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CONTENTS

| | |
|---|---|
| Accrual Regime Contact People | 2 |
| GST Letter Drop - an Apology | 2 |
| Accrual Tax Regime and Specified Leases | 2 |
| Inland Revenue's New Telephone Answering System | 3 |
| GST and Unconditional Gifts | 3 |
| Living Alone Payments - Correction | 4 |
| Family Support Legislation | 4 |
| Disclosure of Inter-Related Arrangement - Section 64H of the Income Tax Act 1976 | 4 |
| Income Equalisation Accounts and Resident Withholding Tax | 5 |
| Foreign Investment Fund Regime | 6 |
| Recent Determinations made by the Commissioner | 8 |
| New Technical Rulings Chapters | 9 |
| Due Dates Reminder | 9 |

Accrual Regime Contact People

In the August Tax Information Bulletin, we said that Accrual Contact People would soon be available in each of our offices to answer questions. These people have now been trained, and a list of their names is printed below.

| Office | Contact Person | Office | Contact Person |
|--------------------------|---------------------------------|--------------------------|--------------------------------|
| Auckland | Jim Baun | Lower Hutt | Philipa Foulds |
| Henderson | Reg Ratahi | Masterton | Murray Henderson |
| | Peter Boswell | Palmerston North | Ruth Hart |
| Manukau | Peter Borich | Porirua | Sandra de Ruiter |
| Otahuhu | David Lampp | Wanganui | Bruce Hutchins |
| Takapuna | John Colgan | Wellington | Phil Steere |
| Whangarei | Anne Puttnam | Central Regional Office | Brian McDiarmid |
| | Colin Spence | Regional liaison | Philipa Foulds (Lower Hutt) |
| Northern Regional Office | Bret Hart | | |
| Regional liaison | Beverly Fairfield (Takapuna) | Blenheim | Jeff Neal |
| | | Christchurch | Graham Gruschow |
| Gisborne | Keith Searle | | Steve Hayes |
| Hamilton | Carl Brandt | Dunedin | Greg Jarvis |
| | Jim Parkinson | Greymouth | Tony Gibson |
| | Alan Maine | Invercargill | Russell Grubb |
| Napier | Keith Jones | Nelson | Peter Scoon |
| New Plymouth | Bob Richards | Oamaru | Charles Fulton |
| Rotorua | Christine Groves | Timaru | Peter Hadlee |
| Tauranga | Martin Chapman | Southern Regional Office | Ray Bowden |
| Te Aroha | Phil Roberston | Regional liaison | Peter Truman (Dunedin) |
| Waikato Regional Office | Tony Baggs | | |
| Regional liaison | Barbara Glynn (Tauranga) | | |

GST Letter Drop - An Apology

Recently, we sent a letter to taxpayers advising them of changes to the Goods and Services Tax Act announced in the budget. In some cases, it went to taxpayers who were no longer registered for GST. Further, the letters to clients of tax practitioners went to their agents, rather than to the people themselves.

We apologise for these errors, which resulted from the use of incorrect criteria for the computer selection of those taxpayers to receive the letter. We have taken steps to make sure it does not happen again.

Inland Revenue regrets any inconvenience caused by this error.

Accrual Tax Regime and Specified Leases

This item sets out a method of calculating a lessor's income under a specified lease. In the case discussed, the lessor was involved in transactions with an overseas bank and overseas lessees. This topic was previously referred to in Public Information Bulletin No. 178, and was also set out in full in Technical Policy Circular No. 89/25. Since these were published Inland Revenue has received further requests for the information, so it is reproduced at Appendix A to this TIB.



Inland Revenue's New Telephone Answering System



Inland Revenue has introduced an automated call handling system in its larger offices. The new system is especially designed to improve our ability to respond to the needs of our clients and answer calls more quickly and efficiently.

Calls will generally be answered within 2 rings by our new self-directing telephone system. As soon as your call is answered you can dial the extension number required. If you do not know the extension number you want press 1, and the system will quickly guide you through the options available. If you do not wish to use any of the options you will be directed to the operator.

The system is designed for touch tone telephones. If you do not have a touch tone telephone you will be automatically directed to the operator after the initial greeting.

The system has been introduced into the following offices:

Head Office, Wellington, Lower Hutt, Porirua, Auckland, Manukau, Henderson, Otahuhu, Takapuna, Hamilton, New Plymouth, Tauranga, Christchurch, Napier, Dunedin, Whangarei and Invercargill. It will be introduced in Palmerston North office in mid-November.

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GST And Unconditional Gifts

The definition of unconditional gift is in section 2 of the Goods and Services Tax Act 1985. Payments falling within the definition of unconditional gift are excluded from the definition of consideration, the value of the supply is nil and no GST is payable.

Inland Revenue has reviewed the definition of unconditional gift. Whether a payment is an unconditional gift depends on the following factors:

- the payment must be a voluntary payment made to a non-profit body; and
- the donor (or an associated person) must either receive no benefit from the payment or, if they do receive a benefit, the benefit must not be conditional nor dependent on the payment. This means that there will only be an unconditional gift if the benefit arises irrespective of the payment being made; and

- a payment by the Crown or a public authority cannot be an unconditional gift.

The following are, and always have been considered, unconditional gifts:

- church plate collections;
- door to door appeals; and
- street collections;

This list is not exhaustive.

As a result of the review, Inland Revenue also considers that some school fee payments (but not school activity fee payments) to state schools may be unconditional gifts.

The policy is set out in full in Appendix B of this TIB.

Living Alone Payments

Section 25 of the Income Tax Amendment Act (No. 3) 1990

There was a mistake in the item on living alone payments that appeared in Appendix A to the Tax Information Bulletin Volume Two No.2 (August 1990).

The paragraph which explained the amendment to section 25 of the Income Tax Amendment Act (No.3) 1990 is correctly set out below.

Section 25 of the Amendment Act makes a consequential amendment to the definition of residual

income tax in section 375 of the principal Act. Residual income tax is the tax liability that remains after deducting all tax credits, source deduction payments and resident withholding tax. The source deduction payment that is made from the living alone payment is included in the list of deductions from the taxpayer's total tax liability in order to determine residual income tax.

Reference LA.ITAA (No.3) 1990

Family Support Legislation

The Social Welfare Amendment Bill (No.2) was introduced in Parliament on 5 September 1990. It contains amendments to give effect to the welfare system changes that were announced in this year's Budget.

Part VIII of the Bill repeals the Family Sup-

port and Guaranteed Minimum Family Income sections of the Income Tax Act 1976. The repeal date is 1 April 1991.

The legislation proposes that the tax credit schemes will still apply for the 1990-91 income year. For 1991-92 and future years the Family Support and Guaranteed Minimum Family Income assistance measures will be delivered under a new system, which will be administered by the Department of Social Welfare.

Disclosure of Inter-Related Arrangement under Section 64H of the Income Tax Act 1976

Exemption from the Requirement of Section 6H(1)

Section 64H(1) of the Income Tax Act 1976 requires every person who is a party to an "inter-related arrangement" to disclose certain details about that arrangement to the Commissioner.

Section 64H(2) allows the Commissioner to exempt certain persons or classes of persons from this disclosure requirement. The exemption dated 24 March 1988 made by the Commissioner had effect until the year ending 31 March 1990.

A further exemption on exactly the same terms as the previous exemption was made by the Commissioner on the 24 October 1990. This exemption has effect for the income year commencing 1 April 1990 and ending 31 March 1991 and is intended to maintain the status quo pending a review of the disclosure requirements under section 64H(2).

The full text of the exemption is in Appendix C to this TIB.

Review of Disclosure Requirements

Inland Revenue is carrying out a review of the disclosure requirements under section 64H(1), with a view to granting further exemptions from those disclosure requirements. If you would like to make a submission as to why a particular person or class of persons should be exempted from the disclosure requirements, please send it to:

The Manager (Technical Policy)
Head Office
Inland Revenue Department
PO Box 2198
WELLINGTON

Please note that the review is being carried out in the context of the existing legislation. Submissions should be in respect of exemptions under the existing section and not suggestions for changes in the legislation itself.

Income Equalisation Reserve Accounts and Resident Withholding Tax

Introduction

The question has been raised as to how the Resident Withholding Tax legislation applies to the interest paid on Income Equalisation Reserve Accounts.

Comment

There are three things to consider in relation to Income Equalisation Reserve Accounts and Resident Withholding Tax Credits.

1 When is the payer of the withholding income required to deduct Resident Withholding Tax?

Section 327C(1) of the Act states:

“... where a person makes a payment which consists in whole or in part of resident withholding income, that person shall, at the time of making the payment, make a deduction of tax (in this Act referred to as resident withholding tax)...”

This means that the payer of the interest income must deduct the resident withholding tax at the time he or she credits the interest to the recipient’s account. In the case of Income Equalisation Reserve Accounts, since the interest income is credited on 31 March, the payer is also required to deduct the Resident Withholding Tax on 31 March.

2 When is the recipient required to return the withholding income?

Section 179(3) states:

“... every refund of the whole or any part of any amount deposited under section 176 of this Act shall be deemed to have been made in respect of the accounting year in which the application for the refund is received by the Commissioner, and the amount of the refund shall be deemed to be assessable income derived by the taxpayer in that accounting year: ...”

This means that the recipient of the interest income is deemed to have derived assessable income in the accounting year in which the refund application is received.

3 When is the recipient entitled to claim the Resident Withholding credit?

Section 327K(2) sets out how RWT deductions are credited against tax liability. The section states:

“... where any resident withholding tax, ... , has been deducted from any amount, being...

(a) interest; ...

derived by any person in any income year, the Commissioner shall credit the resident withholding tax deducted in payment successively of -

(c) The income tax payable by the person for that income year:...”

This means that the recipient is entitled to claim the resident withholding tax credit in “that income year”, that is, the income year in which the income is derived, and where, under S 179(3), the refund is deemed to be derived in the income year in which the refund application is received.

Summary

Where interest is credited on deposits in an Income Equalisation Reserve Account at 31 March in an income year, and

(a) a refund is not applied for - the Resident Withholding Tax credit is not available as a credit in that income year.

(b) a refund is applied for - the Resident Withholding Tax credits on the amounts refunded are available as credits in that income year, i.e. the year of refund.

Reference: H.O. 10.F.1.5, TR Ch 58 Para 10

Foreign Investment Fund Regime

Recent Determinations made by the Commissioner

Introduction

The Commissioner made four determinations on 16 October 1990 under the Foreign Investment Fund (FIF) regime. They are the first such determinations to be made under section 245S(1) of the Income Tax Act 1976.

The determinations are outlined below, together with a brief explanation of the FIF regime and the rights and obligations of affected taxpayers. The determinations are reproduced in full as Appendix D to this TIB.

The FIF regime is part of the International Tax legislation effective from 1 April 1988. This legislation also included the Controlled Foreign Company (CFC) regime, which is outside the scope of this item.

Outline of Determinations made

Determination FIF1: Hill Samuel CSF Fund.

Determination FIF2: Lloyds International Growth Fund.

Determination FIF3: Lloyds International Pacific Fund.

Determination FIF4: Tyndall Overseas Fund Limited.

These four determinations are identical. As none of the exception criteria from the FIF regime are met, they conclude that rights held in the respective foreign entity (e.g. by way of shares or units), constitute an interest in a Foreign Investment Fund in relation to each foreign entity's accounting period ended 31 December 1988.

Objection rights to these determinations are set out below under the heading "Rights of Affected Taxpayers".

Effect of Determinations

These determinations confirm that under the FIF regime, New Zealand resident investors in these foreign entities are liable for income tax on the change in value of any shares or units held over their 1989 and/or 1990 income year. This is in addition to the tax liability on any distributions received.

Which income year is affected will depend on the balance date of the taxpayer; i.e. -

- People with balance dates from 31 December 1988 to 30 September 1989 will be liable in the 1989 income year. Most investors will be in this category.

- People with balance dates from 1 October 1989 to 30 December 1989 will be liable in the 1990 income year.

For all other income years, the FIF regime will apply to these four FIFs as it does for any foreign entity generally.

FIF Status Generally

The legislation relating to FIFs applies to any interest held in a foreign entity in accordance with section 245R(2)(a) or (b) of the Income Tax Act 1976. In particular, this applies to rights held in any foreign company or foreign unit trust (e.g. by way of shares or units), or beneficial interests held in a foreign superannuation scheme or policy of life insurance issued by an offshore entity.

Any such right or interest is effectively deemed to constitute an interest in a FIF, unless any of the exception criteria outlined below are met.

This legislative presumption puts the onus squarely on New Zealand resident investors to show that any one of the exception criteria are met before such an interest can be considered to be excepted from the FIF regime. If it cannot be established that any exception applies, then the obligations which arise are required to be fulfilled.

Exceptions from FIF Status

The most significant exception from the FIF regime is where the foreign entity is resident in either Australia, Canada, France, West Germany, Japan, the United Kingdom or USA. The other main exceptions relate to the foreign entity's level of distributions made, nature of assets held and level of taxes paid.

Determinations Procedure

The legislation contained in section 245S provides scope for any New Zealand resident investor in a foreign entity (or indeed the foreign entity itself) to apply to the Commissioner for a determination as to whether any of the exception criteria apply to a particular foreign entity.

The procedure for such applications is governed by the Income Tax (Foreign Investment Fund Determinations) Regulations 1989. These were reproduced as an appendix to Tax Information Bulletin No. 3, in September 1989. Also, an application form IR 100B has been produced to assist applicants in making

valid applications. Page 4 of that form contains a summary of the regulations referred to above.

Please note that the absence of a determination in relation to any particular foreign entity does not entitle any New Zealand resident investor in that entity to ignore their obligations under the FIF regime.

Obligations under the FIF regime

The obligations which arise under the FIF regime in relation to any FIF are as follows:

- to disclose any interest held in the particular FIF by completing Part A of the form IR 4H "Interest in a Foreign Investment Fund - Disclosure Schedule and Worksheet"; and
- to calculate the FIF income/loss by completing Part B of the form IR 4H; and
- to account for the FIF income or loss in the "Other Income" panel in the appropriate Income Tax return.

You must complete a separate IR 4H form for each FIF in which you hold an interest.

Amended Assessments Required

If you have already sent your 1989 and/or 1990 Tax Return to the Department without including your FIF income, you should -

- complete Parts A and B of the IR 4H form; and
- send the completed IR 4H form(s) to your local Inland Revenue office with a letter attached requesting that your 1989 and/or 1990 return be reassessed.

When we get the completed IR 4H form and letter, we will prepare and issue an amended 1989 and/or 1990 assessment for any further income tax payable.

Please note that if you have calculated 1990 FIF income and had previously opted to estimate your 1991 provisional tax, you may need to re-estimate your 1991 provisional tax liability.

Interests held in other Foreign Entities

You should follow the procedures outlined in this item where your obligations relating to interests in other FIFs have not yet been fulfilled.

Rights of Affected Taxpayers

Any person holding rights in any of the foreign entities referred to in this item (or the foreign entity itself) may formally object to the relevant determination.

Any objection must be in writing, stating the grounds of objection. It must be delivered to the Commissioner by 26 November 1990, which is one month from the date the determinations were published in the Gazette.

Any such objection should be directed to the following address:

The International Tax Central Unit
Inland Revenue Department
P. O. Box 895
Wellington.

Obligations under CFC regime

Please note that although an interest held in a foreign company or foreign unit trust may be excepted from the FIF regime, under the CFC regime an obligation does exist to disclose details of the interest held.

This obligation relates to the 1990 and later income years only and can be met by completing Part A of the form IR 4G "Interest in a Foreign Company - Disclosure Schedule and Worksheet".

Non-Compliance Implications / Penalty Provisions

All taxpayers should be aware that the penalties for non-compliance with obligations arising under the FIF (and CFC) regime are stronger than for other offences under the Act.

Specifically, conviction on any one of the offences listed below may result in up to two years' imprisonment and/or a fine of up to \$50,000.

- knowingly failing to disclose any information required in relation to a FIF;
- knowingly making a false declaration or giving false information to the Commissioner;
- aiding, abetting, or inciting the committing of any of the above.

This is in addition to the normal late payment penalties and penal tax which may be imposed.

Further Information

Further information regarding the FIF regime is provided in chapter three of the IR 275 booklet entitled "International Tax Guide".

That booklet and copies of the forms referred to in this item are available from all Inland Revenue offices.

Recent Determinations made by the Commissioner

The Commissioner signed six determinations on 24 October 1990. Below is a short explanation of each. The full determinations are printed in Appendix C to this TIB.

Determination G22:

This determination isolates the debt and equity components of a convertible note. It is necessary to separate the two elements in order to determine the income derived or expenditure incurred under sections 64B to 64M of the Act.

The equity component of a convertible note is an option to acquire shares. Options to acquire shares are excepted financial arrangements. Any income, gain or loss, or expenditure that is solely attributable to an excepted financial arrangement is not included in the income derived or expenditure incurred in respect of the convertible note under sections 64B to 64M of the Act (authority section 64CA).

This determination is issued pursuant to section 64E(1)(e) of the Act.

Determination G11A: Present Value Based Yield to Maturity Method

This determination rescinds and replaces Determination G11: Present Value Based Yield to Maturity Method signed by the Commissioner on the 21st day of November 1988. The determination differs from Determination G11 by the addition of an example of its application to perpetuities in which all payments are the same after some period.

This determination is issued pursuant to section 64E(1)(a) and section 64E(6) of the Act.

Determination G6C:

This determination rescinds and replaces Determination G6B: Foreign Currency Rates signed by the Commissioner on the 23rd day of April 1990. It includes a clause, at 6(3)(b)(ii), which was inadvertently excluded from the Determination G6B.

Determination G23:

This determination applies where for the purposes of calculating income or expenditure it is necessary to determine a yield or interest rate for valuation purposes. This rate is called the specified rate.

This is a multipurpose determination and will be applied as directed by another determination (e.g. Determination G22) which will detail the appropriate method to calculate income derived or expenditure incurred for a particular class of financial arrangement.

The determination is issued pursuant to sections 64E(1)(a) to (f) of the Act.

Determination G13A:

This determination rescinds and replaces Determination G13: Prices or Yields signed by the Commissioner on the 8th day of February 1989.

The amendment to the determination allows the use of prices or yields, other than those at which the person could trade the financial arrangement at, for valuation purposes provided that the alternative price or yield is adopted for all financial reporting purposes and does not result in a more favourable result for tax purposes.

This determination is issued pursuant to section 64E(1)(d) and section 64E(6) of the Act.

Determination G10B:

This determination rescinds and replaces Determination G10A: Present Value Calculation Methods signed by the Commissioner on the 23rd day of April 1990. It differs from its predecessor by modifying present value calculation Method A to enable it to apply to perpetuities.

This determination is issued pursuant to section 64E(1)(a) and section 64E(6) of the Act.



New Technical Rulings Chapters

Two more chapters of Inland Revenue's updated Technical Rulings are now available. These are:

Chapter 34: Estates and Trusts. This replaces Chapter 8 Parts 1,2 and 3. The GST-inclusive cost of chapter 34 is \$20.70.

Chapter 56: PAYE Tax Deductions. This replaces Part 1 of the previous Chapter 4. The GST-inclusive cost of Chapter 56 is \$32.00.

To purchase either of these chapters under section 15 of the Official Information Act, please send payment, along with your name and address, to:

Manual Sales Section
Inland Revenue Department
P O Box 2198
WELLINGTON

Due Dates Reminder

November

20 PAYE Deductions for first 15 days of November 1990 due - "Large" employers.

Tax Deductions for October 1990 due - "Small" employers.

30 Shareholder-employee statements and ACC Levy form ACC 506 with levy payment due (cases where remuneration was not calculated by 31 May 1990 or included in IR 68 Reconciliation).

December

1 GST Return and payment for period ended 31 October 1990 due.

5 Paye Deductions for last 15 days of November due - "Large" employers only.

7 First instalment of 1991 Provisional Tax due for taxpayers with August balance dates.

Second instalment of 1991 Provisional Tax due for taxpayers with April balance dates.

Third instalment of 1991 Provisional Tax due for taxpayers with December balance dates.

1989 Terminal Tax due for taxpayers with January balance dates.

14 Interest PAYE deducted during November 1990 due - monthly payers.

Dividend PAYE deducted during November 1990 due.

Non-Resident Withholding Tax deducted during November 1990 due.

20 PAYE Deductions for first 15 days of December 1990 due - "Large" employers.

Tax Deductions for November 1990 due - "Small" employers.

*TAX INFORMATION
BULLETIN*



INLAND
REVENUE

TE TARI TAAKE

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