

TAX INFORMATION BULLETIN NO.3

SEPTEMBER 1989

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RESIDENT WITHHOLDING TAX REGIME

- INTEREST PAYE

- DIVIDEND PAYE

The Income Tax Amendment Act (No. 2) 1989 which introduces the Resident Withholding Tax regime received the Governor General's assent on 26 July 1989. The Amendment Act was introduced into Parliament as the Income Tax Amendment Bill (No. 8). Part I of the Amendment Act contains the legislation implementing the resident withholding tax regime and also extends the fringe benefit tax regime to certain non-cash dividends provided to shareholders. Part II of the Amendment Act consists of sundry miscellaneous and consequential amendments to the Income Tax Act 1976.

A comprehensive explanation of the provisions of the Amendment Act as Appendix A to this Bulletin will be issued with TIB No. 4 in approximately three weeks.

This Bulletin summarises the new legislation with particular emphasis on the resident withholding tax provisions (interest and dividend PAYE).

INTEREST PAYE

1. INTRODUCTION

From 1 October 1989 a 24% withholding tax which will be known as Interest PAYE will be deducted from all interest paid by a NZ resident, or by a non-resident carrying on business in New Zealand through a fixed establishment if at any time the payer either:

- i) Holds a certificate of exemption; or
- ii) Incurs the interest expense in the course of carrying on taxable activity.

Interest will not be subject to Interest PAYE if

- i) The interest is "exempt interest"; or
- ii) The recipient holds a certificate of exemption (such persons are referred to as "exempt recipients"); or
- iii) The recipient is a non-resident; or
- iv) The interest is paid between group companies.

The term taxable activity means the regular ongoing activity of any individual or organisation involving the supply of goods and services. The term has the same meaning as it does for GST purposes except that it also includes exempt supplies such as financial services and residential rentals. It does not apply to wages or salary.

Exempt interest is defined in the Act. Some of the more common types of exempt interest are the interest payments in respect of:

- Hire purchase agreements
- Trade credit
- Specified leases
- Bonus Bonds and Post Office Bonus Bonds
- Inflation Adjusted Bonds

2. INTEREST

For the purposes of the Interest PAYE regime, the term "interest", which is any payment made in respect of money lent other than a repayment of money lent, has been expanded to include redemption payments as defined in section 2 of the Income Tax Act 1976. This includes commercial bills, as well as the redemption of any other debt instrument, to the extent that it is not a repayment of money lent.

Interest PAYE is deductible from the difference between the original issue price and the redemption price of the stock and not the difference between the acquisition price of the stock (if bought on the open market) and the redemption price of the stock.

Example

A person buys the following Government stock on 1 June 1989 for \$49,000.

Coupon interest rate	12%
Face value	\$50,000
Issue price	\$45,000
Maturity date	31 December 1989

If the person holds the stock to maturity a sum of \$48,800 will be received.

The redemption payment (which is the interest for Interest PAYE purposes) with respect to the stock is \$5,000 despite the fact that the difference between the person's acquisition price of the stock and its redemption price is only \$1,000

3. \$5,000 THRESHOLD

A person who does not hold a certificate of exemption and who pays interest in the course of carrying on a taxable activity or who holds a Category B type certificate of exemption (e.g., tax exempt entities, non-profit bodies and tax loss taxpayers) is not required to deduct Interest PAYE from the first \$5,000 of interest paid on or after 1 October 1989 and before 31 March 1990.

However, the balance of any interest paid in excess of \$5,000 during this period is subject to Interest PAYE.

From 1 April 1990 persons in this category will only be liable to deduct Interest PAYE if the resident withholding interest in the previous year (to

31 March) exceeded \$5,000 or if it did not, once the accumulated interest paid in the year exceeds \$5,000, Resident withholding interest is the interest that is not exempt interest or paid to an exempt recipient.

4. LIABILITY OF AGENT/TRUSTEE TO DEDUCT INTEREST PAYE

Where an agent receives interest on behalf of another person without tax being correctly deducted that agent must deduct tax before forwarding it to the recipient unless the agent holds a valid certificate of exemption and receives the interest as a trustee (other than a bare trustee). Agents or trustees carrying on a taxable activity through a fixed establishment in New Zealand, whether resident or non-resident, are liable to deduct Interest PAYE from interest payments they make on behalf of another person.

5. PAYMENT OF INTEREST PAYE TO THE DEPARTMENT

Persons deducting Interest PAYE must pay the Interest PAYE to the Inland Revenue at a minimum of six-monthly intervals.

Where a person estimates he or she will deduct \$500 or more (in aggregate) of Interest PAYE during each month of any year the deductions are required to be paid to the Inland Revenue by the 14th of the month following the month the deduction was made. (i.e., in which the interest was paid).

There are two compulsory pay in dates per year regardless of the amount of Interest PAYE deducted They are 14 April and 14 October

Where the person will not deduct \$500 or more (in aggregate) of Interest PAYE during each month of any year that person is required to pay the deductions to the Inland Revenue by the 14th of the month following the month in which the accumulated deductions to date total \$500.

6. TAX DEDUCTION CERTIFICATES

Where interest PAYE has been deducted from interest payments a tax deduction certificate giving full details of the interest and tax must be given to the recipient by the payer by 20 May in the year following the end of the income year in which the interest was paid. Tax Deduction Certificates may be issued periodically throughout the year or for the accumulated totals at the end of the year. While an Inland Revenue form is available there is provision in the Act for the Commissioner to approve a different format provided the information contained on the certificate meets the requirements of the Act.

The recipient of the interest will be required to show this information in their end of year tax return. Although the Tax Deduction certificate does not have to be provided with the tax return it is necessary for it to be retained for a period of three years.

7. ANNUAL RECONCILIATION STATEMENT

All payers of interest will be required to furnish to the Commissioner a reconciliation of the total amount of interest paid for the year and the total Interest PAYE deducted, which should reconcile to the total amount interest PAYE paid to the Inland Revenue. This must be supplied by 31 May in the year following the end of the income year.

8. CERTIFICATE OF EXEMPTION

A certificate of exemption will allow a person or organisation to receive interest or dividends without deduction of PAYE. An application for exemption must be made in writing, using form IR 15E. The following groups are eligible to apply for a certificate of exemption:

Category A - Those persons/organisations to whom the \$5,000 threshold does not apply.

1. REGISTERED BANK, TRUSTEE BANK, OR BUILDING SOCIETY
2. ANY TRUSTEE COMPANY, THE PUBLIC TRUSTEE, AND THE MAORI TRUSTEE .
3. TAXPAYERS WITH INCOME OF MORE THAN \$2 MILLION
4. TAXPAYERS WITH ESTIMATED INCOME OF MORE THAN \$2 MILLION
5. FINANCE HOUSE

Category B - Those persons/organisations to whom the \$5,000 threshold does apply, provided the \$5,000 threshold was not exceeded in the preceding year.

6. CHARITABLE ORGANISATIONS
7. SPORTS OR RACING CLUBS
8. IMPROVEMENT OR RESEARCH PROMOTER
9. LOCAL OR PUBLIC AUTHORITY
10. FRIENDLY SOCIETIES OR CREDIT UNIONS
11. NON-PROFIT BODIES
12. TAXPAYERS WITH LOSSES (OR ANTICIPATED LOSSES)

9. CANCELLATION OF CERTIFICATES OF EXEMPTION

Certificates of exemption will be issued for an unlimited period in all cases except where the exemption is granted under category B number 12. The period the exemption applies to in these cases will be printed on the certificate.

Certificates can be cancelled at a later date if circumstances under which they were issued change. If a person or organisation holding a certificate of exemption no longer meets the criteria under which the certificate of exemption was obtained that person/organisation must meet certain obligations within 5 working days. Those obligations are:

- (a) Advise the Department that the grounds for holding the exemption no longer apply.
- (b) Return the certificate of exemption to the Department.

The Inland Revenue may cancel a certificate of exemption for any of the following reasons:

- (a) The person or organisation no longer qualifies for the exemption;
- (b) The person or organisation does not qualify for the exemption and the certificate was issued on the basis of misleading information;
- (c) Where the exemption was granted to persons or organisations under category A number 4 and;
 - (i) evidence shows that the assessable income before allowable deductions was less than \$2,000,000 in the relevant accounting year; or
 - (ii) satisfactory evidence of assessable income before deductions is not provided; or
 - (iii) Inland Revenue believe the evidence provided is misleading.
- (d) The holder of the certificate of exemption has not paid income tax due by the due date for payment.

In each case the Inland Revenue will notify the holder of the certificate that the exemption no longer applies. The holder has 5 working days to return the certificate to the Inland Revenue and to inform all persons to whom the certificate has been shown that it is no longer valid.

10. GAZETTE NOTICES

Where a certificate of exemption has been cancelled or has expired the number of that certificate of exemption will be published in the Gazette. Also published in the Gazette will be the number of the certificates of exemption that are reissued after a previous certificate has been cancelled or expired.

11. DISCLOSURE PROVISIONS - FOR NON-BUSINESS PERSONS

After 1 April 1990, where a person or organisation pays interest (other than to an exempt recipient) which is to be claimed as a deduction from assessable income, and does not deduct Interest PAYE because the person or organisation is not carrying on a taxable

activity, or because it qualifies for the \$5,000 threshold, it must disclose to the Inland Revenue the following information with its annual return of income for the year in which the interest was paid:

- (a) The full name and last known address of the recipient;
- (b) The total interest paid to the recipient in that income year; and
- (c) The tax file number of the recipient.

12. DISCLOSURE PROVISIONS - FOR FINANCIAL ARRANGEMENTS

Special disclosure requirements apply to exempt recipients with respect to financial arrangements upon which interest is paid where the exempt recipients either buy such arrangements from, or sell such arrangements to a non-exempt recipient on or after 1 April 1990.

If during a year an exempt recipient buys a financial arrangement from a non-exempt recipient or sells a financial arrangement to such a person that exempt recipient is required to include the following information with their annual return of income for the year in which the transaction took place:

- (a) The full name and last known address of the non-exempt person.
- (b) The date of acquisition or sale.
- (c) The consideration paid or received by the exempt person in respect of the acquisition or sale (exclusive of fees).
- (d) The tax file number of the non-exempt person.

13. ASSESSMENTS

Assessments of Interest PAYE may be issued to Payers. The same right of objection rules apply to Interest PAYE as apply to income tax assessments.

14. ADDITIONAL TAX FOR DEFAULT

Additional tax at a flat 10% of the amount of the Interest PAYE paid late or outstanding will be charged, with a further 10% being added at the end of every 6 months while the amount remains outstanding.

15. OFFENCES

The following are listed as offences against the Act and carry severe penalties:

- (a) Failure to deduct Interest PAYE; in whole or in part.
- (b) Failure to pay the Interest PAYE deductions to the Inland Revenue.
- (c) Making a false or misleading application for exemption to the Inland Revenue.

- (d) Altering a certificate of exemption, falsely claiming to be an exempt recipient, possession of an imitation certificate of exemption, causing or attempting to cause a person to refrain from deducting Interest PAYE by production of any document.
- (e) Obtaining or attempting to obtain credit for interest PAYE deductions which belong to another person.
- (f) Failure by an exempt recipient to inform the Inland Revenue that the grounds for obtaining the certificate no longer apply.
- (g) Failure to provide a tax deduction certificate for interest PAYE.

DIVIDEND PAYE

1. INTRODUCTION

As from 1 October 1989 New Zealand companies are required to deduct Resident Withholding Tax from dividends paid to its shareholders resident in New Zealand. This tax is known as "Dividend PAYE" and is referred to as such throughout this bulletin.

For Dividend PAYE purposes there are four (4) main types of dividends. They are:

- Dividends (ordinary);
- Taxable bonus issues;
- Specified dividends;
- Dividends not liable for Dividend PAYE.

Dividends (Ordinary) are dividends including taxable bonus issues, but exclude non-cash and specified dividends.

Taxable Bonus Issue is any bonus issue made in lieu of a dividend, or a bonus issue the company elects to be a taxable bonus issue.

Specified Dividends are dividends paid by:

- a company not resident in New Zealand;
- a company whose constitution prohibits all of its income from being distributed to its proprietor member or shareholders;
- a tax exempt company;
- a company engaged in life insurance or reinsurance;
- a company when that dividend is claimed as a deduction from its income under section 194(5) of the Tax Act (i.e., dividend paid in respect of specified preference shares);
- a Maori Authority.

Dividends Not Liable for Dividend PAYE are:

- non-cash dividends subject to FBT;
- dividends paid to companies whose income from dividends is not taxable;

- excess remuneration treated as a dividend under sections 97 and 190 of the Tax Act;
- dividends paid to holders of a "Certificate of Exemption from Interest and Dividend PAYE".

Several of the rules relating to Dividend PAYE apply equally to each type of dividend while some rules relate only to a particular type. This bulletin sets out, firstly, details relating to specific kinds of dividends and, secondly, points common to all types.

2. ORDINARY DIVIDENDS

Dividend PAYE - On what is it Calculated?

Dividend PAYE is calculated on the "gross" dividend (i.e., the amount of the dividend actually paid plus any imputation and/or dividend withholding payment credit attached to that dividend but before the deduction of Dividend PAYE).

Dividend PAYE - How much is it?

The amount of Dividend PAYE to be deducted from ordinary dividends is calculated by multiplying the amount of the "gross" dividend by 33 cents in the \$1.00. The amount calculated is then reduced by the total of the imputation and/or dividend withholding payment credits (if any) attached to that dividend. The difference is the amount of Dividend PAYE to be deducted.

Example:

Abacus Finance Services Ltd pays a dividend of \$10,000.00. It attaches a \$1,000.00 imputation credit to the dividend.

Dividend paid	\$10,000
<i>add</i> imputation credits	\$ 1,000
"Gross" dividend	<u>11,000</u>
(on which PAYE is calculated)	<u>\$11,000</u>

Dividend PAYE at 33% (of \$11,000.00)	\$3,630.00
less imputation credit attached dividend	1,000.00

Amount of Dividend PAYE payable	<u>\$2,630.00</u>
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Dividend PAYE - Payer's Obligation to Shareholders

Whenever dividends, other than specified dividends, are paid a shareholder dividend statement must be given to the shareholder. This statement is to show:

- the name of the company;
- the date of the payment of the dividend;
- the name and address of the shareholder to whom the dividend was paid;
- the amount of non-resident withholding tax (if any) deducted;

- the amount of any imputation credit attached to the dividend;
- the amount of any dividend withholding payment credit attached to the dividend - Note: For the purposes of advising shareholders, Dividend PAYE is included in this amount;
- the total credits (imputation and dividend withholding payments - including Dividend PAYE);
- the total of the dividend paid to the shareholder and the total credits.

Dividend PAYE is treated as dividend withholding payment credits for the purposes of shareholder dividend statements.

End of Year Procedures

No additional end of year work is caused by the introduction of Dividend PAYE. An annual Imputation and Dividend Withholding Payment Account return (IR 4J) is still required. This will indicate what, if any, information the Inland Revenue may want in respect of Dividend PAYE deducted during the year ending 31 March.

3. SPECIFIED DIVIDENDS

Dividend PAYE - How much is it?

The amount of Dividend PAYE to be deducted from specified dividends is calculated by multiplying the amount of the Specified Dividend by 33 cents in the \$1.00. As no imputation nor dividend withholding payment credit can be attached to a specified dividend, the amount of dividend PAYE can not be reduced in a manner similar to that deducted from ordinary dividends.

Example:

Specified dividend declared	\$11,000.00
Calculate Dividend PAYE @ 33%	\$ 3,630.00

What documentation is required when a Specified Dividend is paid?

If a specified dividend is paid a "Resident Withholding Tax Deduction Certificate" (IR 17) is to be completed and a copy given to the recipient of that dividend. The IR 17 will show details of each payment, or a summary of all payments made for the tax year. It is to be given to the recipient either at the time of the payment of the dividend or annually, but no later than 20th May following the end of the tax year the dividend was paid; whichever the payer chooses.

The information to be shown on the IR 17 is:

- the full name and address of the payer;
- the full name and last known address of the recipient;

- the period (year to 31 March) to which the deduction relates;
- the amount of dividend PAYE deducted;
- total dividend (sum of amount actually paid and the Dividend PAYE deducted).

End of Year Procedures

Payers of Specified Dividends must, not later than 30 May, complete an annual reconciliation statement (IR 17S) and send it to:

Inland Revenue Processing Centre
PO Box 40-141
UPPER HUTT

This will show:

- the amount of the Specified Dividends paid subject to Dividend PAYE;
- the amount of Dividend PAYE deducted;
- the amount of the Specified Dividends paid which were not subject to Dividend PAYE.

4. TAXABLE BONUS ISSUES

Companies making a taxable bonus issue will not, in effect, deduct Dividend PAYE from that issue. The taxable bonus issue has to be grossed up to a pre PAYE figure and the PAYE calculated on that grossed up value. The shareholder(s) must show in their tax return the total of the taxable bonus issue and the PAYE.

5. SPECIAL CASES

(1) Agents and Trusts

Dividend PAYE does not have to be deducted from dividends paid to another person if the payer is satisfied that the other person;

- is a bank, building society, the Public or Maori Trustee or a trustee company, or
- holds a valid certificate of exemption from interest and dividend PAYE and that certificate has not been cancelled.

If an agent or trustee of a bare trust receives a dividend, from which PAYE should have been deducted but was not, that agent or bare trustee must;

- deduct PAYE from the dividend at the time it was received if the person actually deriving the dividend does not hold a valid certificate of exemption,
- pay that deduction to the Inland Revenue by the 14th day of the following month.

Whenever dividend PAYE is deducted by an agent or trustee under the circumstances set out above the

dividend is to be treated as a specified dividend and the rules relating to those types of dividends apply.

(2) Maori Authorities

Distributions made by Maori Authorities are, for Dividend PAYE purposes, to be treated as Specified Dividends and the rules relating to those types of dividends apply.

6. POINTS COMMON TO ALL TYPES OF DIVIDENDS

Dividend PAYE - when and where is it payable?

Dividend PAYE must be paid to the Inland Revenue Department no later than the 14th day of the month following the month in which the dividend was paid.

All payments of Dividend PAYE are to be made to:

Inland Revenue Processing Centre
P O Box 40-104
UPPER HUTT TT

Once a payment has been receipted at the processing centre a replacement pay-in slip will be issued, together with a self addressed envelope, facilitating easier future payments.

Are there any Penalties for late Payments?

Yes. If Dividend PAYE is not been paid by the due date, 10 percent additional tax will be charged on top of the amount of Dividend PAYE calculated. If the amount outstanding has still not been paid six months after the due date a further 10 percent will be added.

Dividend PAYE - is it to be deducted from dividend paid to Non-residents?

No. Non-resident withholding tax (NRWT) is still required to be deducted from dividends paid to persons who are not resident in New Zealand.

7. EFFECT ON SHAREHOLDERS

Dividend PAYE deducted from dividends, other than specified dividends, will be shown as a "dividend withholding payment credit" on the shareholder dividend statement issued by the company.

Dividend PAYE deducted from specified dividends will be shown as "Dividend PAYE deducted" on the Tax Deduction Certificate (IR 17).

No matter what the deduction is called, or the type of form received, the amount of PAYE is to be taken off

any income tax payable at the end of the year. Any excess is to be refunded to the shareholder. The amount of dividend to be shown in the shareholders' returns is to include the dividend actually received plus any credits attached. These credits will include imputation/dividend withholding payment credits (if any) and Dividend PAYE deducted.

As from 1 April 1990 "provisional income" will not include dividends from which PAYE has been deducted.

Provisional tax for the 1990 tax year can be estimated to take into account any PAYE that may be deducted from dividends received from 1 October 1989. Normal penalties will apply if the amount is under-estimated.

8. FRINGE BENEFIT TAX ON NON-CASH DIVIDENDS

From 1 October 1989 companies resident in New Zealand are required to pay fringe benefit tax (FBT) in respect of non-cash dividends paid or made available to non-corporate shareholders.

Non-cash dividends are dividends other than;

- dividends paid in money,
- non-cash dividends.

For FBT purposes the company that provides the non-cash dividends is deemed to be an employer and the shareholder recipient is deemed to be an employee.

Exclusions from FBT apply to non-cash dividends paid or made available to companies, to holders of certificates of exemption, and to certain other dividends.

Non-cash dividends that are subject to FBT are not subject to income tax in the hands of the shareholders.

OTHER AMENDMENTS

In addition to the legislation implementing the resident withholding tax, the Amendment Act also contains the following amendments to the Income Tax Act

Part I - Resident Withholding Tax

- definition of the term "interest", to clarify that the term includes payments made under third party arrangements,
- definition of new terms "non-cash dividends" and "working day"
- definition of the term "dividends", to provide the

circumstances whereby forgiveness of debt to a shareholder gives rise to a dividend and to provide valuation rules in respect of a low interest loans to a shareholder that gives rise to a dividend,

- a restriction of the Child Rebate so that it no longer applies to resident withholding income (interest and dividends),
- repeal of the \$200 interest and dividends exemption with a transitional provision for the 1989/90 income year,
- exemption from income tax of non-cash dividends to the extent to which such dividends are subject to fringe benefit tax,
- removal of the exemption that applies to companies deriving dividends that arise from forgiveness of debt,
- definition of the term “close of trading spot exchange rate”,
- change to the due date for payment of non resident withholding tax from the 20th of the month to the 14th of the month,
- imposition of fringe benefit tax on non cash dividends provided to non-corporate shareholders,
- changes to the pay-period taxpayer provisions,
- miscellaneous amendments and transitional provisions relating to provisional tax,
- amendments to the imputation and dividend withholding payment regimes to provide reporting arrangements for dividend withholding tax,
- increase from \$2 to \$5 the amount of tax that the Commissioner may exercise a discretion as to whether to collect or refund,
- inclusion of resident withholding tax in the definition of the term “residual income tax”,
- publication of names of persons convicted for failing to deduct or to account for resident withholding tax or non-resident withholding tax,
- an amendment to the record keeping requirements of charities;

Part II- Miscellaneous Amendments

- clarification of the meaning of the term “trustee”,
- exclusion from “dividends” of certain livestock and wine and whisky revaluation reserves distributed on winding up,
- amendments relating to the imposition of fringe benefit tax in respect of low interest loans provided by private companies to shareholder employees,
- in relation to the new superannuation regime, to clarify that for the purpose of determining whether an employer’s obligations to a superannuation fund are satisfied the amount of specified superannuation withholding tax is deemed to be received by the fund,
- exclusion from assessable income for family support purposes of recovery of depreciation on the sale of a building,
- amendments to the imputation legislation relating to the treatment of export tax credit refunds as debits to the Imputation Credit Account (ICA) and a relaxation of the provisions dealing with the limitation on refunds of income tax where the ICA has insufficient credit balance,
- a transitional provision to ensure that interest is not charged on provisional tax payable by category 1 superannuation schemes and life insurance companies in respect of any specified superannuation or annuity income for the income years ending 31 March 1989 to 30 September 1989,
- clarification of the terminal tax payment dates applicable to taxpayers who are neither employees nor provisional taxpayers,
- clarification of the due date for payment of penal tax being no later than the 28th day after the date of issue of the assessment of penal tax,
- reduction from 40.5 cents to 33 cents in the rate of income tax payable by superannuation category 3 schemes for the income year commencing 1 April 1989 and subsequent years.

Reference: Appendix A to TIB No. 3,
September 1989.
To be issued with TIB No. 4

GST - LICENSED LOTTERY PROMOTERS

SUMMARY

The Department has been asked to consider the GST implications where a licensed lottery promoter organises a raffle or lottery.

BACKGROUND

A licensed lottery promoter is engaged to promote the sale of tickets in a lottery, raffle or game of chance. Section 32 to 35 of the Gaming and Lotteries Act 1977 govern who may conduct a lottery. Apart from section 33 (which allows a person to conduct a lottery, provided the prizes do not exceed \$50.00) all lotteries must be conducted by a "society". The definition of a "society" is:

"means any corporation, sole, association of persons (whether incorporated or not), or local or affiliated branch of any such organisation, that is established and conducted entirely for any purpose other than a commercial one".

RULING

Clearly a licensed promoter could not meet this definition and therefore would not be granted a licence. This has been confirmed by Internal Affairs. It is the person (society) to whom the licence is granted who conducts the lottery. That person engages the licensed promoter to promote the lottery. Although section 5(10) of the GST Act 1985 makes reference to licensed promoters the Gaming and Lotteries Act 1977 clearly states that they cannot conduct lotteries on their own behalf. They are therefore acting on behalf of the person who holds a licence to conduct a lottery or where a group of people acting co-operatively, as an agent of the group.

The GST implications are as follows:

Promoter

Output tax on Commission (if registered) Input tax credits for any expenses, e.g., motor vehicle expenses.

Individual Clubs

The receipts for selling tickets are payments for the supply of services. If registered for GST purposes there is a GST liability on these receipts. If not registered these receipts would be taken into account in determining whether there is a liability to be registered. Registered persons can also claim an input credit in respect of the costs incurred in selling of tickets.

Co Op. Societies

Output tax on gross receipts - less any cash prizes.
Input tax credits for:

- Commission paid to promoter.
- Prizes of goods or services purchased (subject to tax invoice, etc., requirements).
- Any other costs, e.g., printing of ticket.
- Payment to any individual club that is registered for GST purposes.

Reference

HO REF: GST A.4.1

GST Manual - Chapter 7 Part 1.1 Lotteries
- Chapter 7 Part 6 Agents

SHAREHOLDER/EMPLOYEE REMUNERATION

This item restates the Department's policy in relation to the assessability and deductibility of shareholder/employee remuneration declared after the end of a financial year.

BACKGROUND

It is common for proprietary companies to determine directors' fees, bonuses or extra salaries after the end of an income year once the annual accounts have been completed. The remuneration so determined is claimed as a deduction by the company in the year to balance date. The directors and shareholder/employees return the same remuneration in the following year, being the year of receipt.

RULING

Following TRA Case 12 (1979), 3 TRNZ 127, the Department accepted the above practice where it is clear that the company was definitely committed to the payment of a quantified amount of directors' fees, bonuses or extra salary prior to balance date. The company will be considered to be committed to the payment by the passing of a properly authorised resolution in the company's minute books before the end of the income year.

As to the question of the assessability of the remuneration the law is settled that salary or wages or similar types of income are derived for tax purposes at the time the income is paid or otherwise made available to the employee. This is so notwithstanding that the services giving rise to the income may have been rendered or performed in an earlier year.

The timing of the payment will also determine when any PAYE tax deductions or withholding payments should be paid to Inland Revenue.

The Department has also accepted that where a regular pattern of backdating the deduction by the company has been established over a period of years, that practice will be allowed to continue. This would be the case whether or not the legal requirement of a fully committed resolution had been met. The department would expect that established practice to continue regardless of the effects of the recent changes to the company income tax rates.

Reference: H.O. 10.C.10.6
TR Chapter 5, Part 111

ESTATE AND TRUST RETURNS, IR 6

ERROR IN THE IR 6 RETURN

The 1989 Return of Income for Estates and Trusts omits a panel for deduction of charges incurred for the preparation of the return.

Although this has been omitted any expenditure incurred in the preparation of all annual returns is deductible pursuant to section 165 of the Income Tax Act 1976.

Income Tax (Foreign Investment Fund Determinations) Regulations 1989

Section 245S of the Income Tax Act 1976 provides for a formal procedure, whereby a foreign entity, or any person holding rights in relation to that entity, can request a determination from the Commissioner as to whether or not the rights held constitute interests in a Foreign Investment Fund.

Determination regulations known as the "Income Tax (Foreign Investment Fund Determinations) Regulations 1989" were passed by Order in Council on 31 July 1989 and are included as Appendix B to this bulletin. They were notified in the "Gazette" on 3 August 1989 and take effect 28 days from that date, being 31 August 1989.

Whilst the determination regulations make provision for a fee to be charged to the applicant for a determination, no fees will be charged in respect of applications received by 31 March 1991, in relation to a request for a determination to be made in terms of section 245S of the Income Tax Act 1976.

An application form IR 100B, "Foreign Investment Fund Regime - Application for a Determination under section 245S of the Income Tax Act 1976" is available for persons wishing to avail themselves of the determination procedures and can be obtained from your local Inland Revenue office. The reverse side of the IR 100B provides an outline of the determination regulations and procedures.

Reference: Appendix B to TIB No. 3,
September 1989

PRESS RELEASES

1. Non-profit Bodies Facing PAYE Deductions

"Thousands of sports clubs, charities and non profit organisations may have 24% PAYE deducted from the interest they receive from 1 October", the Commissioner of Inland Revenue, David Henry, said today. "This is because even though they are not liable to tax and qualify for a certificate of exemption from Interest PAYE, they have not applied for one", Mr Henry said.

The Department has been advertising the availability of the certificates including a freephone service. Only 3000 have applied so far out of an expected 26,000. "If these organisations do not apply to Inland Revenue for a certificate of exemption by 31 August they will not receive it in time for their bank to process, and as a result Interest PAYE will be deducted from their interest" Mr Henry said.

A wide range of people and organisations qualify for a certificate of exemption and can still get one by immediately completing an application form which is available from any Inland Revenue office.

The Interest PAYE freephones are still operational and can give advice or send an application form. The number to ring is 0800 802 803.

Mr Henry also stressed "Once the certificate of exemption is received the holder will have to advise the bank or payer of interest immediately so that the bank can ensure the 24% Interest PAYE is not deducted".

If an organisation does not apply for a certificate of exemption in time and Interest PAYE is deducted that organisation will have to apply to Inland Revenue to get the tax back.

2. 600 Happier Taxpayers - Problem Resolution Service

Over 600 taxpayers are much happier after having their tax problems sorted out through Inland Revenue's Problem Resolution Service. The Service was launched in May of this year to handle complaints from taxpayers who have been unable to resolve their problem through the Department's normal channels.

"In the two months ending June 1989, 638 taxpayers have used the service", the Commissioner of Inland Revenue, David Henry, said today.

"Approximately 65% were experiencing delays in receiving refunds and replies to letters. 70% of their

problems were the result of staff errors and work backlogs. Where it is found the errors were attributable to staff members, immediate training is given to reduce the likelihood of the problem reoccurring” Mr Henry said.

Inland Revenue says that the Problem Resolution Service managed to sort out the majority of problems within 5 working days.

“We have received a very favourable response, to the establishment of the service, from both the public and professions. Although one very upset person who contacted the service suggested that his problem could be best resolved by lynching the Commissioner. However, after using the Service his opinion of the Department had greatly improved and my neck is safe”, Mr Henry said.

Another taxpayer, with a relatively minor problem which had not been sorted out through normal channels, was referred to the Service. Upon checking the file it was found that the taxpayer had made a number of errors when completing his tax returns. “We found he was entitled to an additional refund”, Mr Henry said.

An explanatory pamphlet on the Problem Resolution Service is available from any Inland Revenue office.

PROVISIONAL TAX

“USE OF MONEY” INTEREST/PENALTY PROVISIONS

Over recent weeks concern has been expressed by tax practitioners that insufficient information has been made available to them in respect of the new additional tax/interest application rules, particularly in relation to interest. Obvious confusion has arisen over the differentiation between penalties and interest charged to the taxpayer and interest payable by the Department. The purpose of this item is to clarify these rules as they apply to 1989 provisional and residual income tax payments.

Before giving a brief overview of how the interest provisions are applied, it is necessary that the reader understand the interest concept. That is - that the interest calculated recognises the use of money during the period from the third provisional tax instalment due date to the date interest ceases to accrue. It is *not* a penalty for any default in payment or an underestimation of liability. These latter two instances are explained in 1 and 2 below.

Throughout the text reference is made repeatedly to the term ‘residual income tax’. This term relates to the difference between the total amount of tax assessed (including late payment and underestimation penalties) and the amount of tax paid.

HOW INTEREST/ADDITIONAL TAX IS IMPOSED

Under the system operating for 1989 provisional tax, there are three ways in which taxpayers can be penalised, and they could in certain circumstances incur all three penalties. These penalties are:

1. Late Payment Penalty (Sec 398)

Where an instalment is short paid, late paid or not paid, 10% additional tax will be imposed. This could also be subject to six monthly incremental penalties.

2. Underestimation Penalty (Sec 384)

Where provisional tax is calculated using the estimate option and the amount last estimated is less than 80% of the residual income tax, a flat 10% additional tax for under estimation will be imposed.

Where taxpayers voluntarily estimate, the additional tax is 10% of the lesser of;

- (i) the difference between the 1989 provisional tax paid up to the third instalment date and the 1989 residual income tax assessed;
- (ii) the difference between the 1989 provisional tax paid up to the third instalment date and the 1988 residual income tax increased by 10%.

- Where taxpayers have 1989 provisional income in excess of \$1,000,000, i.e., compulsory estimates, the additional tax is 10% of the difference between 1989 provisional tax paid and 1989 residual income tax.

3. “Use of Money” Interest (Sec 398A)

For

- (i) all non-individuals who are provisional taxpayers;
- (ii) all individuals in the capacity of trustees, i.e., beneficiaries’ income is excluded, and
- (iii) individuals where 1989 provisional income is more than \$100,000 or those who estimate.

Interest is calculated on a daily basis at a rate of 10% per annum and will be:

- charged to the taxpayer if residual income tax is more than provisional tax;
- paid to the taxpayer if residual income tax is less than provisional tax.

Interest is applied to the difference between the total

amount of tax assessed, including additional tax for late payment and underestimation and the amount of tax paid. It is calculated on a daily basis using the following formula:

$$\frac{a \times b}{365} \times c$$

where

- (a) is the amount underpaid/overpaid,
- (b) is the rate of interest - currently 10%,
- (c) is the number of days that interest is payable.

INTEREST APPLICATION DATE

Interest is imposed from the third provisional tax instalment date until the earlier of:

- the date of the assessment;
- the date the tax, including penalties, is paid in full;
- the terminal tax due date.

Should an assessment be issued more than thirty days before the residual income tax date, the amount of interest imposed at that assessment date will not change, provided the TOTAL amount assessed is paid within thirty days of the date of the assessment. The fact that residual income tax is not due until 7 February 1990 will not avoid the incurring of interest. The interest charge is for the "use of money". If payment is not received in full within this thirty day period, interest will continue to be charged from the date of the assessment to the residual income tax due date. In most cases this will be 7 February for 31 March balance dates. Any amounts outstanding beyond 7 February will attract late payment penalties.

EXAMPLE

Taxpayer is a Company

1988 provisional income is	\$55,000
1988 residual income tax is	\$26,400
Using the special company formula, 1989 provisional tax is	\$18,223

All instalments are paid in full on time

1989 provisional income is	\$75,000
1989 residual income tax is	\$21,000

1989 assessment issued 21 November 1989

As provisional tax paid is less than 1989 residual income tax, interest must be imposed.

1989 residual income tax is	\$21,000
1989 provisional tax paid is	<u>\$18,223</u>

Amount underpaid	\$2,777	a
Interest rate	10%	b
Number of days from 7 March 1989 to 20 November 1989	258	c

$$\frac{\$2,777 \times 10\%}{365} \times 258 \quad \$196.29$$

The 1989 assessment would show -	
1989 residual income tax	\$2,777.00
Interest	<u>\$ 196.20</u>
Total Payable	\$ 2,973.29

This amount would not increase if it was paid before 20 December 1989.

Inland Revenue will not pay out interest on voluntary payments.

Any interest charged or paid for use of money is neither assessable nor deductible to the taxpayer.

INCOME TAX TREATMENT OF BAD DEBTS SINCE THE INTRODUCTION OF THE ACCRUALS RULES

INTRODUCTION

This item states the Department's policy on the treatment of bad debts under the accrual provisions of the Act. Where the accruals provisions do not apply the Department's policy has not changed.

BACKGROUND

The accruals regime applies to financial arrangements. Therefore debt that has arisen under a financial arrangement, after the implementation date of that financial arrangement, is subject to the accruals treatment of bad debts.

Debt that arose before the relevant implementation date, or debt that is an excepted financial arrangement, is not subject to the accruals provisions and is treated in the same way as prior to the introduction of the accruals regime.

COMMENT

A bad debt comprising income from a financial arrangement previously returned by the taxpayer will be an allowable deduction under section 64G(1) of the Act.

A deduction for principal will only be allowable under section 64G(2) where the taxpayer is in the business of holding or dealing in such financial arrangements and the parties to the arrangement are not associated persons. A deduction for the principal will be allowed for a dealer who is an associated person under sections 104 and 106(1)(b) of the Act if section 106(1)(a) is satisfied. If the taxpayer is not in the business of holding or dealing in such financial

arrangements, a deduction will not allowable for the principal.

On the remission of the debt a base price adjustment is calculated. A deduction is only allowable under the base price adjustment for a holder who is

- (a) In the business of holding or dealing in such financial arrangements; and
- (b) Not an associated person with the debtor, - otherwise section 64F(6) applies.

Reference: Appendix C to TIB No. 3,
September 1989

INCOME TAX AMENDMENT ACT 1989: SUPERANNUATION

PIB No. 182 dealing with the Taxation Reform Bill (No. 5) 1988 included an outline of the new taxation regime applying to private superannuation.

Appendix D to this TIB provides a more extensive explanation of those provisions which were passed in the Income Tax Amendment Act 1976.

Reference: Appendix D to TIB No. 3
September 1989

WINDING UP DISTRIBUTION TAX (WUDT)

The last day for payment of WUDT is 30 September 1989, for companies who make distributions on or before 30 September 1989 (but after 1 April 1988), in the course of and for the purpose of winding up. All payments are to be made to:

The District Commissioner
Inland Revenue Department
Private Bag
Masterton.

WUDT is payable at the rate of ten percent of the amount of the dividend paid or distributed to the shareholders. The following information should accompany the WUDT payment:

- IR 4B - Return of Winding Up Distribution Tax
- A copy of the company balance sheet as at the balance date the immediately prior to the distribution.
- A list of all company and tax exempt shareholders and the amounts distributed to them.
- A copy of the resolution giving effect to the winding up.

Please note that if the WUDT is paid by 30 September 1989 the company's shareholders will not have to include the dividend in their personal income tax returns.

Reference: Income Tax Amendment Act
(No. 3) 1988
Sections 27, 28 and 29
Pamphlet IR 4P.

FBT AND MAJOR SHAREHOLDER- EMPLOYEES

The amendments contained in section 51 of the Income Tax Amendment Act (No. 5) 1988 extend the application of the Fringe Benefit Tax (FBT) regime to fringe benefits provided to major shareholder-employees.

Further amendments relating to the application of the FBT regime to overdrawn current accounts of shareholder-employees were made by section 33 of the Income Tax Amendment Act (No. 2) 1989 enacted on 26 July 1989.

Appendix E to this Bulletin explains the application of the amendments to the legislation.

Reference: Appendix E to TIB No. 3,
September 1989

DUE DATES REMINDER

- October 1 GST return and GST payment for period ended 31 August due.
 - October 7 Due date for payment of 1989 Land Tax. Due date to pay third instalment 1990 Provisional Tax for taxpayers with October 1988 balance dates. Due date to pay 1988 Terminal Tax for taxpayers with November balance dates. Due date to pay second instalment 1990 Provisional Tax for taxpayers with February balance dates. Due date to pay first instalment 1990 Provisional Tax for taxpayers with June Balance dates.
 - October 14 August Quarter's Dividend Withholding Payments due.
 - October 20 September Tax Deductions payment due September Non-Resident Withholding Tax Deductions payment due. FBT return and FBT payment for quarter ended 30 September due
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QUESTIONNAIRE

In TIB No.1, issued July 1989, we told you that we would include a questionnaire with TIB No. 3 so that you could let us know if you wished to receive just the TIB or the TIB plus Appendices. We also want to know what you think of the new format of the TIB and the questionnaire will now be included with TIB No. 5.

*TAX INFORMATION
BULLETIN*



THIS IS AN INLAND REVENUE DEPARTMENT SERVICE
TO PEOPLE WITH AN INTEREST IN THE TECHNICAL ASPECTS
OF TAXATION IN NEW ZEALAND.