KPMG

TaxMail

8 September 2015

Regular commentary from our experts on topical tax issues

Issue 3

R&D Tax Bill reported back

Snapshot

The Finance and Expenditure Select Committee of Parliament has reported back on the Taxation (Annual Rates for 2015-16, Research and Development, and Remedial Matters) Bill. The Bill:

- Refunds R&D tax losses for qualifying businesses.
- Allows tax deductions for certain currently non-deductible and non-depreciable (i.e. "black hole") R&D expenditure.
- Clarifies the GST treatment of bodies corporate.
- Contains miscellaneous international tax and other remedial amendments.

While the Select Committee has recommended a number of useful improvements to the Bill, in response to public submissions, these are relatively minor in scope.

Calls by submitters for more significant reform, e.g. to simplify, extend or retract certain proposals, have largely been ignored.

The Bill now awaits enactment. We expect this will be in the next few weeks.

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It is worth noting that the vast majority of submissions on the Bill were not accepted

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What has changed?

The Bill proposals were discussed in detail in our March taxmail. The Select Committee's key recommendations follow.

Refund of R&D tax losses

The key change is to expand the range of companies that are eligible to have R&D tax losses refunded. The Bill excluded qualifying companies, groups including foreign companies, and companies that have not complied with all their tax obligations from the new rules. The Select Committee has recommended their inclusion. The latter due to concerns that a minor dispute with Inland Revenue could result in a company being excluded.

Other changes recommended by the Select Committee include:

- Labour expenditure, for calculating R&D tax losses to be refunded, can include fringe benefits and employer superannuation contributions.
- R&D tax loss refunds not having to be repaid on an amalgamation with another company, but the amalgamated company would retain the liability.
- Requiring R&D tax loss information to be filed at the same time as the tax return. The Bill as introduced provided an additional 14 days. (The Select Committee report also notes Inland Revenue will allow additional time to file for refunds during the first year of the new rules.)
- Allowing Inland Revenue to consult Callaghan Innovation on marginal R&D tax loss refund applications.
- The Ministry of Business, Innovation and Employment having responsibility for implementing and administering the new rules, rather than Inland Revenue.

Only minor changes to other rules

The Select Committee did not recommend any substantive changes to the following proposals in the Bill (see our March taxmail for further information on these):

- Deductions for "black hole" expenditure on certain intangibles.
- Changes to the GST treatment of bodies corporate. The Select Committee recommended some drafting amendments to:
  - Clarify that body corporate "funds" subject to output tax on registration mean the value of money and assets received by the body corporate as exempt supplies, excluding the common property of the body corporate.
  - Change the definition of "body corporate" to "unit title body corporate", to exclude a body corporate of a retirement village.
- The various Controlled Foreign Company, Foreign Investment Fund and Foreign Superannuation tax amendments.
- The removal of the multi-year tax return filing requirement for individuals, due to Inland Revenue's upcoming Business Transformation changes.
- Application of market interest rates to calculate FBT on employment-related loans.
- Allowing provisional tax pooling to be used to meet interest costs for additional tax arising under a dispute.
- Remedial amendments to the bad debt deductibility and financial arrangement rules.

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Additional recommendations

The Select Committee included a couple of additional remedial amendments to improve the workability of the Income Tax Act:

- Clarifying that accommodation payments and accommodation allowances are covered by the rules for valuing overseas accommodation.
- Widening the scope of the income tax exemption that currently applies for charitable entities to include their wholly-owned subsidiaries. This was in response to a KPMG submission.

Our view

The Select Committee received and considered 20 submissions on the Bill, including by KPMG. It is worth noting that the vast majority of submissions on the Bill were not accepted.

The Select Committee process involves Officials reviewing submissions and providing their recommendations, in an Officials' Report. The Select Committee, with the help of an independent advisor, then makes its decisions.

In our experience, it is generally difficult to get major change to a Tax Bill affected at the Select Committee stage. This will particularly be the case where any changes will have revenue or administrative implications for Government.

While the Select Committee recommended a number of useful improvements to the Bill, particularly in relation to the R&D tax loss refund proposal, these are relatively minor in nature. A notable exception is the Select Committee's concern that:

> *the [Inland Revenue's] existing computer system has limited ability to implement and administer new approaches such as [the R&D tax loss refund proposal].*

As a result, the Committee noted:

> *Rather than seeking to adapt the department's existing system, it is proposed that the Ministry of Business, Innovation and Employment, which already administers a grants programme for R&D, use its ICT system to implement and administer this initiative.*

This highlights the practical challenge for Government in implementing new tax policy measures. This is likely to be heightened as Inland Revenue begins its Business Transformation changes. The transition will need to be carefully managed.

For further information

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