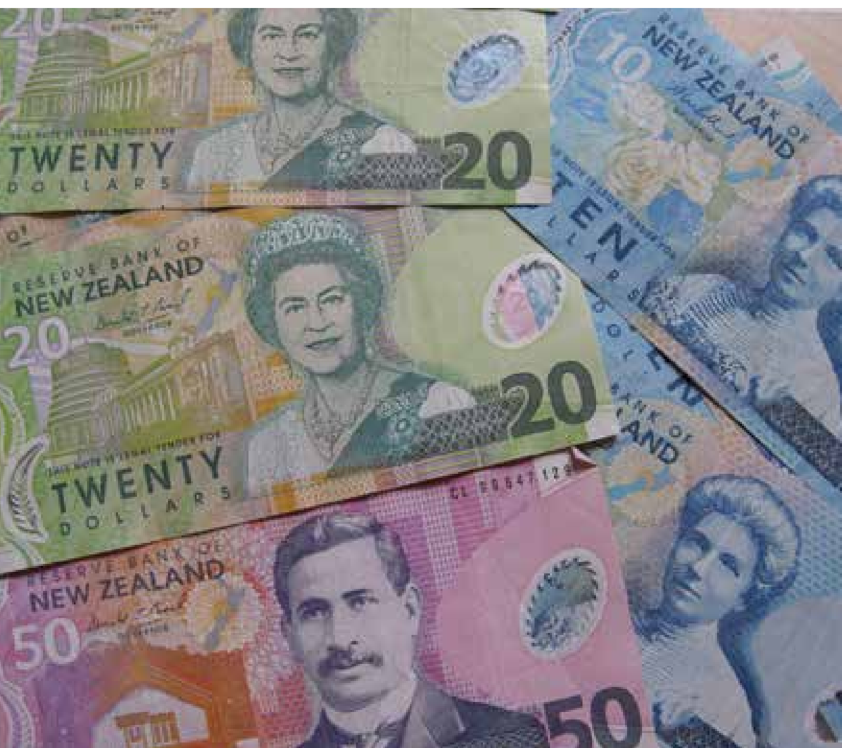
Inland Revenue Compliance Focus 2012 – 13

Inland Revenue recently released its compliance focus report, 'Helping you get it right – Inland Revenue's Focus 2012-13'. Similar to last year, Inland Revenue's compliance activities are grouped under four key themes.

They are:

- Everyone pays and receives the right amount.
- Inland Revenue receives the right information at the right time.
- Everyone files and pays on time.
- Inland Revenue provides confidence and certainty to its customers.

This year's focus is wide ranging – from international tax and complex financing transactions to the hidden economy and fraud. There is also a continued focus on the integrity of the GST (and remuneration) systems and processes used by central and local government.



As a group, central and local government and their entities collect over a quarter of the GST take[1]. It is therefore easy to see why Inland Revenue has continued to have a focus on ensuring central and local government are getting their GST obligations right. In particular, with the public sector undergoing significant structural and organisational change, Inland Revenue is concerned that such changes may pose an increased risk of system and process errors which can result in the incorrect amount of GST being accounted for.

We encourage central and local government organisations to consider conducting self-reviews of their systems and processes to check that they are meeting their GST obligations. In the event that errors are discovered, a voluntary disclosure may be made to Inland Revenue. Being proactive in this way will usually result in a more favourable outcome compared to Inland Revenue identifying errors in the course of an audit.

Inland Revenue is also paying particular attention to property transactions. Inland Revenue's monitoring and alert system notifies them when properties are transferred and, in some cases, when they are marketed. Inland Revenue has specifically noted that zero-rating of commercial property transactions between GST-registered entities has reduced the risk associated with these transactions. However, Inland Revenue will check for future changes of use or properties reverting to non-registered ownership as GST may be payable in these situations.

1 http://www.ird.govt.nz/aboutir/reports/compliance-focus/compliance-focus-2010-11/government/compliance-gst.html

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Do you import goods into New Zealand?

The administrative penalty regime available to New Zealand Customs has been extended to include GST errors.

A number of changes were made to the administrative penalty regime in the Customs and Excise Act 1996 with effect from 4 June 2012.

Customs has the power to impose penalties for errors made in relation to import entries. In a significant change in policy, the penalties are applicable even if there is only GST payable to Customs on importation.

Generally, importers who are GST-registered and use imported goods for making taxable supplies are able to claim back any import GST payable to Customs via their GST returns. Before the changes took effect the maximum penalty applicable to goods subject to GST only on importation was $50 per entry. This reflected the fact that in most circumstances where there was only import GST payable, errors made in relation to import entries did not result in a reduced tax take overall.

Following the changes, penalties will be calculated based on 20%, 40% or 100% of the shortfall (capped at $50,000 per import entry) depending on the severity of the offence. A minimum penalty of $200 will be imposed.

As a result of the changes, the maximum penalty per import entry for goods which are subject to both duty and GST on importation, has increased from $10,000 to $50,000. Businesses which import goods into New Zealand should review procedures for valuing and classifying goods for Customs purposes. Care should be taken to ensure that the import entry is accurately completed and specifically in relation to:

- tariff classification
- valuing the goods for Customs purposes (including making relevant adjustments to the transaction value to take account of for example, royalties)
- transportation and insurance costs.

It is likely Customs will seek to impose an administrative penalty if the error results in an underpayment of duty or GST, or the entry is otherwise 'materially incorrect'.

Care should be taken to ensure that the import entry is accurately completed.

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Offshore online shopping

Online shopping is rapidly increasing in New Zealand. In a recent PwC Australia and New Zealand online shopping survey, it was revealed that 1.9 million New Zealanders are now buying online and will spend NZ$3.19 billion online in this year alone.

It is expected that figure will grow by close to 15% annually over the next four years. The survey also found that 35% of all online purchases made by New Zealand shoppers in the last year were through international websites, which equates to NZ$1.12 billion being sent overseas.

Currently, private imports of goods with a value of less than $400 are generally exempt from GST and customs duties. That is, when a New Zealand shopper purchase goods from a foreign online retailer, for example Amazon, that foreign retailer does not have to account for the 15% GST that all New Zealand retailers are subject to and so can effectively offer a lower price on those goods.

Although many factors affect offshore and domestic prices, the current GST rules create an advantage for the offshore retailer.

It is also worth reflecting on the amount of GST foregone through offshore online shopping. With the Government working hard to get back to surplus, the estimated $168 million of GST on this year's offshore spend would assist achieving their target.

The current rules cause a distortionary effect and run counter to the broad-based (limited exceptions) design of New Zealand's GST rules.

We believe effort needs to be put into investigating whether there are more efficient ways of collecting the import GST and duty.

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9th Edition ADLS/REINZ Real Estate contract

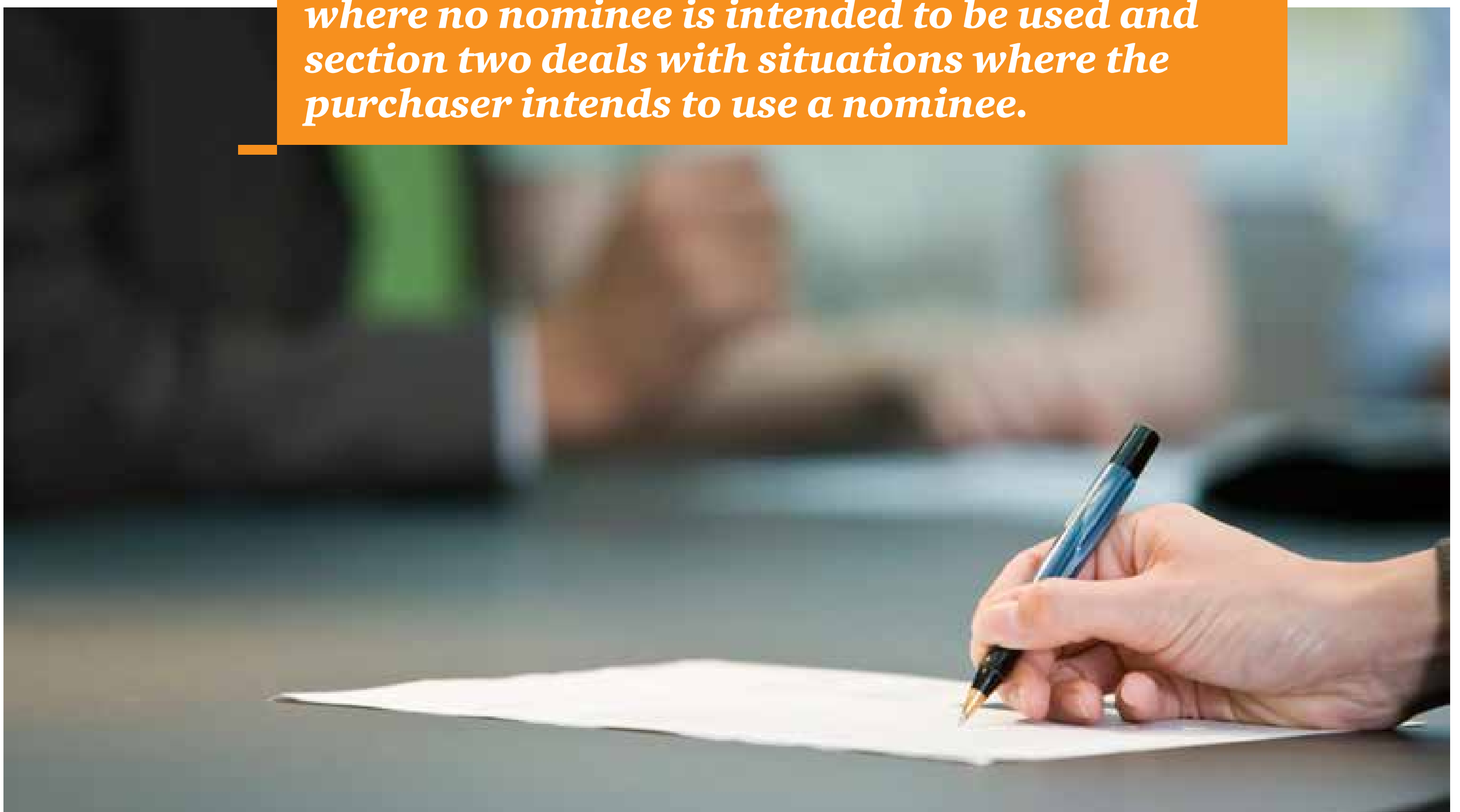
In July 2012, ADLS and REINZ released their latest edition of the ***'Agreement for the Sale and Purchase of Real Estate (9th edition)'.***

In terms of the GST position, matters of note for businesses and GST practitioners are:

Revamped definition of 'Default GST'.

References to additional defined terms in the GST Act such as 'goods', 'principal place of residence', 'recipient' and 'registration number'.

A revamped Schedule 2 dealing with the GST information relating to compulsory zero-rating (CZR). The Schedule is now divided into two parts – section one deals with situations where no nominee is intended to be used and section two deals with situations where the purchaser intends to use a nominee.



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September 2011 Tax Bill receives its second reading

In early August 2012, the Taxation (Annual Rates, Returns Filing, and Remedial Matters) Bill, first introduced in September 2011, received its second reading. As reported in previous GST Directs, the most significant GST changes contained in the September 2011 Bill relate to:

- An extension of the GST base to apply to charges for the late payment of an account (unless certain exclusions apply).
- Measures designed to prevent GST deductions being claimed in relation to expenses not paid if a liquidator or receiver changes from a payments to invoice basis of GST accounting.

In our June 2012 GST Direct we covered a number of practical issues in relation to the late payment fees proposal. Many businesses have both late interest and fixed dollar (flat fee) late fees applicable, as well as both prompt payment discount and late fee terms. These businesses will now need to grapple with the proposed changes and consider systems, contract and pricing issues. New interpretation issues will also arise. We eagerly await Inland Revenue's further guidance in relation to this area.

We remind our readers that the GST position on late fees isn't new but it's about to be turned on its head with retrospective effect. In a 2003 report, officials commented on GST and fixed dollar (or flat) late fees and observed that GST should be determined on ordinary principles, ie. there has to be a nexus between the payment and the supply. On ordinary principles amounts paid for late payment in breach of contract are damages and not consideration.

We remind our readers that the GST position on late fees is not new but it's about to be turned on its head.

Various legislative rules confirm these amounts to be damages as a remedy for an unpaid seller. Businesses have rulings from Inland Revenue confirming GST does not apply. All this is about to change.

In a welcome development, the September Bill will make a number of clarification changes that will improve the application of the existing GST laws in practice. Some of these measures will be back dated to April 2011.

These include:

- clarifying the definition of land for CZR purposes
- inserting a new section 11(8D) to provide that an assignment or surrender of an interest in land is covered by CZR
- clarifying how CZR applies to leases with lumpy payments
- clarifying the transitional rules in relation to the old and new rules for apportioning GST deductions
- clarifying the grouping, nomination and simultaneous use rules.

On 14 August 2012, a Supplementary Order Paper (SOP) to the September Bill was introduced and will further amend the GST Act to remedy supposed asymmetry in the GST treatment of premiums for and receipts under a contract of insurance. The asymmetry has arisen due to the application of the reverse charge rules in situations involving non-resident insurers. The amendment will be backdated to 1 January 2005 being the application date of the reverse charge. We are pleased to see this amendment as it confirms the position applied in practice.

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Legislative certainty/clarity

'The GST is just a simple tax'

As discussed earlier, Inland Revenue has released its statement 'Helping you get it right – Inland Revenue's compliance focus 2012 – 2013'. On page 26 of their document they state 'we provide confidence and certainty for our customers', and 'our customers need to have certainty about what they need to do to comply'. ***We agree.***

Let's test the statement against Inland Revenue's actions in relation to just one current, 'live', issue – how the GST grouping rules work in relation to the compulsory zero-rating of land transactions.

Example:

Say there are three companies in a group. Two are GST-registered and one is not registered. All three entities enter into an agreement to dispose of assets to a GST-registered purchaser. One of the GST-registered group companies is selling an interest in land. The other registered group company is selling non-land assets. The non-registered entity is also selling an interest in land. There is a single agreement with the multiple vendors selling to a single purchaser.

Question:

Are all of the sales subject to CZR, or just the sale of the land interest made by the one registered vendor?

The answer turns on how the grouping rules fit within the GST Act as a whole. By this we mean there are two possible approaches.

1. The grouping rules are just a simplification measure, intended to reduce the compliance costs of groups, by permitting a single return instead of multiple returns.

2. They are intended to treat the group as a single 'consolidated' entity, called the 'representative member'.

Under the first option, only the sale by the GST-registered group member can be zero-rated. The sale by the non-registered member is outside the scope. This is notwithstanding the fact that all transactions (except the latter) are booked in the return lodged by the representative member.

Under the second option, the answer to our question would be that all transactions are zero-rated under CZR, including the sale by the non-registered vendor.

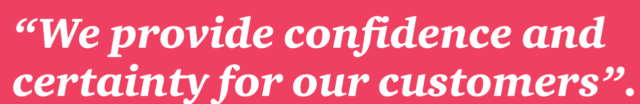
Legislative certainty/clarity 'The GST is just a simple tax'

The Inland Revenue Officials Report to the Finance and Expenditure Committee on the September 2011 Bill, which awaits its third reading, discusses an amendment which attributes section 78F statements issued by/to a member to be issued by/to the representative member of a GST group.

Inland Revenue advised the FEC that 'this will ensure the information is treated as being given and received by the person that is actually registered for GST and will be completing the requisite returns'.

This could imply that transactions by or to a non-registered member will be attributed to the registered representative member – a consequence being application of CZR to a transaction which, absent the group, would be outside of the scope of the tax. Is this an intended outcome? And where does it leave taxpayers who are trying to answer the earlier questions? This issue also existed before CZR was introduced, and arose when a GST group with separate vendor entities (each owning part of the business) attempted to apply the going concern zero-rating rules when selling to a single purchaser.

This article is not intended to fully analyse the position, rather we simply highlight the importance of Inland Revenue's statement in its compliance focus document. There are many such examples.



"We provide confidence and certainty for our customers".

Inland Revenue

"Our customers need to have certainty about what they need to do to comply".

Inland Revenue

FS Corner

Making the B2B election

The business-to-business (B2B) financial services GST regime has been in place since 2005. It is an elective regime which, broadly, allows a supply of financial services to be zero-rated where the recipient of the financial service makes at least 75% taxable supplies during a 12-month period. This is beneficial for financial service providers as it allows them to claim greater input tax.

Election into the regime requires written notice to be given to the Commissioner. The legislation does not permit retrospective elections into the B2B regime. We are aware of several instances of financial services suppliers registering for GST and applying the B2B rules without providing a separate election notice to the Commissioner. This oversight could result in adverse consequences such as the denial of input tax deductions and the prospect of having penalties and use-of-money interest imposed.

For those considering entry to the B2B regime, remember to:

- provide a written notice to Inland Revenue electing into the B2B regime
- retain a copy of the election notice
- retain a copy of Inland Revenue's confirmation of the election.

This is beneficial for financial service providers as it allows them to claim greater input tax.