KPMG
cutting through complexity

Beyond borders

A New Zealand tax guide for internationally mobile people and business

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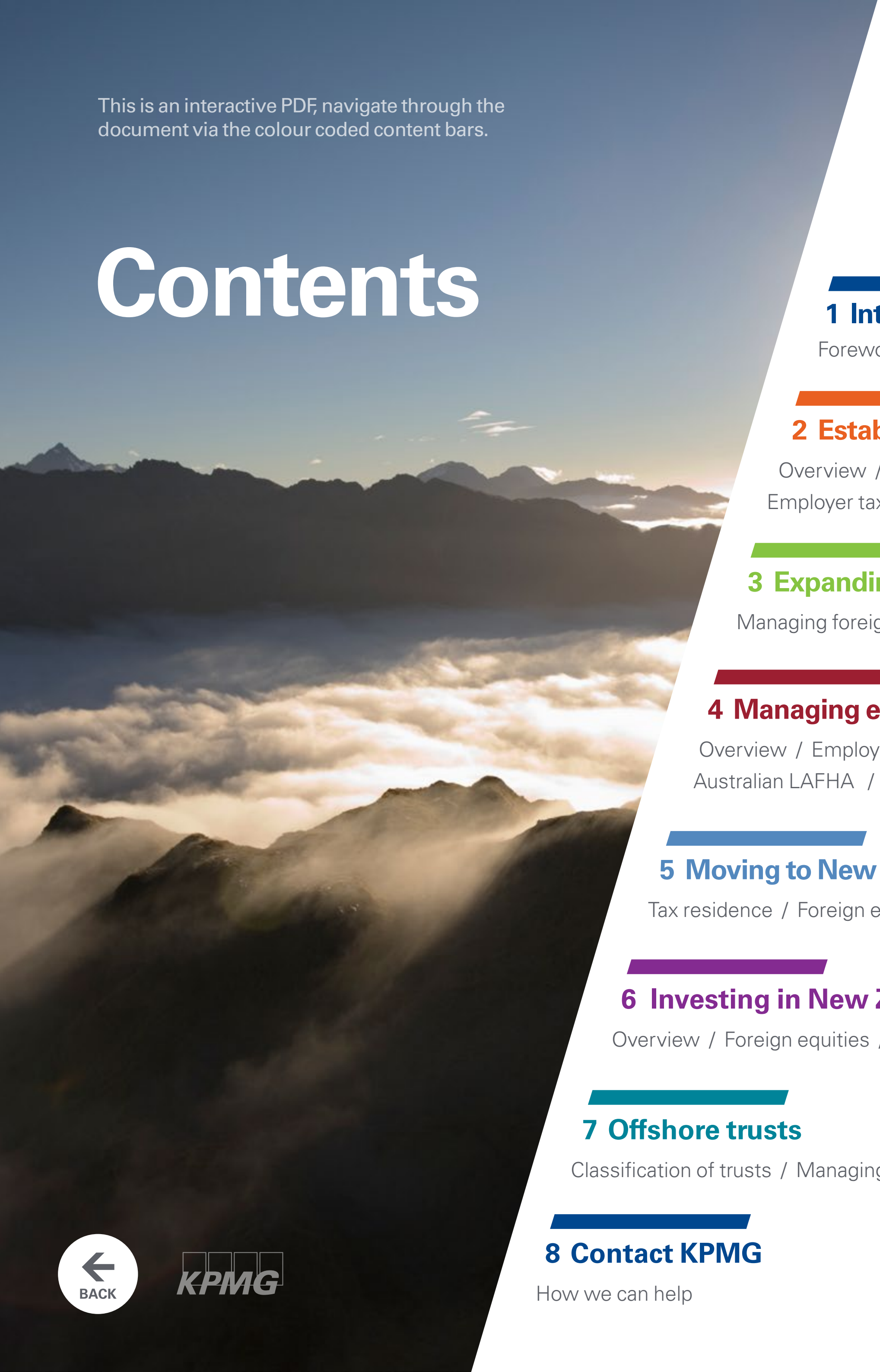

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Introduction

“When you travel, remember that a foreign country is not designed to make you comfortable. It is designed to make its own people comfortable.”

Clifton Fadiman

1A | Foreword

Tax systems rarely have much regard for the comfort of foreign visitors. Given that tax rules are different in each country – it can be one of the more complex and bewildering parts of trying to relocate, or do business, across a border.

Unexpected taxes, penalties, interest, and other tax hooks all lie in wait for the unsuspecting.

This book has been designed to help people – whether individual or running a business – who are not familiar with New Zealand tax. It also provides information to New Zealand companies looking to expand offshore, or managing a mobile workforce.

It is not going to make you a tax expert (leave that to us), but it will highlight some of the key issues that you need to be aware of. It will also arm you with the right questions to ask your KPMG advisor.

If you are coming to New Zealand on behalf of KPMG New Zealand, we welcome you to this part of the world. We look forward to helping make your transition here as comfortable as possible.

1B | Lets get started

International mobility and business is vitally important to the New Zealand economy and future prosperity. This includes individuals or businesses coming to New Zealand, and New Zealanders and their businesses broadening their horizons offshore.

At KPMG, we recognise the need to help smooth the process of investing overseas, and attracting offshore capital to New Zealand. Too often, effort and energy can be absorbed by dealing with regulatory and tax requirements, instead of being focussed on the main purpose - whether that is growing your business, or relocating your family and career.

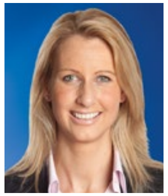
Our objective is to take these worries away, freeing you up to focus on what is important to you.

I am delighted to present this Beyond Borders publication as a guide to help inform you of some of the key issues you might face as you move to New Zealand, or expand beyond our borders. This booklet is aimed at providing some initial information and to arm you with the key questions that might need to be considered to smooth your path.

Beyond Borders is broken into chapters focussed on specific activities:

- Businesses coming to New Zealand may find chapters 2 & 4 most relevant.
- New Zealand business expanding offshore should consider chapters 3 & 4
- Individuals relocating to New Zealand will find most interest in chapters 5 & 6, and if you are a beneficiary of a trust chapter 7.

What ever your endeavours, I wish you well.



Rebecca Armour
Auckland
Tax - Director
KPMG New Zealand

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Establishing a business in New Zealand

Is your business tendering for a contract, or delivering a project in New Zealand? Or are you sending staff to New Zealand to open an office?

This chapter provides an overview of the various tax obligations you might encounter.

2A | Overview

YOU NEED TO KNOW

- Whether your business activities will be taxable and, if so, to what extent
- Whether to use a subsidiary or a branch in New Zealand
- How to structure your contracts and supply chain to minimise the activities taxed in New Zealand
- How your employees' activities impact on the tax status of the business

Whether you are tendering for a specific project, or opening an office in New Zealand, you'll need to be aware of your tax and financial reporting obligations.

Failure to consider tax and compliance costs could have a significant impact on the profitability and price of your contract, or your ability to carry on business efficiently here. Good planning – and being well-advised – will make all the difference.

The duration and nature of your activities will largely determine whether you are taxable in New Zealand. But the extent to which profits are taxable, and the reporting obligations the business will have, can be influenced to an extent. KPMG can advise on the most effective ways to manage your legal structure, operational disciplines, and supply chain.

2B | Income tax

YOU NEED TO KNOW

- Whether your activities create a ‘permanent establishment’
- How to manage your New Zealand tax exposure
- How to manage withholding tax that will be deducted from gross contract payments

WHAT IS TAXED

Under the New Zealand tax system, **non residents** are taxed only on their **New Zealand-sourced income.** This includes the profits from a business carried on, or a contract performed, in New Zealand.

The corporate tax rate is 28% at the time of writing.

WHEN DO YOU BECOME TAXABLE

If your business is based in a country that has a double tax agreement (DTA) with New Zealand, you will be taxable in New Zealand if the activities are carried on here through a ‘permanent establishment’.

Whether a permanent establishment is created will depend on the specific DTA. Usually activities carried on for more than six months are likely to create a permanent establishment. Some activities do not create a permanent establishment because they are not core to a business income-earning activity. An example of this would be having a presence in New Zealand only to gather information about opportunities, rather than securing and filling those orders.

2B | Income tax

MANAGING YOUR EXPOSURE

A non-resident is taxable only on profits derived from New Zealand. This means the structure of a contract can significantly reduce your exposure to New Zealand tax.

The choice between operating as a branch or subsidiary can also impact on the attribution of income to New Zealand, and your financial reporting obligations. These are discussed in later sections.

NON RESIDENT CONTRACTORS TAX

If you are a non-resident providing services in New Zealand, payments received may be subject to a withholding tax (referred to as 'non-resident contractors tax').

If you do nothing about this, 20% of the gross payment will be withheld by your customer. If you are not taxable, or if you can establish that a lower withholding is appropriate, you may be able to obtain an exemption certificate or reduced rate certificate from Inland Revenue.

2C | Personal income tax

YOU NEED TO KNOW

That employees will usually become taxable if they are in New Zealand for more than either three or sic months

That an employee's tax status can alter your tax obligations as an employer

That extending beyond six months unexpectedly can create problems

EMPLOYER'S OBLIGATIONS

A non-resident individual is taxed in New Zealand on income from employment services performed here.

If an individual is in New Zealand for less than three months, they are likely to be exempt from tax. Also, if they are here for 183 days or less in a 12-month period, they may be relieved from tax under a DTA (if they come from a country that has a DTA with New Zealand).

These exemptions are important for both the individuals and the business employing them. If the individual is liable to tax in New Zealand, their employer will have an obligation to deduct PAYE (salary withholding tax). It is important that employers are aware of their employees' movements, as prior visits, or remaining in New Zealand for a holiday, could alter their residence and/or liability and, in turn, the employer's obligations.

PERSONAL INCOME TAX RATES

Personal income tax is imposed at marginal rates up to 33%, as shown in the table.

Income band	Tax rate
$0 to $14,000	10.5%
$14,001 to $48,000	17.5%
$48,001 to $70,000	30%
$70,001 and above	33%

SHORT VISIT EXEMPTION (92 DAY EXEMPTION)

A non-resident employee may be exempt from tax on their employment income if they are:

- In New Zealand for 92 days or less in a tax year, and
- Employed and paid by a non-resident, and
- Subject to tax on the income in their home country.

2C | Personal income tax

DTA RELIEF (183 DAY EXEMPTION)

If an employee is resident in a country that has a DTA with New Zealand, they will typically be relieved from tax in New Zealand on their employment income if they are:

- In New Zealand for 183 days or less in any 12 month period
- Employed by a non-resident and their salary is not borne by a New Zealand permanent establishment.

MANAGING EXEMPTIONS

If an employee is exempt, you will not need to deduct PAYE. However, the exemption can often only be confirmed with the benefit of hindsight. If you expect your employees to be exempt, they can apply for a special tax code (STC). This will confirm that you do not need to withhold PAYE.

A STC may not be needed if everything goes according to plan. If there is any uncertainty, it is prudent to have the STC in case the person's stay extends and they cease to be eligible for the exemption. If a STC is not held, a voluntary disclosure may need to be made to Inland Revenue.

Inland Revenue may request a bond be held for the amount of the PAYE as a condition to issuing you with an exemption certificate from non-resident contractors tax (see earlier section on "Income Tax").

2D | Tax equalisation

YOU NEED TO KNOW

- Whether you should equalise your employees
- What it might cost

OVERVIEW

Tax equalisation is a way to ensure that your employees are no worse off financially when they are transferred to work in another country. Tax equalised employees are guaranteed a net salary – calculated after taking away the amount of tax that they would have paid in their home country if they had remained there. The employer then pays any actual tax that is payable in either country.

It's important that you fully understand the costs of tax equalising employees before adopting such a policy.

2E | Employer tax obligations

YOU NEED TO KNOW

- Whether your employees will be taxable
- If you need to deduct PAYE and pay FBT
- What other employer taxes may apply

WHEN ARE YOU REQUIRED TO DEDUCT PAYE

PAYE ("Pay as you earn") is New Zealand's salary withholding tax. If your employees are taxable in New Zealand, you will be required to deduct PAYE. This needs to be accounted for either monthly, or twice monthly depending on the size of your payroll.

The PAYE system is also used to manage and collect the ACC levy (Accident Compensation Corporation) and KiwiSaver contributions.

PAYE is imposed on any cash remuneration, expenditure on account of an employee and accommodation benefits that are taxable in New Zealand. Whether these amounts are taxable will often depend on the employee's personal circumstances.

FRINGE BENEFITS TAX

FBT is paid by the employer on non-cash benefits provided to employees. Fringe benefits include making a car available for private use, low interest loans, and benefits in kind, including benefits provided overseas. Contributions made to foreign superannuation schemes are subject to FBT.

With the exception of Australia, FBT is not dealt with by New Zealand's DTAs. This means there can be a mismatch in treatment and the potential for double taxation.

2F | Goods and Services Tax

YOU NEED TO KNOW

- That GST is charged at 15% on most goods and services
- That a non-resident entity may be required to register for GST
- Whether it is beneficial for you to register for GST
- That GST is imposed on imported goods
- Whether your contract adequately addresses GST

WHEN DOES GST APPLY?

Goods and Services Tax (GST) is imposed on most goods and services at 15%. New Zealand has few exemptions (mainly for financial services), but allows GST to be zero-rated (charged at 0%) on exports.

A non-resident is required to register if they expect to make supplies over $60,000 in a year, and if they have a fixed establishment in New Zealand.

A fixed establishemnt is a similar (but not identical) concept to permanent establishment.

Inland Revenue may consider a business to have a fixed establishment for GST purposes if the activities here exceed six months. In some cases, this could mean that you need to charge GST, even if you do not have a permanent establishment here.

SHOULD YOU REGISTER FOR GST?

Your contract should contemplate whether GST would be added in those circumstances, and who will bear the cost of GST (and customs duty, if any) on goods imported to perform the contract. This is essential if your client is a financial services provider (such as a bank) who cannot fully recover GST costs.

You may wish to register for GST voluntarily, especially if your costs include a significant New Zealand component. Registering for GST will mean you need to charge GST, but will allow you to claim back the GST on your expenses. For short term contracts, you may need specific terms in your contract to enable you to charge GST and register.

2G | Transfer pricing and customs

YOU NEED TO KNOW

- How transfer pricing rules will govern your taxable profit in New Zealand
- That a subsidiary offers greater certainty when allocating profits to New Zealand
- How to structure your operation and supply chain to manage your tax position

BRANCH OR SUBSIDIARY?

You might expect that a similar profit should be attributed to New Zealand regardless of whether you operate here through a branch of a non-resident entity, or establish a New Zealand subsidiary. In practice, however, a subsidiary provides greater certainty.

Transfer pricing rules deal with the pricing of goods and services between associated parties. The rules provide greater clarity around how to calculate the profits that are properly taxed in New Zealand. In contrast, the requirement to attribute income and expenses to a branch leaves greater uncertainty - and therefore greater risk of challenge from Inland Revenue.

SUPPLY-CHAIN PLANNING

A significant part of managing your New Zealand tax liability is about managing your supply chain and operational disciplines. If risk or functionality is in New Zealand, the transfer pricing rules will require the reward from those risks and functions to be in New Zealand.

If the functions and supply chain are split between New Zealand and overseas, it is important that this can be substantiated and is documented. It will also need to be reflected in the contractual terms between your business and the New Zealand customer.

CUSTOMS DUTY AND GST ON IMPORTS

If you will be importing goods into New Zealand, GST (and customs duty, if any) will be collected by New Zealand Customs Service. If you are registered for GST, you should be able to claim back this GST. If you are not registered, it could represent a significant cost. It is important that you confirm and manage this exposure - either by registering for GST, or having the New Zealand client act as the importer.

If you are the importer, you may also want to manage the cash flow impact of paying GST to Customs, but only claiming it back when your GST return is filed.

2H | Financial reporting

YOU NEED TO KNOW

- When to register with the Companies Office
- What information will need to be filed

WHAT IS REQUIRED?

Once you begin to carry on business in New Zealand, you will usually be required to register with the New Zealand Companies Office within 10 days.

A subsidiary is required to prepare accounts, have them audited and file them with the Companies Office. Accounts need to be filed within five months and 20 working days from balance date.

A branch has similar requirements, but in addition is also required to file the accounts of its parent entity (i.e. the non-resident company that has a branch in New Zealand). You should consider whether this level of disclosure is feasible and desirable. If not, a subsidiary may be preferred.

WHAT ARE THE PENALTIES?

Although the penalties for not meeting these reporting requirements generally start off quite minor, they can escalate to sanctions imposed on the directors personally. This is clearly something to be avoided.

3

Expanding offshore

This chapter discusses some of the tax issues that need to be considered before expanding into offshore markets.

3A | Managing foreign taxes

YOU NEED TO KNOW

- **What foreign taxes will be imposed**
- **What filing and compliance obligations you will face**

TYPES OF TAX

It is important to go into a new country with an open mind and open eyes. It is unwise to assume taxes will be anything like New Zealand. Overseas countries may have multiple layers of tax–federal, state, provincial, city, church (and that's just on income).

Taxes may also be imposed by way of GST or VAT, capital gains tax, payroll tax, sales tax, stamp duty, transfer tax, property tax, social security, medicare and inheritance or estate taxes. Any of these could potentially come into play.

As well as taxes imposed directly, there are withholding taxes to consider. It is common for withholding tax to be imposed on payments to non-residents. Typically, these might cover payments of interest, dividends and royalties, and payments for services performed in the country.

AVOIDING TAX LEAKAGE

Although withholding taxes are normally offset against any New Zealand tax payable on the income received, there can still be an extra cost caused by the multiple layers of tax. These layers can include a combination of taxes paid overseas, withholding taxes, and tax paid by the ultimate New Zealand investor. If managed poorly, they can add up to significantly more than the New Zealand tax that would be paid on the same income.

When setting up a business overseas, it is useful to model the expected tax liability as part of your budgeting process. It will also help you decide on a business structure.

3B | Business structure

YOU NEED TO KNOW

- That tax will become a major distraction (and cost) if not properly managed
- That by adding a single border, you more than double the tax issues
- What impact your legal structure, funding and supply chain will have on tax efficiency
- How profits and gains will be repatriated

TAX IMPLICATIONS

When expanding your business into a new jurisdiction, the legal structure of your business could influence the tax liabilities faced by your business, your employees and you. The structure can also have an impact on how you repatriate future profits, and the tax you pay to do so.

OTHER IMPACTS

Tax is not the only consideration. The legal structure through which you operate can also determine your financial reporting and regulatory obligations. It is also advisable to consider what your exit strategy might be in the future, and whether the intended structure facilitates or inhibits such an exit.

Legal structure can also influence your immigration status. In some countries, it makes a difference whether you are looking to enter the country as a business representative, to establish a local business entity, or as an employee of a New Zealand company.

3C | Equity compensation

YOU NEED TO KNOW

- **How equity compensation plans can help you recruit, retain and reward without cash burn**
- **Why the primary focus should be on the commercial objectives, with tax secondary**

THE BENEFITS

Setting up in a new country is rarely easy, or cheap. It's quite likely that you will be faced with the challenge of trying to secure good senior staff without burning through cash. This is one scenario when equity compensation (a share plan) should be considered.

Properly structured, a share plan can help you to recruit, retain and reward senior staff without depleting your much-needed cash reserves. A well-designed scheme can also help to reduce the risk of recruitment and remuneration decisions by ensuring that reward only comes with proven performance.

THE OPTIONS

Share plans can take many different forms – upfront share grant, options, restricted shares – and can be funded different ways. Each approach will have a different commercial outcome. Will your employee be exposed to upside and down of share price movements? Will they contribute capital or effort? What will be the performance triggers? They may also have different tax outcomes – is the benefit taxable, if so is tax payable upfront or deferred?

Tax efficiency is important when designing a share plan (especially if cash burn is one of the reasons for considering it in the first place). Tax should not, however, take priority over achieving the scheme's real purpose to secure and retain good staff. It should be a good balance between commercial and financial drivers.

3D | Corporate governance

YOU NEED TO KNOW

- That good governance is about building the value of your business in a sustainable way
- How an advisory board, and/or independent directors, might assist your business
- Whether your business' operations and governance are robust enough to manage the rigors of overseas expansion

ARE YOU PREPARED?

If you are expanding your business offshore, things are about to get more complicated. Now is a good time to consider whether you have appropriate corporate governance in place.

Expansion offshore is a significant step – and an opportunity to make sure that you have your ducks in a row for the future. A sound governance framework will also help avoid the missteps that often occur when expanding overseas – e.g. should you focus on one market at a time? How do you make sure compliance and regulatory requirements are satisfied without distracting from the main business? What is the best use of talent, funds and resources? KPMG has specialist governance advisors who can help you navigate all these issues.

4

Managing expatriates

Expatriates are coming under greater scrutiny by tax authorities around the world. New Zealand is no exception. This chapter looks at some of the current issues for expatriates, and Trans-Tasman business travellers.

4A | Overview

YOU NEED TO KNOW

- **That tax authorities are taking greater interest in expatriates and business travellers**
- **That greater pressure is being put on protecting tax revenues**

A POINT OF FOCUS

As Governments seek to remedy fiscal deficits, tax authorities around the world are looking for additional sources of revenue.

In New Zealand, we're seeing greater focus on areas of the economy where tax could be in dispute – including protecting national borders – as each country looks to protect its portion of shared taxes.

An area that is getting a lot of attention internationally is extended business travellers, and short-term assignees. These are individuals where the taxing rights of each country are finely balanced, and disputes commonly arise.

KPMG New Zealand's IES team (International Executive Services) works closely with both employers and expatriates. We help manage the tax issues that arise from doing business across borders, and managing an internationally mobile workforce.

4B | Employee transfer versus contract

YOU **NEED** TO **KNOW**

- **That the structure of a secondment will dictate tax outcomes**
- **That three and six months are significant tipping points for personal tax**
- **That project extensions beyond six months can create significant tax issues**

WHAT'S THE DIFFERENCE?

How a secondment is structured will influence the tax treatment of both the employee and the businesses involved.

Essentially, the options are **a transfer** or **a contract.** Transferring the employee means creating an employment relationship with the overseas (host) business, and removing the home business from any involvement. Alternatively, the home business can contract to perform services for the host business and send an employee to perform those services.

Often it is not clear which of these options is being implemented, but the distinction is important to determine the tax obligations.

THE TAX IMPACT

The contract scenario is less likely to result in the employee being taxable in the host country – if they are there for less than six months and can claim relief under the DTA. On the other hand, the business needs to consider whether it is taxable in the host country. The transfer scenario is more likely to make the employee taxable in the host country, but reduces the risk for the home country business.

Often the decision of structure will turn on the expected duration of the secondment. Three or six months will be an important tipping point for the employee's taxes, and for your business' obligations and liability.

4C | Accommodation benefits

YOU NEED TO KNOW

- **Inland Revenue is toughening up on tax-free accommodation benefits**
- **That Inland Revenue's interpretation could impact on short term business travellers**
- **How Inland Revenue's position impacts your assignment costs**

THE BACKGROUND

New Zealand taxes the accommodation provided to employees, regardless of whether it is provided directly or reimbursed. For many years, it has been widely accepted that there is no taxable benefit if the employee is maintaining a home elsewhere.

THE CURRENT SITUATION

Recently, Inland Revenue has reversed its interpretation claiming that its prior (and long held) interpretation was incorrect. Nothing has been published, but the issue is being adjusted on audit.

The Inland Revenue's interpretation is likely to have a much wider reach than intended. There is the potential for even short term accommodation to be taxable.

Although Inland Revenue's interpretation may not be accepted by the courts, it first has to be litigated. In the meantime, employers need to consider the cost of accepting Inland Revenue's interpretation, or the cost of defending against it.

4D | Trans-Tasman projects

YOU NEED TO **KNOW**

- **That a project will be taxable in Australia if services are performed there for more than 183 days in any 12 month period**
- **That assisting an Australian associate can create a tax liability immediately**

WHEN DOES TAX LIABILITY ARISE?

If a New Zealand business performs services in Australia (or vice versa) for more than 183 days in a 12 month period, a permanent establishment is deemed to arise. This makes the New Zealand business taxable in Australia. Although the 183 days are measured across a single project, it aggregates time spent on the same project by associated entities.

In the ATO's view Australian associates are included. This means a New Zealand business assisting with an Australian project could be taxable – even if only assisting for a few days – if the project itself extends for more than 183 days. Having a permanent establishment creates a tax obligation for both the business and the employees.

SHORT SECONDMENTS

If the employee is seconded temporarily to Australia, and is there for less than 90 days, the employee may be relieved from Australian tax on employment income under the secondment exemption in the DTA. This applies even if the business has a permanent establishment.

POLICIES AND PRACTICES

It is important that a business tracks its people and projects, so they know when tax obligations might arise.

KPMG can help develop policies and practices to deal with these issues and to manage your exposure to overseas tax systems.

4E | Australian LAFHA

YOU NEED TO KNOW

- **That changes have been made to the Australian LAFHA from 1 October 2012**
- **That New Zealanders will probably cease to qualify for tax-free LAFHA**
- **How this will impact your costs**

THE REQUIREMENTS

The Australian Government has proposed changes to the taxation of living away from home allowances (LAFHA). The changes are proposed to take effect from 1 October 2012. The proposed changes include a requirement that a home be maintained in Australia for LAFHA concessions to apply. This means that somebody temporarily in Australia from New Zealand may become taxable on a LAFHA.

For businesses transferring staff into Australia, and paying LAFHA, this change is likely to increase the cost of assignments.

4F | Australian temporary residents

YOU NEED TO KNOW

- **That Australia has a temporary residents' tax exemption on foreign investment income**
- **That the ATO has determined that New Zealanders do qualify**

THE REQUIREMENTS

Australia has a tax concession for foreign investment income of temporary residents.

New Zealanders generally qualify for the concessions without time limit (unless they become an Australian citizen or permanent resident, or marry one). Other temporary residents qualify only for as long as they hold a temporary visa.

A CONTENTIOUS ISSUE

In a 2011 audit case, the ATO adopted an interpretation that New Zealanders would cease to be eligible for the concession if they left Australia even for a short business trip or holiday. Although finally settled in favour of New Zealand citizens, this is a cautionary illustration of how tax authorities are aggressively pursuing revenue.

After a period of consultation, the ATO and Treasury finally issued a Taxation Determination. This confirmed that the ATO would accept that New Zealanders qualify for the temporary resident tax concession.

5

Moving to New Zealand

If you are coming to live in New Zealand, there are a few things you need to know about your tax position. This chapter will provide you with an overview of those essential facts.

5A | Tax residence

YOU NEED TO KNOW

- **That New Zealand taxes its residents on their worldwide income**
- **That tax residence is not the same as your immigration residence status**
- **Whether you are eligible for the transitional residents' exemption**

TAX RESIDENCE

When moving to New Zealand, the single biggest influence on your tax position will be your status as a New Zealand tax resident. A tax resident is taxed on worldwide income, with a tax credit allowed if taxes are paid overseas. In contrast, a non-resident is taxable only on New Zealand-sourced income.

Tax residence is determined by meeting one of two tests.

The first test is a simple count of days. The second test considers whether you have an enduring connection to New Zealand, i.e. a permanent place of abode. These tests are outlined in more detail below.

DAY COUNT TEST

If you are in New Zealand for more than 183 days in any 12 month period, you are tax resident from the first of those days. It's important to note the period in question is any rolling 12 month period – not the tax year or calendar year.

You are considered to be in New Zealand for 'the day' if you are here for any part of the day.

PERMANENT PLACE OF ABODE

The permanent place of abode test is not as clear-cut as the day count test. Whether you have established a 'permanent place of abode' is determined by looking at your circumstances as a whole, and whether you have an enduring relationship with New Zealand. Factors considered include economic, family and social ties to the country.

This test is determined by case law, and will depend on your specific circumstances. As a consequence, this is a constant source of tension between taxpayers and the Inland Revenue.

5A | Tax residence

TRANSITIONAL RESIDENCE

A special concession is available to transitional residents. This group includes new migrants, and New Zealanders returning after at least 10 years. A transitional resident is exempt from tax on offshore investment income for four years. This creates a period in which overseas investments can be reviewed and restructured. As a transitional resident you have the opportunity to implement tax planning strategies to help ensure your holdings are tax efficient and to minimise future tax compliance obligations. Your KPMG adviser can help with this.

IMPLICATIONS OF BECOMING TAX RESIDENT

The following sections discuss the main tax regimes that apply to foreign equities and financial arrangements if you are not eligible for the transitional resident exemption, or after the transitional period expires.

5B | Foreign equities

YOU NEED TO KNOW

- **That the FIF regime taxes foreign equities on an assumed 5% return per annum**
- **That other calculation options are available and might give you a better result**
- **Whether exemptions apply to your shares**

FOREIGN INVESTMENT FUNDS

Dividends derived from New Zealand shares are taxed. Any gain on sale is only taxed if held on revenue account - for example, if shares are actively traded or held as part of a business. Some Australian shares that are listed on the ASX are exempt from the FIF regime and taxed in the same way as New Zealand shares (this exemption is discussed below).

Foreign equities are subject to the foreign investment fund (FIF) regime. The FIF rules calculate an amount of income to be attributed to the shareholding. Several methods are available to calculate the attributed income, but the default (and most commonly used) method is the fair dividend rate (FDR) method.

If income is calculated under the FIF regime, this is the only income that is taxed from the foreign shares. This means, if income is calculated under the FDR method, dividends and gains are not separately taxable.

FAIR DIVIDEND RATE METHOD

The FDR method calculates income as 5% of the market value of shares held on 1 April at the start of each income year. Only the 5% is taxed, even if actual income and gains from the shares exceeds this amount.

The 1 April measurement date for calculating the market value of investments subject to tax means that shares acquired during the tax year will not be taxed in the first year of ownership. Conversely, shares sold during the tax year will be taxed as if they were held for the full year. So the timing of transactions around the end of the tax year (31 March) is important.

Anti-avoidance rules ensure that shares are not bought and sold within a tax year to avoid tax (by avoiding the 1 April measurement date).

ALTERNATIVE METHODS

If the total return (income and gains) across an individual's portfolio of foreign shares is less than 5%, the comparative value method can be used instead of FDR. This taxes the actual dividends, as well as realised and unrealised gains or losses, derived from the shares. If your portfolio makes an overall loss, however, you cannot deduct or carry forward that loss.

5B | Foreign equities

MINOR TOTAL HOLDINGS

If the total cost of all foreign shares held is less than $50,000, income does not get attributed under the FIF regime. In this case, dividends are taxable.

AUSTRALIAN SHARE EXEMPTION

Shares are exempt from the FIF regime if they are shares:

- In an Australian resident company (not unit trust)
- Listed on the ASX
- Included in an ASX market index.

This accounts for approximately 450 to 500 of the top Australian shares. These shares are exempt from the FIF rules, but taxed on dividends.

5C | Financial arrangements

YOU NEED TO KNOW

- **That these rules apply to all financial arrangements, including bank accounts, debt securities, derivatives**
- **That the income taxed can include unrealised exchange gains**
- **Whether you are eligible for the cash basis concession**
- **That the cash basis concession only defers income**
- **How to manage the volatility created by these rules**

FINANCIAL ARRANGEMENTS

The financial arrangement rules calculate taxable income derived from financial arrangements. 'Financial arrangements' is a broadly defined term that includes all bank accounts, term deposits, bonds, debt securities and derivatives. The general intention of the rules is to tax the total economic return from the financial arrangements, spread over the life of the investment. For example, a USD bank account would give rise to income from both interest and a foreign exchange gain, or loss.

EXAMPLES FOR 2012 TAX YEAR

If held for the entire 2012 tax year (to 31 March 2012), the exchange movement from holding these currencies all give rise to a loss. Such a loss may be deductible, unless it fails as private expenditure.

Currency	Fx Loss	Currency	Fx loss
AUD	7%	EUR	12%
USD	6%	GBP	7%
SGD	6%	CHF	4%

If you have liabilities in these currencies, you will have a taxable gain!

5D | Financial arrangements

SPREADING INCOME

Income from a financial arrangement must be spread over the life of the arrangement, and complex rules direct how to do this. The consequence is that unrealised gains will typically be taxed on an annual basis. If your total holdings are under certain thresholds, there is a concession allowing income to be calculated on a cash basis, so only realised gains are taxed.

CASH BASIS CONCESSION

Income from financial arrangements can be returned on a cash basis if you meet one of the following criteria:

- $1,000,000 absolute value of assets/liabilities
- $100,000 absolute value of income/expenditure

In either case, the difference between cash basis income and accrual income must be less than $40,000.

Regardless of whether you benefit from the cash basis concession, you will be taxed on the total return from your financial arrangements. The cash basis is only a timing benefit. This means you need to keep records to enable the income to be calculated when the financial arrangement matures or is sold.

5E | Superannuation

YOU NEED TO **KNOW**

- **That foreign superannuation schemes may be taxed under the FIF regime**
- **That your distributions may be taxable, if your scheme is exempt from the FIF regime**
- **Whether your planned withdrawal or transfer will be taxed**

FOREIGN SUPERANNUATION

An interest in a foreign superannuation scheme is a FIF interest (outlined above), unless it meets specific exemptions.

A foreign superannuation scheme is broadly defined as a trust or company established for retirement savings. These rules will include most countries' employment-related superannuation schemes, although it will depend on their precise terms. It will typically include 401k plans from the US, and PEPs, SIPPs and ISAs from the UK.

POSSIBLE EXEMPTIONS

Other than Australian superannuation schemes, the most common exemptions are for certainemployment-related superannuation, or pension schemes. There are several criteria that must be met to apply these exemptions. Care must be taken with these exemptions – disqualification is easy, depending on the terms of the scheme.

Australian superannuation schemes are exempt from the FIF regime, provided they are one of four specified types of scheme that are regulated in Australia. In our experience, most Australian superannuation schemes qualify for the exemption. However, this is not necessarily a good thing.

5E | Superannuation

TAX AS A FIF OR ON DISTRIBUTION

If your superannuation scheme is subject to the FIF regime, you will be taxed annually on the underlying investment income (see section above on the FIF regime). If your scheme is exempt, you will most likely be taxed on distributions from the scheme – at least to the extent of earnings that have accumulated in the scheme over the contributions made by you and/or your employer.

It is important to keep this tax on distributions in mind when withdrawing funds from a scheme, or transferring funds between schemes. This includes QROPS (schemes approved for UK pension transfers – list here) transfers from the UK, but will soon (hopefully) be addressed for Australian superannuation schemes under the trans-Tasman portability rules.

PROPOSED CHANGES

Inland Revenue has released a discussion document on foreign superannuation. This proposes to change the taxation of lump sum distributions from foreign supperannuation schemes.

If implemented, a percentage of any lump sum withdrawl would be taxed. The percentage would depend on how long you have been in New Zealand prior to the withdrawl. Such schemes would then be excludes from the FIF regime.

5F | Your own business

YOU NEED TO KNOW

- That dividends from a foreign company will not be taxed if you are transitional resident
- That New Zealand does not tax capital gains on sale of shares
- Whether or not your company is a CFC
- Whether you exercise management and control in New Zealand

ARE YOU A TRANSITIONAL RESIDENT?

If you own a business overseas, you will need to consider how your move to New Zealand will impact on it.

If you are a transitional resident, you will not be taxed on foreign investment income for four years. This means foreign dividends, FIF income (discussed earlier) and CFC income (discussed below) are not taxed during this period. Any remuneration for services will still be taxable.

Even if you are not a transitional resident, New Zealand does not have a capital gains tax, so you will typically not be taxable on sale of shares in a business. This could be advantageous if you are planning to exit your business.

IS YOUR BUSINESS A CFC?

New Zealand's CFC rules tax income of a foreign company in the hands of its shareholders. A company is a Controlled Foreign Company (CFC) if it is controlled by five or fewer New Zealand residents, or if a New Zealand resident has de facto control. Shareholdings held by associated parties are aggregated when working out whether a company is a CFC. There is an exemption from attributing CFC income from certain active businesses carried on overseas.

MANAGEMENT AND CONTROL

A company is treated as resident in New Zealand if either the centre of management or director control is here. Both of these tests are fact-specific and the outcome will depend on how you operate. For example, holding board meetings overseas helps ensure director control is not exercised here – but will be of limited benefit if, in fact, decisions are made by conference call. Determining the location of the centre of management can be more difficult, as the answer may differ depending on whether day-to-day or senior management is considered.

The consequences of a company being tax resident in New Zealand can be significant. The company will become taxable on its worldwide income, subject to DTA relief and credit for foreign taxes, and dividends will no longer be considered to be foreign income for transitional residents.

6

Investing in New Zealand and offshore

This chapter provides an overview of the main tax rules applying to investments held by a New Zealand tax resident.

6A | Overview

YOU NEED TO KNOW

- That New Zealand does not have a capital gains tax
- That new migrants may not be taxed on foreign investment income for four years
- That different investment vehicles can result in different tax outcomes
- How your investments might be taxed when you are a tax resident

TAXING INVESTMENTS

New Zealand taxes the worldwide income of tax residents, and the New Zealand-sourced income of non-residents. Tax applies regardless of whether income is received in, or remitted to, New Zealand.

New Zealand does not have a capital gains tax. However, gains that might be considered to be capital gains are still taxed if they arise from financial arrangements (discussed below). This can also apply if you are a trader, or if the asset was acquired for the dominant purpose of sale.

Income derived from investments is added to your taxable income, and taxed at your marginal tax rate (maximum 33% for the tax year to 31 March 2013).

New migrants and New Zealanders returning after 10 years or more may be classified as transitional residents.

Transitional residents are exempt from tax on investment income derived from foreign investments. If you are eligible for the exemption, it lasts for four years from the time you become tax resident.

The rules applying to foreign equities and financial arrangements discussed in this chapter do not apply to non-residents.

6B Foreign equities

YOU NEED TO KNOW

- That the FIF regime taxes foreign equities on an assumed 5% return per annum
- That other calculation options are available and might give you a better result
- Whether exemptions apply to your shares

FOREIGN INVESTMENT FUNDS

Dividends derived from New Zealand shares are taxed. Any gain on sale is only taxed if held on revenue account - for example, if shares are actively traded or held as part of a business. Some Australian shares that are listed on the ASX are exempt from the FIF regime and taxed in the same way as New Zealand shares (this exemption is discussed below).

Foreign equities are subject to the foreign investment fund (FIF) regime. The FIF rules calculate an amount of income to be attributed to the shareholding. Several methods are available to calculate the attributed income, but the default (and most commonly used) method is the fair dividend rate (FDR) method.

If income is calculated under the FIF regime, this is the only income that is taxed from the foreign shares. This means, if income is calculated under the FDR method, dividends and gains are not separately taxable.

FAIR DIVIDEND RATE METHOD

The FDR method calculates income as 5% of the market value of shares held on 1 April at the start of each income year. Only the 5% is taxed, even if actual income and gains from the shares exceeds this amount.

The 1 April measurement date for calculating the market value of investments subject to tax means that shares acquired on or after 2 April will not be taxed in the first year of ownership. Conversely, shares sold on or after 2 April will be taxed as if they were held for the full year. So the timing of transactions around the end of the tax year (31 March) is important.

Anti-avoidance rules ensure that shares are not bought and sold within a tax year to avoid tax (by avoiding the 1 April measurement date).

ALTERNATIVE METHODS

If the total return (income and gains) across an individual's portfolio of foreign shares is less than 5%, the comparative value method can be used instead of the FDR. This taxes the actual dividends, as well as realised and unrealised gains or losses, derived from the shares. If your portfolio makes an overall loss, however, you cannot deduct or carry forward that loss.

6B | Foreign equities

MINOR TOTAL HOLDINGS

If the total cost of all foreign shares held is less than $50,000, income does not get attributed under the FIF regime. In this case, dividends are taxable.

AUSTRALIAN SHARE EXEMPTION

Shares are exempt from the FIF regime if they are shares:

- In an Australian resident company (not unit trust), and
- Listed on the ASX, and
- Included in an ASX market index.

This accounts for approximately 450 to 500 of the top Australian shares. These shares are exempt from the FIF rules, but taxed on dividends.

6C | Financial arrangements

YOU NEED TO KNOW

- **That these rules apply to all financial arrangements, including bank accounts, debt securities, derivatives**
- **That the income taxed can include unrealised exchange gains**
- **That the cash basis concession only defers income**
- **Whether you are eligible for the cash basis concession**
- **How to manage the volatility created by these rules**

FINANCIAL ARRANGEMENTS

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This means you need to keep records to enable the income to be calculated when the financial arrangement matures or is sold.

6D | Portfolio Investment Entities (PIEs)

YOU NEED TO KNOW

- That a PIE is a widely held collective investment vehicle
- That the maximum tax payable in a PIE (28%) is less than the top marginal rate (33%)
- That tax paid by an unlisted PIE on your behalf is a final tax (if paid at the correct rate)

WHAT IS A PIE?

Fund managers in New Zealand will typically offer managed funds that meet the requirements to be a portfolio investment entity, or PIE. Such funds must be widely-held and have restrictions on the minimum number of investors, the maximum interest those investors can hold, and the types of investments the fund makes.

If you invest in an unlisted PIE, you will need to advise the fund manager of your PIE tax rate (called the Prescribed Investor Rate, or PIR). This rate is determined based on your previous two years' income. The fund will then account for tax on your behalf.

Provided you have indicated the correct tax rate, the tax paid by the PIE will be a final tax. PIE income that is attributed to you will not need to be included in your tax return. The maximum PIE tax rate is 28%, so there may be a tax advantage to investing through a PIE.

Listed PIEs are taxed differently. They are taxed at 28% and impute dividends paid. The dividend is exempt, unless you choose to include it in your return. You would only do this if your tax rate was lower than 28%.

7

Offshore trusts

This chapter looks at the main issues associated with offshore trusts when coming to, or living in, New Zealand.

7A | Classification of trusts

YOU NEED TO KNOW

- **An offshore trust will be classified as either a foreign or non-complying trust**
- **The main consideration is the tax residence of the settlor(s)**
- **Distributions from a non-complying trust are taxed at 45% of any income or capital gains distributed**

FOREIGN OR NON-COMPLYING TRUST

An offshore trust that makes a distribution to a New Zealand resident beneficiary will be classified as either a foreign trust or a non-complying trust. The distinction is important because it determines both the amount of the distribution that is taxable, and the rate at which it is taxed. A trust is a foreign trust if no settlor of the trust is, or has been, tax resident in New Zealand. Distributions of income from a foreign trust are taxed at the beneficiary's marginal tax rate. Distributions of capital gains and corpus are tax-free.

If a settlor of the trust is resident in New Zealand, the trust may be a non-complying trust. Distributions of both income and capital gains from a non-complying trust are taxed at 45%.

7B | Managing trust status and distributions

YOU NEED TO KNOW

- **That an election needs to be considered when a settlor becomes resident**
- **How to manage distributions from offshore trusts to manage the beneficiaries' tax**

SETTLOR BECOMING NEW ZEALAND RESIDENT

If a settlor of a foreign trust becomes resident in New Zealand, an election must be made to bring the trust within the New Zealand tax system. Failure to do so will mean that the trust becomes a non-complying trust, with distributions being taxed at 45%. The settlor may also become liable to account for tax as agent of the trustee if any further settlements are made.

This election needs to be made within 12 months of the settlor become tax resident, or ceasing to be a transitional resident.

ORDERING RULES

Distributions from both foreign trusts and non-complying trusts are taxed depending on their composition – income, capital gains or corpus. The ordering rules dictate the composition of a distribution for tax purposes. These rules deem income and accumulated income to be distributed before capital gains. Corpus, or the capital of the trust, is the last to be distributed.

These rules can come into conflict with the actual composition of a trust distribution – for example, even if a beneficiary is only entitled to capital distributions, they may be deemed to receive income.

The rigidity of these rules means it is possible to manage the distributions to determine how income and capital are distributed to different beneficiaries.

NEED FOR HISTORIC RECORDS

If a foreign, or non-complying, trust makes a distribution to a New Zealand resident beneficiary, it may be necessary to trace the history of income, gains and past distributions.

If the make-up of a distribution cannot be determined, it is assumed to be entirely taxable.

7C | Issues for settlors leaving New Zealand

YOU NEED TO KNOW

- What needs to be considered when a complying trust ceases to have a New Zealand resident settlor
- That you need overseas tax advice if you leave New Zealand as a trustee or settlor
- If you are the settlor of a New Zealand complying trust, there are some additional issues you need to consider when you leave New Zealand
- Failure to do so before you leave, could result in your personally, or the trust, having additional tax issues to address

EXEMPTION FOR FOREIGN INCOME

New Zealand taxes trusts based, in part, on the residence of the settlor. So when the settlor ceases to be resident, it is possible that the trust may cease to be taxed on foreign income. This can happen when a trust has no New Zealand resident settlor at any time throughout the income year – regardless of whether the trustee is New Zealand resident.

LOSS OF COMPLYING STATUS

Overseas income being earned by the trust with no New Zealand tax imposed can be a positive planning opportunity, but it is a double-edged sword. If you return to New Zealand, and become tax resident again, the trust will then become a non-complying trust – with distributions of income and gains taxed at 45%.

So if you are the settlor of a trust that holds foreign assets, and you are going to become non-resident, you need to manage these issues before the end of the tax year that you cease to be New Zealand tax resident.

OVERSEAS TAX ISSUES

Trusts are taxed differently in different countries. Some countries focus on the trustee, while others look through to beneficiaries. The consequence of this is that trusts may complicate your tax affairs if you move to a new jurisdiction.
It is important to seek advice in the country you are moving to, and to work with advisors who can manage the complexity of multiple jurisdictions.

8

Contact us

A selection of experienced professionals offering skills and ideas that are second to none.

8A | How we can help...

Tax issues become complicated when international borders are involved. KPMG has an international network of professionals who can help you to navigate the complexity and difficulties of doing business, or living and investing, in multiple tax jurisdictions.

To help you, we have provided contact details for people who can provide or co-ordinate KPMG services based on geographic location within New Zealand, and the leaders of our specialist lines of business. The KPMG New Zealand team can bring to bear a wealth of global knowledge and experience. We work regularly with the wider KPMG network and have relationships with colleagues in many other jurisdictions. Our relationships give you access to expertise from both sides of the border that you are working across - ensuring you can be well-advised, and leaving you free to focus on what is important to you.

If in doubt, please contact **Rebecca Armour** who will make sure that you are guided to the right person.

Contact details are available on the following page.

cutting through complexity

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