KPMG

TaxMail

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Regular commentary from our experts on topical tax issues

Issue 1

Business tax, AEOI and foreign trust legislation introduced

Snapshot

A second omnibus Tax Bill for 2016 has been introduced. It contains:

- A new Accounting Income Method (AIM) for calculating provisional tax, limits the application of use-of-money interest (UOMI), and proposes a series of other business tax changes to enhance compliance;
- A requirement for NZ financial institutions to review and report non-resident account holders (and their financial account information) to Inland Revenue, who will automatically exchange this information with other participating countries under the OECD's Automatic Exchange of Information (AEOI) initiative; and
- Enhanced disclosure requirements for New Zealand foreign trusts, following the independent review's recommendations earlier this year.

The proposals will have wide effect. The Bill largely implements proposals which have been consulted on previously and are about simplifying tax for business and fulfilling NZ's tax transparency commitments as a global citizen. Those affected can now see the detail of the proposals to assess their business and systems impacts.

The second omnibus Tax Bill of 2016 has wide impact

The business tax measures will help business in managing their provisional tax, UOMI and penalty exposures and are welcome

The AEOI and foreign trust disclosure measures are about NZ's commitments as a global citizen to enhance tax transparency

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What are the Bill's proposals?

Business tax measures

Accounting Income Method ("AIM")

The centrepiece is the new AIM to calculate and pay provisional tax. Eligible businesses will be able to rely on AIM-capable software to calculate and pay tax as income is earned. A minimum of six payments a year will be required.

An end-of-year tax return will still need to be filed. However, the expectation is that with reasonably accurate and regular AIM tax calculations and payments, any square up will be minor.

Key to the AIM is accounting software which can make tax adjustments and recalculate financial and tax amounts, as required to correct for errors. The software must also be able to be updated for tax changes as they are made. The Commissioner will determine what tax adjustments must be made by the software.

Certification of AIM-capability will be based on a software provider's statutory declaration that the software is fit for purpose.

Eligible businesses for the AIM will generally be those with less than $5 million of turnover. Larger businesses will need to use a large business AIM-capable software package (approved by Inland Revenue).

Other measures

These include:

- UOMI will apply from the third instalment date only, for businesses using the standard uplift method to calculate their provisional tax.
- The threshold for application of UOMI, for provisional tax, will be raised from $50,000 to $60,000 of residual income tax (RIT) and be extended to entities.
- The 1% monthly incremental late payment penalty will be removed.
- Contractors will be able to self-assess withholding tax rates (a minimum rate of 10% for residents and 15% for non-residents will apply, unless a special rate is approved by Inland Revenue). If an IRD number is not provided the rate will be 45%. Labour hire firms will be required to withhold tax from contract payments.
- Inland Revenue will be able to disclose certain tax debt information to credit reporting agencies and information to assist with enforcement by the Companies Office.
- Simplified rules are proposed for calculating motor vehicle and premises deductions.
- Holiday leave paid within 63 days of balance date will not have to be deducted.

The business tax measures in the Bill are largely unchanged from the proposals previously consulted on. Refer KPMG's taxmail and submission on those proposals for more information.

Implementing AEOI in New Zealand

New Zealand's commitment to AEOI will be implemented through a specific set of rules that give the OECD's Common Reporting Standard (CRS) and its commentary the force of New Zealand law. Key features include:

- Requiring NZ financial institutions to undertake due diligence on all account holders ("the wider approach"). This will mean residents of a country that has not signed up to AEOI will need to be reviewed. It will be optional for NZ financial institutions to report these accounts to Inland Revenue.

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- Allowing regulations and determinations to be made on which entities and financial accounts are excluded from AEOI obligations. These will also be used to prescribe the countries that New Zealand will exchange information with.
- Specific civil penalties for NZ financial institutions, and account holders, who fail to take specific actions or provide information required under AEOI. The account holder penalties will also apply to FATCA non-compliance.
- Confirming a 1 July 2017 start date and a 31 March mandatory reporting period for AEOI.

The Bill is consistent with the factsheet Inland Revenue published in July (see our commentary on that here). Also, refer KPMG's previous taxmail and submission on the AEOI implementation proposals.

Foreign trusts – enhanced disclosure requirements

The Bill implements the recommendations made by the *Government Inquiry into Foreign Trust Disclosure Rules* ("the Shewan Inquiry"). These include:

- Registration of foreign trusts with Inland Revenue.
- Provision of trust details (including information relating to settlors, beneficiaries and the trust deed) on registration.
- Annual returns which update trust information and provide details of settlements and trust distributions, as well as the annual accounts.
- Registration and annual return fees.

A failure to comply will mean a foreign trust is subject to New Zealand tax on its worldwide income. Inland Revenue will provide access to a register of foreign trusts to the Police and the Department of Internal Affairs.

Refer our taxmails on the Shewan Inquiry recommendations and the Government's response and KPMG's submission to the Shewan Inquiry for further information.

Who's impacted?

The AIM and the "safe harbour" UOMI rules, in particular, should have a positive impact for businesses, in managing their provisional tax. The late payment penalty changes will also help business.

The AEOI proposals will affect a wide range of NZ entities. The FATCA rules show there are a range of entities who may not consider themselves financial institutions but are caught. (These include family trusts depending on their investments and how they are managed.) As AEOI has slightly different definitions to FATCA, entities will also need to consider whether they have different obligations under each.

The enhanced disclosure proposals for foreign trusts are likely to have a much wider impact than stated. For example, there are likely to be New Zealand resident trustees of family trusts established by a family member living offshore (e.g. in Australia or the United Kingdom). Those trusts appear to be covered by the proposals. Unless the new disclosure rules are complied with, those family trusts would become subject to New Zealand tax on their worldwide income.

Our view

The approach in the Bill

The Bill takes the welcome approach of grouping provisions relating to particular proposals. All of the AIM changes are in one part, for example. This makes it easier to assess the proposals individually.

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However, the Bill takes an inconsistent approach to clarifying matters of technical detail across the different proposals. Government regulations and Inland Revenue determinations can be made to progress various AEOI matters. In contrast, detailed legislative sections apply for calculating motor vehicle deductions (and other business tax measures). Giving administrative flexibility to change an approach is useful but the basis on which that is done needs to be clear. This is an approach which could be used more widely with appropriate provisions which clearly set out the basis for a determination or regulation.

The specific proposals

The AIM, UOMI and contractor withholding tax proposals take an overly protective approach. There are detailed rules to prevent manipulation of tax payments. That concern is, in our view, misplaced as provisional tax (and withholding tax generally) is not a final tax. It also suggest that AIM software cannot simply be relied upon to "get it right". A relaxation of the requirements will make the new business tax regime more likely to be useful and applied by taxpayers.

For AEOI, there is a potential for duplication of reporting. Inland Revenue's Making Tax Simpler: Investment income information proposals released for consultation last month will require monthly reporting of certain income and tax details of account holders. Officials' concern is that AEOI imposes a higher standard than existing tax (and non-tax) information requirements, and non-compliance could impact New Zealand's international standing. However, we believe there is an opportunity to develop a single set of "know your client" and reporting rules, for tax purposes, for residents and non-residents, which meet both local and AEOI requirements. (You can read our taxmail on the investment income information proposals here.)

Making the OECD's CRS and its commentary part of New Zealand law is designed to help with global consistency. However, this will import any future changes automatically, and could make it difficult for NZ financial institutions and their account holders to keep track of the various updates. NZ financial institutions will need a system to keep up-to-date with the OECD's position and notify customers accordingly. Alternatively, up to date Inland Revenue guidance should be provided.

Achieving the policy intent

In some cases, it is not clear that the Bill gives effect to the proposals. For example, it is not clear to us that the foreign trust registration requirement works as intended. The expected call for submissions should give those affected an opportunity to have the proposals clarified.

For further information

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