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Inland Revenue
Te Tari Taake

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BINDING RULINGS

This section of the *TIB* contains binding rulings that the Commissioner of Inland Revenue has issued recently.

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For full details of how binding rulings work, see our information booklet *Adjudication & Rulings – a guide to Binding Rulings (IR 715)* or the article on page 1 of *Tax Information Bulletin* Vol 6, No 12 (May 1995) or Vol 7, No 2 (August 1995).

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PUBLIC RULING WITHDRAWN AND NEW PUBLIC RULING ISSUED

BR Pub 00/09 (Directors' fees and GST), published in *TIB* Vol 12, No 9 (September 2000), contained an application period that could be seen to be retrospective. This was not intended. The Commissioner's usual practice is to apply binding public rulings prospectively where his view of the law has altered. For that reason, BR Pub 00/09 has been withdrawn and a new public binding ruling, BR Pub 00/11, has been issued with a period of application from 26 October 2000 to 31 March 2005. The new public binding ruling is the same as the withdrawn ruling.

DIRECTORS' FEES AND GST

PUBLIC RULING BR Pub 00/11

This is a public ruling made under section 91D of the Tax Administration Act 1994.

Taxation Laws

All legislative references are to the Goods and Services Tax Act 1985 unless otherwise stated.

This Ruling applies in respect of sections 6(3)(b), 8, and 57(2)(b).

The Arrangement to which this Ruling applies

The Arrangement is the engagement, occupation, or employment as a director of a company. The engagement may either be by direct contract between the director and the company for whom the person acts as a director, or by a third party appointing, or agreeing to provide, a director to a company.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

- If a natural person is engaged as a director and the services are not undertaken as part of carrying on the person's own taxable activity, the engagement will be excluded from the term "taxable activity" due to the application of section 6(3)(b). The proviso does not apply as the services are not supplied as part of carrying on the person's taxable activity:
- If a natural person is engaged as a director as part of carrying on his or her taxable activity, the proviso to section 6(3)(b) will apply and the services will be deemed to be supplied in the course or furtherance of that taxable activity. If the person is registered for GST or is liable to be registered for GST, the person will be required to account for GST on the fees received for the supply of the directorship services:

- If a natural person is contracted by a third party to take up an engagement as a director of a company and the person has not accepted the directorship as part of carrying on a taxable activity:
  - the engagement of the natural person as a director will be excluded from the term "taxable activity" due to the application of section 6(3)(b). The proviso does not apply as the services are not supplied as part of carrying on the person's taxable activity;
  - the provision by the third party of the services of the natural person director does not fall within the provisions of section 6(3)(b), as the third party has not been engaged as a director of a company. If the third party is registered for GST or is liable to be registered for GST, that third party will be required to account for GST on the fees received for the supply of the person's services as a director of the company:
- If a natural person is contracted by a third party to take up an engagement as a director of a company and the engagement is part of carrying on the person's taxable activity:
  - the engagement of the natural person director will fall within the proviso to section 6(3)(b) and the services will be deemed to be supplied in the course or furtherance of the taxable activity;
  - the provision by the third party of the services of the director does not fall within the provisions of section 6(3)(b), as the third party is not engaged as a director of a company. If the third party is registered for GST or is liable to be registered for GST, that third party will be required to account for GST on the fees received for the supply of the person's services as a director of the company:
- If an employee, as part of his or her employment, is engaged as a director of a third party company by way of a contract between his or her employer and the third party company:
  - the engagement of the employee will fall within the provisions of section 6(3)(b) and is therefore excluded from the term "taxable activity". The proviso to the section does not apply as the services are not supplied as part of carrying on a taxable activity of the employee;
  - the provision by the employer of the services of a director does not fall within the provisions of section 6(3)(b), as the employer is not engaged as a director of a company. If the employer is registered for GST or is liable to be registered for GST, that employer will be required to account for GST on the fees received for the supply of the employee's services as a director of the company:
- If an employee is engaged by a third party company to be a director of that company, where: the employee is required to account to the employer for the directors fees received; there is no contract between the employer company and the third party company; and where the employee does not undertake the services as part of carrying on his or her own taxable activity:
  - the engagement as director will be excluded from the term "taxable activity" due to the application of section 6(3)(b). The proviso does not apply as the services are not supplied as part of carrying on the person's taxable activity;
  - if the employer is registered for GST or is liable to be registered for GST, the employer is required to account for GST on the consideration received for the supply of services to the employee, i.e. permitting the employee to be a director.
- If a partner in a partnership accepts an engagement as a director of a company as part of the partnership's business:
  - the activity of the partner, in accepting the engagement as a director, falls within the provisions of section 6(3)(b) and is therefore excluded from the term "taxable activity". The proviso to the section does not apply as, although the partner may be carrying on the taxable activity of the partnership, the services are deemed to be supplied by the partnership in terms of section 57(2)(b);
  - the provision by the partnership of the services of the director does not fall within the provisions of section 6(3)(b), as the partnership is not engaged as a director of a company. The partnership will be required to account for GST on the fees received for the supply of the partner's services as a director of the company as it is considered to be part of the normal taxable activity of the partnership.

The period for which this Ruling applies

This Ruling will apply to supplies made within the period 26 October 2000 to 31 March 2005.

This Ruling is signed by me on the 24th day of October 2000.

Martin Smith

General Manager (Adjudication and Rulings)

COMMENTARY ON PUBLIC RULING BR PUB 00/11

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusions reached in Public Ruling BR Pub 00/11 ("the Ruling").

Background

Section 6 defines the term "taxable activity" for the purposes of the Act. Under section 6(1), a person conducts a taxable activity when all of the following characteristics are present:

- There is some form of activity.
- The activity is carried on continuously or regularly.
- The activity involves, or is intended to involve, the supply of goods and services to another person for a consideration.

Section 6(3) provides certain exclusions from the term "taxable activity". Under section 6(3)(b), the activities of a salary and wage earner, or of a person in receipt of directors' fees, are excluded from the term.

Under the proviso to section 6(3)(b), if a person, in carrying on a taxable activity, accepts any office, any services supplied by that person in holding that office are deemed to be supplied in the course or furtherance of that taxable activity. Therefore, if a GST-registered sole trader takes on a company directorship in carrying on a taxable activity, the proviso applies and GST is chargeable on the directors' fees paid.

Public Information Bulletin (PIB) 164 issued in August 1987 contained an item titled "GST on Directors' Fees". The item concerned the circumstances in which directors' fees did and did not attract GST. The item listed indicators that could be used in identifying the correct GST treatment to be applied to directors' fees. These indicators were:

1. Directors' fees paid to directors personally, and retained by them.

   Not subject to GST—excluded from the meaning of taxable activity by section 6(3)(b).

2. Directors' fees paid to directors personally, but applied by them to their partnership or business income, where the partnership or business is a registered person.

   Subject to GST—subject to the proviso to section 6(3)(b).

3. Directors' fees paid directly to director's partnership or company, where that partnership or company is a registered person.

   Subject to GST—a normal taxable supply.

In July 1988 the Department issued *PIB* 175 containing, at page 26, a further item "GST on Directors' Fees", restricting the policy set down in *PIB* 164. The item advised that the proviso to section 6(3)(b) applies only to a sole trader, eg an accountant (being a registered person) who, in carrying on his or her taxable activity, is appointed a director of a company. The statement said that directors' fees paid to a partner in a partnership or to a shareholder, director, or employee of another company are not therefore subject to GST. The reason given for this interpretation was that, in terms of the Companies Act 1955, a director could only be a natural person. Therefore, directors' fees either paid to directors on behalf of their companies or partnerships, or paid directly to the company or partnership for directorship services carried out by their employees or partners, do not attract GST under this policy.

Inland Revenue published an interpretation statement in *Tax Information Bulletin* Vol 8, No 4 (September 1996) on "Tax deductions from directors' fees paid to GST-registered persons". This interpretation statement is also relevant to the subject matter of this Ruling, even though it deals with tax deductions under the Income Tax Act 1994. The statement says, at page 3, that if an employee is acting as a director of a company on behalf of another company, the directors' fees paid are for services rendered by the employer company. Regulation 4(2) of the Income Tax (Withholding Payments) Regulations 1979 ("the Regulations") states that payments for work done or services rendered by a company are not withholding payments. Therefore, tax deductions are not required to be made from the payments. Similarly, if a company pays directors' fees to a partnership account in return for the partner performing partnership services, the fees are business income of the partners and the Commissioner will not require tax deductions to be made under section NC 13 of the Income Tax Act 1994. Therefore, if it is the company or partnership that is providing the services of its employee or partner as a director, the question arises as to whether GST should be charged on these services as they would normally be supplied in the course or furtherance of a taxable activity of the company or partnership.

This Ruling replaces the policy items on "GST on Directors' Fees" contained in *PIBs* 164 and 175.

Legislation

The definition of the term "person" is contained in section 2(1) of the Act and states:

> includes a company, an unincorporated body of persons, a public authority, and a local authority

Section 2 also contains the definition of "registered person" being:

> … a person who is registered or is liable to be registered under this Act.

Section 6 states:

> (1) For the purposes of this Act, the term "taxable activity" means -
>
> (a) Any activity which is carried on continuously or regularly by any person, whether or not for a pecuniary profit, and involves or is intended to involve, in whole or in part, the supply of goods and services to any other person for a consideration; and includes any such activity carried on in the form of a business, trade, manufacture, profession, vocation, association, or club:
>
> (b) Without limiting the generality of paragraph (a) of this subsection, the activities of any public authority or any local authority.
>
> (2) Anything done in connection with the commencement or termination of a taxable activity shall be deemed to be carried out in the course or furtherance of that taxable activity.
>
> (3) Notwithstanding anything in subsections (1) and (2) of this section, for the purposes of this Act the term "taxable activity" shall not include, in relation to any person, -
>
> (a) Being a natural person, any activity carried on essentially as a private recreational pursuit or hobby; or
>
> (aa) Not being a natural person, any activity which, if it were carried on by a natural person, would be carried on essentially as a private recreational pursuit or hobby; or
>
> **(b) Any engagement, occupation, or employment under any contract of service or as a director of a company:**
>
> **Provided that where any person, in carrying on any taxable activity, accepts any office, any services supplied by that person as the holder of that office shall be deemed to be supplied in the course or furtherance of that taxable activity; or …** (Emphasis added)

Section 8(1), dealing with the imposition of goods and services tax, states:

> Subject to this Act, a tax, to be known as goods and services tax, shall be charged in accordance with the provisions of this Act at the rate of 12.5 percent on the supply (but not including an exempt supply) in New Zealand of goods and services, on or after the 1st day of October 1986, by a registered person in the course or furtherance of a taxable activity carried on by that person, by reference to the value of that supply.

Section 57, dealing with unincorporated bodies, states:

> (1) For the purposes of this section -
>
> "Body" means an unincorporated body of persons; and includes -
>
> (a) A partnership:
>
> (b) A joint venture:
>
> (c) The trustees of a trust:
>
> "Member" means a partner, a joint venturer, a trustee, or a member of any body:
>
> "Partnership" and "partner" have the same meanings as in the Partnership Act 1908.
>
> (2) Where a body that carries on any taxable activity is registered pursuant to this Act, -
>
> (a) The members of that body shall not themselves be registered or liable to be registered under this Act in relation to the carrying on of that taxable activity; and
>
> **(b) Any supply of goods and services made in the course of carrying on that taxable activity shall be deemed for the purposes of this Act to be supplied by that body, and shall be deemed not to be made by any member of that body; and**
>
> … (Emphasis added)

Section 151(3) of the Companies Act 1993 states:

> A person that is not a natural person cannot be a director of a company.

Application of the Legislation

Section 8(1) provides that GST is charged on the supply (but not an exempt supply) in New Zealand of goods and services by a registered person in the course or furtherance of a taxable activity carried on by that person.

Therefore, one of the determining features in ascertaining whether there is a liability to account for GST, is the existence of a "taxable activity". Another determining feature is whether the person is a "registered person".

Section 6(1) defines a "taxable activity" as an activity that is carried on continuously or regularly, and involves or is intended to involve the supply of goods and services to another person for a consideration. The section also includes within the term "taxable activity" the activities of any public or local authority.

Under section 6(2), anything done in connection with the commencement or termination of a taxable activity is deemed to be carried out in the course or furtherance of that taxable activity.

Paragraphs (a), (aa), (b), (c), and (d) of section 6(3) exclude from the term "taxable activity" such activities as hobbies, employment under a contract of service and engagement as a director of a company, certain Government-type and local authority appointments, and the making of exempt supplies.

The proviso to paragraph (b) states that if a person, in carrying on a taxable activity, accepts any office, services supplied by that person in holding that office are deemed to be supplied in the course or furtherance of that taxable activity. Therefore, if a person is carrying on a taxable activity, and accepts an engagement as a company director in carrying on **that** taxable activity, the proviso will apply.

If it is established that a taxable activity is in existence after applying section 6, the question of whether the person is liable to account for GST will depend on the application of the remaining criteria set down in section 8. One of these criteria is whether the person is a "registered person", ie whether the person is registered for GST or is liable to be registered for GST, which includes whether the taxable activity threshold amount in section 51 has been satisfied.

Section 57(2)(b) provides that where a partnership carries on a taxable activity, any supply of goods and services made as part of carrying on that taxable activity is deemed to be supplied by the partnership and not by any of the partners.

Section 151(3) of the Companies Act 1993 provides that only a natural person can be a director of a company.

The following scenarios illustrate how section 6(3)(b) is applied to a person engaged as a director of a company to determine the existence of a taxable activity. It is important to note that the Ruling itself deals specifically with section 6(3)(b). If it is established that an activity does not fall within the exclusion from a "taxable activity" set down in that section, the remaining criteria under section 8 must be applied in order to determine the existence of a liability to account for GST.

Note that it is the contractual relationship between the parties, founded on a genuine basis, that determines the GST treatment of the relevant transactions (*Wilson & Horton v CIR* (1995) 17 NZTC 12,325).

A. Personal capacity

A natural person is engaged as a director of a company in that person's personal capacity and not as part of carrying on any taxable activity.

The activity of this person falls within the provisions of section 6(3)(b) in that it involves a person who is engaged as a director of a company. The activity is therefore excluded from the term "taxable activity". The proviso does not apply, as the person has not accepted the engagement as part of carrying on a taxable activity.

B. Carrying on a taxable activity

A natural person is engaged as a director of a company as part of carrying on that person's taxable activity.

The activity of this person falls within the provisions of section 6(3)(b) in that it involves a person who is engaged as a director of a company. The activity is therefore *prima facie* excluded from the term "taxable activity". However, as the person has accepted the engagement as part of carrying on a taxable activity, the proviso deems the services to be supplied in the course or furtherance of that taxable activity. If the person is registered for GST or is liable to be registered for GST, the person will be required to account for GST on the fees received for the supply of the directorship services.

C. Person contracted as a company director

A natural person is contracted by a third party to take up an engagement as a director of a company. The person is not undertaking the directorship as part of carrying on any taxable activity. The third party invoices the company for its services in providing it with a director.

The engagement of the person as a director of a company is excluded from the term "taxable activity" under section 6(3)(b). The proviso to the section does not apply as the services are not supplied as part of carrying on the person's taxable activity. The provision by the third party of the services of the director does not fall within the provisions of section 6(3)(b), as the third party is not engaged as a director of a company. Provided the third party is registered for GST, or is liable to be registered for GST, that party will be required to account for GST on the fees received for the supply of the services of the person as a director of the company.

D. Person contracted as a company director in carrying on a taxable activity

A natural person, as part of carrying on a taxable activity, is contracted by a third party to take up an engagement as a director of a company. The third party invoices the company for providing the services of the director, who in turn invoices the third party for his or her services.

The engagement of the person as a director of a company is *prima facie* excluded from the term "taxable activity" under section 6(3)(b). However, as the person has accepted the engagement as part of carrying on a taxable activity, the proviso to the section deems the directorship services to be supplied in the course or furtherance of that taxable activity. The natural person's liability for GST will therefore depend on satisfying the remaining requirements of section 8. The provision by the third party of the services of the director does not fall within the provisions of section 6(3)(b) as the third party is not engaged as a director of a company. Provided the third party is registered for GST or is liable to be registered for GST, that party will be required to account for GST on the fees received for the supply of the person's directorship services.

E. Employee engaged as director

An employee of an employer is engaged as a director of a third party company as part of the person's employment duties.

The engagement of this person as a director of a company is excluded from the term "taxable activity" under section 6(3)(b). The proviso to the section does not apply as the person has not accepted the directorship as part of carrying on a taxable activity—the person is merely carrying out employment duties.

The provisions of section 6(3)(b) do not apply to the employer who is supplying the services of its employee as the employer is not engaged as a director of a company. Provided the employer is registered for GST, or is liable to be registered for GST, that party will be required to account for GST on the fees received for the supply of the services of the person as a director of the company.

F. Employee required to pay over directors' fees to employer

Sometimes an employee is permitted to accept directorships of third party companies provided the employee accounts to the employer for the fees received. This might occur with family companies. In this type of scenario there would not be a contract between the employer and the third party company.

In this situation, the engagement of the person as a director of a company is excluded from the term "taxable activity" under section 6(3)(b). The proviso to the section does not apply as the person has not accepted the directorship as part of carrying on a taxable activity. The employer company, provided it is registered for GST, or liable to be registered for GST, will be required to account for GST on the supply of services to the employee. These services could best be described as allowing the employee to undertake directorship duties in work time or permitting the employee to be a director.

G. Partner in a partnership engaged as a director

A partner in a partnership accepts an engagement as a director of a company as part of the partnership's business.

The engagement of this person as a director of a company is excluded from the term "taxable activity" under section 6(3)(b). The proviso to the section does not apply as, although the partner may be carrying on the taxable activity of the partnership, the services are deemed to be supplied by the partnership in terms of section 57(2)(b). Therefore, the partner is not required to account for GST on the supply of the directorship services. Section 6(3)(b) does not apply in the case of the partnership as the partnership is not engaged as a director of a company. The partnership supplies the services of one of its partners to the company as part of its taxable activity. The partnership will therefore be required to account for GST on the fees received for the supply of the partner's directorship services.

Examples

Example 1

Taxpayer A, who is not registered for GST, is a partner in a firm of chartered accountants. Company B engages taxpayer A as a director, and pays him fees for his services. Taxpayer A's appointment as a director is not connected with his involvement in the partnership nor has he accepted the directorship as part of carrying on a taxable activity. He retains the fees, having received them in his personal capacity.

Taxpayer A is engaged as a director of a company, an activity that is excluded from the term "taxable activity" by section 6(3)(b). The proviso to the section does not apply, as taxpayer A is not providing directorship services as part of carrying on a taxable activity. Taxpayer A is not required to account for GST on the fees received for directorship services.

Example 2

Taxpayer B is a human resources consultant in business on her own. She is registered for GST. She accepts a company directorship as part of carrying on her taxable activity, and receives fees for her services.

Taxpayer B's engagement as a director is *prima facie* excluded from the term "taxable activity" in terms of section 6(3)(b). However, as she has accepted the engagement as part of carrying on her taxable activity, the proviso to the section deems the directorship services to be supplied in the course or furtherance of her taxable activity. She should therefore account for GST on the fees she is paid.

Example 3

A GST-registered financial management company supplies the services of one of its specialist employees as a director of another company. Directors' fees are paid to the company for the services provided.

The engagement of the employee as a director is excluded from the term "taxable activity" under section 6(3)(b). The proviso does not apply as the employee has not accepted the office as part of carrying on a taxable activity. Therefore, the employee is not required to account for GST on the supply of the directorship services. Section 6(3)(b) does not apply to the activity of the management company as that company is not engaged as a company director. The fees are paid in consideration of the management company providing the services of one of its employees to the other company. This is a supply in the course or furtherance of a taxable activity of the management company and that company will be required to account for GST on the fees received for this supply.

Example 4

A partner of a GST-registered legal partnership is elected onto the board of directors of a client company as a representative of the partnership. The partnership is providing legal advice to the company, which in turn pays fees into the partnership's account.

The engagement of the partner as a director of a company falls within the provisions of section 6(3)(b) and is therefore excluded from the term "taxable activity". The proviso to the section does not apply as, although the partner may be carrying on the taxable activity of the partnership, the services are deemed to be supplied by the partnership in terms of section 57(2)(b). Therefore, the partner is not required to account for GST on the supply of the directorship services. The provisions of section 6(3)(b) do not apply to the partnership as it is not engaged as a director of a company.

The partnership will therefore be required to account for GST on the fees it receives from the company.

Example 5

A GST-registered accountant in business on his own is contracted by a consulting firm to take up an engagement as a director of a company with the object of monitoring the company's financial systems.

The engagement of the accountant as a director of a company is excluded from the term "taxable activity" under section 6(3)(b). However, as the person has accepted the engagement as part of carrying on his taxable activity, the proviso to the section deems the directorship services to be supplied in the course or furtherance of his taxable activity. The accountant will therefore be required to account for GST on the fees he receives in respect of these services. The provision by the consulting firm of the services of the accountant does not fall within the provisions of section 6(3)(b) as the firm is not engaged as a director of a company. Provided the consulting firm is registered for GST or is liable to be registered for GST, it will be required to account for GST on the fees received for the supply of the directorship services of the accountant.

Example 6

Company A agrees to one of its employees taking up a directorship position with Company X on the proviso that the employee hands over the directors' fees payable to the employee by Company X. There is no contract between Company A and Company X.

The engagement of the employee as a director is excluded from the term "taxable activity" under section 6(3)(b). The proviso does not apply as the employee has not accepted the office as part of carrying on a taxable activity. Therefore, the employee is not required to account for GST on the supply of the directorship services. If Company A is registered for GST or is liable to be registered for GST, it is required to account for GST on the supply of services, ie permitting the employee to be a director of Company X.

NEW LEGISLATION

TAXATION (FBT, SSCWT AND REMEDIAL MATTERS) ACT 2000 00/34

SECURITIES AMENDMENT ACT 00/35

The Taxation (FBT, SSCWT and Remedial Matters) Bill was introduced into Parliament in March 2000. The legislation resulting from the bill's passage through Parliament was enacted as two separate Acts in September 2000:

- The Taxation (FBT, SSCWT and Remedial Matters) Act 2000, and
- The Securities Amendment Act.

The main features of the legislation are the introduction of a multi-rate fringe benefit tax and a superannuation fund withdrawal tax to counter avoidance of the top personal tax rate through the use of employer contributions to superannuation funds.

POLICY ISSUES

SUPERANNUATION FUND WITHDRAWAL TAX

Sections CL 3-21, EN 6-7, NE 2, NE 2AA, NE 3, NEA 1 of the Income Tax Act 1994; sections 32A–32C and 165AA of the Tax Administration Act 1994; section 7A of the Securities Act 1978

Introduction

A new legislative measure is intended to counter avoidance of the top personal tax rate through the use of employer contributions to superannuation funds. In certain circumstances, a 5% fund withdrawal tax will apply to withdrawals from superannuation funds.

Background

The specified superannuation contribution withholding tax (SSCWT), set at 33%, is a tax on employers' contributions to superannuation funds.

Increasing the top personal tax rate to 39% from 1 April this year and leaving the SSCWT rate unchanged at 33% introduced scope for avoidance of the 39% rate. Employees earning over $60,000 could have negotiated an increase in their employer superannuation contributions, which are subject to the 33% SSCWT rate, with a corresponding reduction in salary and wages subject to tax at 39%. They could have withdrawn the increased employer contributions shortly afterwards, thus avoiding the 39% top personal tax rate.

The fund withdrawal tax is intended to remove this avoidance concern. It works by applying a 5% tax on certain withdrawals from superannuation funds. The principal exemptions are for withdrawals when ceasing employment and for reasons of significant financial hardship, and by those earning under $60,000 a year.

The measure has been designed to prevent avoidance of the 39% rate without creating disincentives for increasing superannuation savings.

At 5%, the fund withdrawal tax should remove the tax benefit for those earning over $60,000 a year from substituting employer contributions to a superannuation fund for salary and wages. However, the Government signalled in its report to the Finance and Expenditure Committee on the submissions received that the measure is anti-avoidance in nature and if significant revenue is received by way of this tax the rate will be reviewed.

Key features

- A withdrawal tax of 5% of the amount withdrawn from a superannuation fund will apply to certain withdrawals. If the trustee can identify the amount of the employer contribution on a member's behalf, only that amount may be taxed.
- Contributions made before 1 April 2000 and contributions that continue at levels set before that date are not subject to the withdrawal tax.
- The tax on a withdrawal is payable by superannuation fund trustees in the following income year unless the superannuation fund winds up or leaves New Zealand. This measure is intended to address a number of provisional tax and use-of-money interest issues.
- The legislation allows superannuation fund trustees to withhold the withdrawal tax from a withdrawal as well as recover any withdrawal tax due from any member if insufficient tax was withheld from a withdrawal.
- Members and trustees may request from members, employers and other superannuation funds any information necessary to apply the withdrawal tax. Trustees may rely on the information provided as being correct unless there are reasonable grounds for them to believe the information is not correct.

Withdrawal exemptions

- The withdrawal tax does not apply to funds that are withdrawn on, shortly before, or after an employee ceases employment except in limited circumstances.
- The tax does not apply to withdrawals made for reasons of significant financial hardship. A list of circumstances that may give rise to significant financial hardship is included in the legislation to provide guidance to trustees.
- The withdrawal tax does not apply to withdrawals necessary to settle the division of matrimonial property.
- An exemption is provided for those earning less than $60,000 a year. If in any of the four income years preceding the year of a withdrawal, a member's taxable income, including employer specified superannuation contributions, is less than $60,000, the withdrawal tax will be reduced by 25%. This means that, if in all four years the $60,000 threshold is not exceeded, no withdrawal tax applies at all.
- Withdrawals made on the basis of partial retirement are also exempt. Partial retirement occurs when:
  - the member works less than 30 hours per week
  - has reduced working hours as a lead-in to full retirement
  - provides written notification that he or she does not intend to increase hours in paid employment in the future
  - the employer certifies that there is no understanding to increase work hours in the future, and
  - all employer and employee contributions to a superannuation fund cease.
- Withdrawals used to purchase a life annuity, or one to be paid over ten or more years, are not subject to the withdrawal tax. The same provisions apply to pensions with those terms.
- Withdrawals to meet fund administration costs and the costs of group and individual life, health, sickness or accident insurance on behalf of members are exempt.

Although the legislation provides exemptions for certain types of withdrawal, such as withdrawals on the grounds of partial retirement, they can only take place if authorised by the superannuation fund's trust deed. For example, if a superannuation fund trust deed does not provide for an inservice withdrawal, any exemption and those provisions relating to inservice withdrawals are not relevant to that fund or its members.

Treatment of transfers to or from superannuation funds and superannuation schemes

Table 1 outlines the withdrawal tax treatment of a transfer from a superannuation fund or scheme to another superannuation fund or scheme—for example, from a superannuation fund to a foreign superannuation scheme.

Table 1. Tax treatment of transfers

Transfers[1]	To a superannuation fund	To a defined benefit superannuation fund	To a superannuation scheme	To a foreign superannuation scheme
From a superannuation fund				
• Supporting information provided	Transfers retain their same nature as in transferring fund[2] (Section CL 14(1))	Grandparented and employee contributions retain their nature[2] (Section CL 14(3))	Withdrawal[4] (Section CL 14(1))	Withdrawal[4]
• Supporting information not provided	Treated as employer contributions to superannuation savings (Section CL 14(2))	CL 4 applies subject to exemption application[3] (Section CL 14(4))	Withdrawal[4]	Withdrawal[4]
From a defined benefit superannuation fund				
• Supporting information provided	Transfers keep same nature as in transferring fund[2]	Grandparented and employee contributions retain their nature	Withdrawal[4]	Withdrawal[4]
• Supporting information not provided	Treated as employer contributions to superannuation savings	CL 4 applies subject to exemption application[3]	Withdrawal[4]	Withdrawal[4]
From a superannuation scheme	Treated as member contributions	Treated as member contributions	n/a[5]	n/a[5]
From a foreign superannuation scheme	Treated as member contributions	Treated as member contributions	n/a[5]	n/a[5]

Note:
1. Section CL 13 deems a transfer to be a withdrawal.
2. "Retain their nature" is considered to mean that employer contributions received from a transferring fund continue to be treated as employer contributions. See discussion in section CL 14 for full discussion.
3. Not deemed to be employer contribution to superannuation saving as the rules for defined benefit fund rules work by taxing withdrawals other than those grandparented, exempt or made by members.
4. No specific rules so transfer is simply treated as withdrawal.
5. The withdrawal tax affects only superannuation funds. Transfers between schemes do not enter the withdrawal tax base except to the extent that a scheme making a transfer was previously a superannuation fund, in which case the superannuation fund rules apply.

Other features

- Employees may elect, with the approval of their employer, that a 39% SSCWT rate apply to specified superannuation contributions made by the employer on the employee's behalf. Only employees who earn over $60,000 a year are likely to use this option.
- Employees may elect to apply the optional 39 percent SSCWT rate from 1 October 2000.
- Employees may also elect to apply the PAYE rules to an employer superannuation contribution.

Application date

The withdrawal tax rules apply from 14 September 2000. From that date, withdrawals may be subject to withdrawal tax. However, the withdrawal tax exemption for withdrawals of existing amounts in a superannuation fund applies to employer contributions up to and including 31 March 2000. Employer contributions after that date may be subject to the withdrawal tax if withdrawn after 14 September 2000. Similarly, the exemption for employer contributions that have not increased is based on the employee's last pay period ending before 1 April 2000.

The option to elect a 39% SSCWT rate applies from 1 October 2000.

Detailed analysis

Key definitions

Superannuation fund is a superannuation scheme registered under the Superannuation Schemes Act 1989.

Superannuation scheme is any:

(a) trust or unit trust established by its trust deed principally for the purpose of providing retirement benefits to beneficiaries who are natural persons, or

(b) company (not being a unit trust) that is not resident in New Zealand which has been established principally for the purpose of providing retirement benefits to members or relatives of members who are natural persons

(c) arrangement constituted under an Act of Parliament principally for the purpose of providing retirement benefits to natural persons other than the Social Security Act 1964, and

(d) similar legislative arrangement as detailed in paragraph (c) constituted under the legislation of a country outside New Zealand.

Defined benefit fund is a superannuation scheme registered under the Superannuation Schemes Act 1989 that must comply with section 15(1)(a) of that Act. Section 15(1)(a) refers to a scheme acting on the principle of unallocated funding. This definition is included in section OB 1 of the Income Tax Act 1994.

SECTION CL 3: EXEMPTIONS

Grandparenting exemptions – contributions made before 1 April 2000

Subsection (1)(a) provides an exemption for the withdrawal of any amount that exists in a superannuation fund on the close of business on 31 March 2000.

As a superannuation fund may not balance on 31 March 2000, the compliance cost of determining the amount existing in a fund on that date may be high. Therefore, a superannuation fund has the option of determining the amount existing in a superannuation fund as at the fund's balance date immediately preceding 1 April 2000.

This exemption also applies to an amount which existed in a different superannuation fund as at 1 April 2000, which has subsequently been transferred under section Cl 14(1) and is now being withdrawn.

Subsection(1)(b) exempts earnings on those amounts existing in a superannuation fund at 31 March or the balance date chosen by the fund. This exemption for earnings on the grandparented amounts reflects a general approach in the withdrawal tax rules that returns take the underlying nature of the funds generating them.

These exemptions reflect that contributions made before 1 April 2000 occurred before the increase in the top personal tax rate to 39%. As the 6% margin between the top tax rate and the SSCWT rate came into being from 1 April 2000, contributions made before that date could not have been made with the intention of avoiding the 39% rate. Therefore they are not subject to the withdrawal tax.

Subsection(1)(a) is supported by Section CL 3(2), which requires the value used to determine an amount that exists in a superannuation fund to be the market value.

Section CL 3(3) covers contributions due to, but not received by, a superannuation fund on the date the fund chooses to balance. The best example of the application of this rule would be specified superannuation contribution deductions made by employers but not yet paid to a superannuation fund. This subsection provides that amounts due but not received at 31 March 2000, or the balance date of the fund (if elected), still comprise part of the balance of the fund.

Employee contributions exemption

Subsection(1)(c) exempts withdrawals of member contributions because they are made from after-tax income. The term "member contributions" is defined in section OB 1 to include any return on those contributions.

The use of the word "return" in the context of these provisions refers to any fund earnings attributable to that contribution, whether taxable or non-taxable. For example, for the purposes of the withdrawal tax, the withdrawal of a return on employer contributions to superannuation savings is potentially liable, even though it may not have been taxable for income tax purposes.

Grandparenting exemption – locked-in contribution level

Subsection(1)(d) provides grandparenting for employer contributions to superannuation savings that continue at existing levels. This measure reduces compliance costs and reflects the fact that the contribution levels were set before the increase in the top marginal tax rate gave rise to a tax advantage from salary sacrifice.

The exemption continues as long as the level of contribution does not increase from what it was on the last pay period ending before 1 April 2000. If the level of contributions increases, all contributions are then liable.

Definition of "employer contributions to superannuation savings"

The definition of "employer contributions to superannuation savings" means specified superannuation contributions made on or after 1 April 2000 other than:

- Contributions subject to the 39% SSCWT rate. The election of the 39% withholding rate is provided for under section NE 2AA and removes any salary sacrifice concern.
- Specified superannuation contributions treated as salary or wages under section NE 2A.

The definition also includes any returns on the liable specified superannuation contributions and reserves. The extent to which reserves are included depends on the size of the superannuation fund. "Reserves" are defined as specified superannuation contributions made on or after 1 April 2000 that do not vest in a member.

The reserves of a superannuation fund with ten or more unassociated members include those that have been allocated to a member of a superannuation fund other than those allocated for smoothing investment returns. This measure is included to reduce the compliance costs that larger superannuation funds would incur in having to track reserves accurately.

Although the term "smoothing investment returns" is not defined, the concept of smoothing is considered to be one of lowering returns to members in years the fund has a higher than average return, and raising the return in years of lower returns to maintain an average return. As part of that smoothing policy, specified superannuation contributions may be included.

In the case of all other superannuation funds with nine or fewer members, all reserves (as defined) are treated as employer contributions to retirement savings.

In this provision the general Income Tax Act definition of "associated person" in section OD 7 applies. This means that natural persons are associated if connected by blood relationship (within the fourth degree), marriage, or adoption. Further, a person is associated with another person if their marriage partner has a blood relationship with that second person.

Definition of not increasing contributions

Section CL 3(4) provides that an employer is not treated as increasing the level of specified superannuation contributions if the increase is required by a trust deed or a contract in existence before 1 April 2000. An increase in the level of employer contributions does not include an increase in the amount of contributions if the percentage of salary remains the same. Therefore, if an employee's pay increase does not change an employer's percentage contribution rate, no increase in employer contribution has occurred for the purpose of this section.

Expense exemptions

Subsection(1)(e), (f) and (g) provide exemptions for withdrawals from a member's account to meet superannuation fund administration costs, and for group or individual life, health, sickness and accident insurance. The exemptions recognise that these withdrawals are necessary for effective management of the superannuation fund. Section CL 3(6) defines "fund administration costs" to be the fees and expenses associated with the management and marketing of the superannuation fund.

Various classes of insurance are also exempted. The reason is that these types of insurance are common to many superannuation funds, and imposing the tax on withdrawals to provide these benefits would significantly affect the structure of the industry and impose significant compliance costs.

Subsection(1)(h) exempts withdrawals to pay an amount claimed under paragraphs (f) or (g). The combined effect of paragraphs (f), (g) and (h) is that withdrawals from a fund to pay the various listed types of insurance are exempt, and if a claim under an insurance policy is made, paying that claim out to a member is also exempt.

Transfer exemptions

Subsection(1)(i) and (j) provide exemptions for direct transfers of an amount from a superannuation fund to another superannuation fund and from a superannuation fund that is winding up to another superannuation fund.

As the definition of "superannuation fund" includes defined benefit superannuation funds, these exemptions also apply to transfers from those funds.

The objective of these exemptions is to avoid withdrawals from a superannuation fund triggering the withdrawal tax when the amount being withdrawn is not actually received by the member.

The term "direct transfer" is a payment by a superannuation fund to another superannuation fund without the amount being physically received by the member (at which point there is a risk that the member may not transfer the amount withdrawn from the first fund to the second fund). Direct transfer also includes the member authorising a superannuation fund to make payment as agent to another superannuation fund.

Ordering of withdrawals

Given the various exemptions and the different treatment accorded employer, employee and grandparented contributions, different tax outcomes can arise depending on the ordering of the amounts withdrawn. The withdrawal tax does not provide any ordering rules. For example, the legislation does not presume, or specify, that withdrawals have to be on a first-in, first-out basis. The ordering of withdrawals is a matter for the member making the withdrawal and the trustee of the superannuation fund involved.

SECTION CL 4: IMPOSITION OF WITHDRAWAL TAX

Under section CL 4(1), superannuation funds subject to these rules are those receiving employer contributions on behalf of members and those receiving transfers from other superannuation funds. The second inclusion reflects the fact that no tax is paid when a superannuation fund makes a direct transfer to another superannuation fund, so the fund receiving the transfer becomes liable if the transferred amount is withdrawn.

Section CL 4(2) establishes the amount of the withdrawal which is gross income to the superannuation fund. This is:

Gross income equals:	0.05	x	amount
	tax rate		withdrawn

Given the 33% tax rate on superannuation funds, this formula results in 15.15% of any withdrawal being gross income to a superannuation fund. Multiplied by the 33% tax rate, this results in a tax liability equal to 5% of the amount withdrawn—the rate of withdrawal tax set by the Government.

Subsection (2) provides that the full amount of the withdrawal is liable. The issue of limiting this to employer contributions is dealt with under subsection (6) (***Employer contributions of superannuation savings restriction*** on page 17).

Exemption for those earning under $60,000

Sections CL 4(3) and (4) provide the exemption for those earning under $60,000 a year.

If in any of the four income years preceding the year of withdrawal, the member's taxable income, including his or her employer specified superannuation contributions, is less than $60,000, the withdrawal tax is reduced by 25%. Application of this provision requires the superannuation fund to know whether the member's income is less than the threshold, otherwise the withdrawal tax applies in full. The provisions in the new sections 32A and 32B of the Tax Administration Act 1994 allow members and superannuation fund trustees to request the required information from employers. Employer specified superannuation contributions are the gross contributions by the employer before SSCWT applies.

This provision requires the member's gross income and employer contributions to be less than $60,000. It is not necessary to determine this total to the cent in every case, but simply to ensure that the result would be over or under the threshold. It is only close to the threshold that a higher level of accuracy is required.

For example:

- Members earning $70,000 over each of the last four income years need not request from their employer their employer superannuation contribution levels to determine that the exemption does not apply.
- Members earning $30,000 each year with an employer contributing 5% of salary need not establish the level of employer superannuation contributions on their behalf to determine that the exemption does apply.

The exemption is based on the four income years before that in which the withdrawal is made. The income and employer contributions in the income year the withdrawal is made are excluded, as determining a likely current year income and employer contribution would have significant compliance costs with possibly little, or no, increase in the accuracy of the application of the exemption.

Non-monetary withdrawals

Section CL 4(5) ensures that non-monetary withdrawals have their monetary value for withdrawal tax purposes.

Employer contributions of superannuation savings restriction

Subsection CL 4(6) provides that the application of the withdrawal tax is limited to employer contributions to superannuation savings if these can be established.

In effect, subsection CL 4(2) provides that if no information about the nature of the withdrawal is available, the full amount is liable. Subsection (6) limits the application if the information necessary to calculate the employer contribution component is available. (Section CL 3(1)(a) – (d) limits the application of the tax to the extent that information on those amounts, rather than information on employer contributions, is available.)

To ensure that trustees can obtain the necessary information, new powers for trustees to request information are included in sections 32A to 32C of the Tax Administration Act.

SECTION CL 5 TO 12 EXCEPTIONS

Sections CL 5 to CL 12 provide exemptions for withdrawals made for reasons of significant hardship, matrimonial property settlements, annuities and pensions, cessation of employment and partial retirement.

SECTION CL 5: HARDSHIP EXEMPTION

Section CL 5 provides that a withdrawal is exempt to the extent that it is necessary to alleviate significant financial hardship. Subsection (2) provides a list of difficulties that may cause significant financial hardship:

(a) a member's inability to carry out his or her usual occupation because of temporary illness, injury or disability, or permanent illness, injury or disability

(b) a member's inability to meet minimum living expenses

(c) a member's inability to meet mortgage repayments on the principal family residence to such an extent that the mortgagee is seeking to foreclose

(d) the cost of modifying a residence to meet special needs arising from the disability of a member or a member's dependant

(e) the cost of medical treatment for the illness or injury of a member or a member's dependant

(f) the cost of palliative care for a member or a member's dependant

(g) the cost of a funeral or burial for a deceased member or a member's dependant.

The list is not intended to be exhaustive, rather it is set as a guide to the circumstances that should be considered for significant financial hardship. This is reflected in the fact that the definition of "significant financial hardship" is inclusive, allowing other circumstances also to be considered.

The existence of any of these circumstances in themselves, with the exception of paragraphs (b) and (c), is not sufficient to constitute serious financial hardship—rather, they must give rise to serious financial hardship for the member. For example, paragraph (e) specifies the cost of medical treatment as a circumstance which may result in the significant financial hardship exemption applying. However, if these medical costs were minor, meeting them might not impose significant financial hardship, so any fund withdrawal to cover these costs would be liable if not otherwise exempt.

The events referred to in paragraphs (b) and (c) are slightly different from the other circumstances in that they, in themselves, are likely to constitute significant financial hardship.

SECTION CL 6: MATRIMONIAL PROPERTY EXEMPTION

Section CL 6 provides that a withdrawal is exempt to the extent necessary to settle a division of matrimonial property upon separation or dissolution of marriage. A withdrawal of property as part of a matrimonial property agreement alone, rather than as a consequence of separation or dissolution of marriage, will be liable provided the other exemptions do not apply.

SECTION CL 7: PENSIONS AND ANNUITY EXEMPTION

Section CL 7 exempts withdrawals as annuities or pensions. A restriction applies in that the annuity or pension must be payable for life or ten or more years. This does not mean that the annuity must be paid for ten years, but that is the period the annuity must cover on issue. Also exempted are withdrawals to purchase an annuity meeting the above restrictions.

Deliberate use of pensions and annuities to avoid the withdrawal tax—for example, by a person commuting an annuity (receiving its cash value) immediately after issue—may be subject to the application of the anti-avoidance provisions of the Income Tax Act.

CESSATION OF EMPLOYMENT

Section CL 8: Cessation of employment exemption

Section CL 8 provides for an exemption for withdrawals on or after, or shortly before, cessation of employment. "Cessation of employment" is defined in section CL 11.

Subsection (1) establishes that a withdrawal on or after cessation of employment is not subject to the tax if employment ceased because of injury, disablement or death. In effect, this provision ensures that withdrawals in these cases will be exempt from the tax regardless of the level of employer contribution and length of service.

Subsections (2) and (3) provide the cessation of employment exemption. Subsection (2) provides that the cessation of employment exemption detailed in subsection (3) applies if a member is employed for two years or more and, in the year of cessation and the two preceding years, employer contributions on behalf of the member have not increased by 50% or more. The employer contribution in the year of cessation must be annualised.

Subsection (3) exempts withdrawals that meet the subsection (2) criteria and are made on or after cessation of employment as well as shortly before cessation of employment. In this last case, the withdrawal must be in anticipation of the member ceasing employment.

Subsections (4) and (5) further define whether an employer's contributions have increased by 50% or more. Subsection (4) exempts increases in contribution levels if they occur before 1 April 2000 or in accordance with a requirement of a trust deed or a contract in existence before 1 April 2000. Subsection (5) exempts increases to the extent the additional contribution is to make up for underpaid contributions.

Subsection (6) provides that a non-exempt withdrawal on cessation of employment will be subject to withdrawal tax up to the maximum of the employer contributions from the start of the income year two years before the member ceases employment. In other words, the liable employer contributions to superannuation savings will equal the amount contributed by the employer over the last two full income years and the period up to the date of withdrawal.

Example

A member ceases employment with a company for which she has worked for the last four years and nine months. Before she stopped employment, her employer's contributions had increased by 100% in the final year. Under the superannuation fund's trust deed, the member can withdraw all the employer contributions. The amounts she withdraws are:

- Current year employer contributions: $9,000 (covering the nine months of the year up to the date of the cessation of employment)
- Year 4 $6,000
- Year 3 $6,000
- Years 1 and 2 $5,000

As the member did not cease employment on the grounds of injury, disablement or death, section CL 8(1) does not apply. Neither does section CL 8(3) because of the significant increase in contributions by her employer.

The withdrawal tax liability under section CL 8(6) is limited to $21,000, being the amount contributed by the employer in the year of withdrawal and the two immediately preceding years. The $10,000 representing the first two years of employer contribution is not included in the withdrawal tax liability calculation.

Starting the measurement period from the beginning of an income year reduces the compliance costs associated with undertaking this calculation, although it does extend the measurement period to a maximum of three years less one day.

Subsection (7) ensures that only amounts contributed by the employer with whom the member is ceasing employment, and any return on those contributions, are exempt. Therefore, withdrawals of contributions made by a previous employer are not exempt (unless of course they are exempt in their own right—perhaps because they are withdrawn after cessation of that earlier employment). Also, employer contributions to superannuation savings made by a second employer with whom the member is not ceasing employment, are not exempt and are fully liable, subject to the application of any other exemptions. Each withdrawal must be considered separately and its treatment worked out accordingly. Subsection (7) also ensures that the two-year "look back" rule in subsection (6) applies only in relation to contributions made by the employer with whom the member is ceasing employment.

Section CL 9: Contribution lock-in rule

Section CL 9(1) provides that if a member, who would be liable for withdrawal tax on cessation of employment, chooses to defer receipt of that withdrawal for two years, the withdrawal tax will not apply. This provision is on the basis that deferral of receipt for two years on cessation of employment addresses the concern that the withdrawal may be made as a substitute for salary.

This subsection does not specify the evidence required to verify deferral of the receipt of the withdrawal. In practice, this would involve sufficient records to show cessation of employment by a member, a request by that member for a withdrawal, and evidence that the withdrawal was not received by the member for two years after the request.

Subsection (2) provides that a withdrawal under subsection (1) that is deferred for two years or more after cessation of employment does not have to be locked away to be free of the withdrawal tax.

Section CL 10: Cessation of employment and defined benefit funds

The treatment of defined benefit funds varies from that of defined contribution funds in that the rules taxing withdrawals of amounts within two years of beginning employment, or when an employer increases contributions by 50 percent or more, do not apply. This means that all withdrawals from a defined benefit fund are exempt on cessation of employment. The basis for this variation is that, under a defined benefit fund, the employee's withdrawal entitlement is independent of the amount of employer contribution.

Eligible withdrawals may be made on or after cessation of employment as well as shortly before cessation of employment. In the latter case the withdrawal must be in anticipation of the member ceasing employment.

Section CL 11: Definition of cessation of employment

"Cessation of employment" is defined to exclude a member transferring from one employer to a related employer. Employers are related if they are separate employers but one is a branch or division of the other, or they are associated. The association test is that set out in section OD 7.

SECTION CL 12: EXCEPTION FOR WITHDRAWAL ON PARTIAL RETIREMENT

Section CL 12 provides that a member meeting certain criteria, defined as partial retirement, may make exempt withdrawals. Section CL 4 does not apply to a withdrawal at the time, or after a person partially retires if:

- The member is employed for 30 hours a week or less. This test is to ensure that the member is not in full employment.
- The member reduces work hours because he or she is nearing full retirement. This provision establishes that a reduction in work hours must have occurred and that the cause of that reduction is the approach of full retirement.
- The member notifies the trustee in writing that he or she does not intend to increase hours in paid employment in the future. This test is to ensure that the first two tests are not being met only for a short period of time, but will be met up until full retirement. However, this test is intention-based and does not prevent an increase in worked hours in the future.
- The member and his or her employer (or employers) cease contributing to any superannuation fund. This provision ensures that a member who is partially retiring is not both contributing to a superannuation fund and drawing down on that superannuation fund.

This exemption balances the need to recognise partial retirement with the objective of preventing the use of superannuation funds to avoid the 39% top marginal tax rate.

Although the test for no increase in hours is intention-based, that intention must have a reasonable basis. To ensure this, the member's written notice of partial retirement must include a signed statement by the employer that the employer's understanding is that paid employment for that member will not increase in the future.

Subsection (3) provides that the written notice of a member's intention need not be updated every time a member makes a withdrawal, provided the member's intention has not changed.

TRANSFERS OF FUNDS

Section CL 13: Transfers are withdrawals

Section CL 13 provides that an amount transferred directly from one superannuation fund to another superannuation fund or superannuation scheme is a withdrawal. The purpose of this provision is to ensure that the withdrawal tax applies in cases other than those exempted.

Section CL 14: Transfers from superannuation fund to superannuation fund

Section CL 14 provides for the treatment of amounts transferred from one superannuation fund to another.

Subsection (1) provides that an amount transferred from one superannuation fund to another (other than a defined benefit fund) retains its nature in the receiving fund if the transferee fund is informed of the nature of the funds.

This means that, for example, employer contributions that are transferred retain their nature as employer contributions in the receiving superannuation fund if detailed. Amounts contributed before 1 April 2000 continue to be treated as amounts contributed before that date.

Amounts subject to the two-year lock-in rule under section CL9 also retain their nature on transfer as long as appropriate information is provided.

Subsection (2), however, provides that if information as to the nature of an amount transferred is not provided to the receiving superannuation fund, the amount received is to be treated as employer contributions to superannuation savings. This means the amount would be liable for withdrawal tax if withdrawn, subject to the various exemptions, such as significant financial hardship.

Although, in most cases, it is expected that the information would be provided by the transferring superannuation fund, the section does allow information to be provided by an employer or past employer. This is mainly to cover cases where the transferring fund is unable or unwilling to provide information.

Subsections (3) and (4) provide for transfers to defined benefit funds. As the amount of employer contributions relating to a particular member is unknown, subsection (3) provides that the amounts on transfer that keep their nature are member contributions and amounts in the transferring superannuation fund as at 31 March 2000 (or earlier balance date if section CL 21 applies). Subsection (4) requires the transferring superannuation fund to provide the required information as to the nature of the transfer. This is on the basis that an employer or past employer would not be in a position to provide information as to the nature of the amounts transferred, since employer contributions are not attributable to individual members.

Subsection (4) provides that if the transferring superannuation fund does not notify the nature of the amounts transferred to a defined benefit fund, section CL 4 applies to a subsequent withdrawal of the amount transferred. For ease of understanding, this subsection makes clear that the exemptions may still apply to that withdrawal.

Section CL 15: Transfers from a superannuation scheme to a superannuation fund

Section CL 15 defines the nature of transfers from a superannuation scheme to a superannuation fund. It provides that the amount received by a superannuation fund from a superannuation scheme is treated as member contributions to the fund.

Contributions to superannuation schemes have been taxed appropriately, either through the fringe benefit tax rules, or through the member making contributions from post-tax income. Therefore, no withdrawal tax issues are raised by a withdrawal of these amounts from a superannuation scheme. Consistent with this, the transfer of these amounts to a superannuation fund, and subsequent withdrawal from that fund, does not raise a withdrawal tax issue.

Section CL 16: Superannuation funds investing in superannuation funds or schemes

This section provides the rules for superannuation funds that are members of a second superannuation fund or a superannuation scheme.

Subsection (1) provides that when a superannuation fund invests in another superannuation fund, the payment into, and withdrawal from, the second superannuation fund is not a transfer from the first fund. This means that the rules relating to transfers of amounts between superannuation funds and the associated information provision rules do not apply. The subsection also provides that the return of the investment to the first superannuation fund is not treated as a withdrawal from the second fund.

Subsection (2) provides that when a superannuation fund invests in a superannuation scheme, the investment into the superannuation scheme, and the withdrawal of that investment, are not a transfer and are not subject to the information provision rules. (The withdrawal from the scheme is not subject to withdrawal tax.)

The intention of the measure is that an investment by a superannuation fund in another fund or a scheme raises no withdrawal tax issues on entry or exit.

CHANGE IN NATURE OF SUPERANNUATION FUNDS AND SCHEMES

Section CL 17: Superannuation fund becomes superannuation scheme

Subsection (1) provides the withdrawal tax rules for when a superannuation fund becomes a scheme other than a foreign superannuation scheme. The objective is to ensure that amounts potentially liable for the withdrawal tax retain their nature when withdrawn. The subsection provides that amounts retain their nature and that the withdrawal tax provisions continue to apply.

Subsection (2) provides that the value of the amounts in the superannuation fund at the time it becomes a scheme are determined according to their market value.

Section CL 18: Superannuation fund becomes foreign superannuation scheme

The withdrawal tax model is one of creating gross income on which a superannuation fund pays income tax at a rate which equates to the withdrawal tax. However, if a superannuation fund becomes a foreign superannuation scheme, New Zealand income tax ceases to be payable, so the withdrawal tax ceases to apply. To address this, this section deems all amounts in the superannuation scheme to have been withdrawn immediately before the fund becomes a foreign superannuation scheme. This will give rise to withdrawal tax obligations, subject to the application of the exemptions.

Section CL 19: Superannuation scheme becomes superannuation fund

This section provides that amounts in a superannuation scheme that becomes a superannuation fund are member contributions. This equates to the treatment of individual members withdrawing from a superannuation scheme and transferring the withdrawal to a superannuation fund.

If a superannuation fund becomes a superannuation scheme and then reverts back to a superannuation fund, any amounts contributed during the superannuation scheme period are treated as member contributions. Amounts contributed before the fund becomes a scheme are covered by section CL 17. This section provides that:

- Amounts in the superannuation fund at the time it became a superannuation scheme retain their nature, and
- On withdrawal, they are treated as if they had continued to be in a superannuation fund.

Section CL 20: Treatment of winding-up of a fund

This section provides that when a superannuation fund is wound up, a distribution in respect of a person's membership is treated as a withdrawal and the rules on withdrawals apply. This provision also applies to a partial wind-up of a superannuation fund. If the member is ceasing employment at the same time the superannuation fund winds up, the withdrawal could be exempt under the cessation provisions, subject to the two-year rule and the level of employer contribution involved.

Amounts can be transferred on wind-up, under the transfer rules, to a second superannuation fund, resulting in no withdrawal tax liability on the amounts transferred.

MISCELLANEOUS MATTERS

CL 21: Balance date option

Section CL 21 provides the authority for a trustee to calculate the amount that exists in a fund other than on 31 March 2000. This section works in conjunction with section CL 3(1)(a) and CL 3(1)(b).

Section EN 6: Timing of gross income from withdrawal

Section EN 6(1) provides that gross income of a superannuation fund is derived in the income year following the withdrawal. This measure is intended to remove provisional tax and use-of-money interest issues raised if a disproportionate number of withdrawals were made late in an income year.

Subsection (2) provides that this rule does not apply to a withdrawal in the year a fund is wound up or a superannuation fund becomes a foreign superannuation scheme. Subsection (3) provides that in these cases the gross income is derived in the income year of the withdrawal.

The first exception to the deferral of the recognition of the gross income reflects the fact that a delayed income tax obligation would postpone the wind-up of the fund. In the second case, it is the concern that the superannuation fund is leaving the New Zealand tax base.

If a superannuation fund that has become a superannuation scheme winds up, the withdrawal tax is due in the year of wind-up. This is because section CL 17 deems that section EN 6 applies as if a withdrawal from a superannuation scheme were a withdrawal from a superannuation fund. Payments on wind-up are treated as withdrawals.

Section EN 7: Late balance date superannuation funds

This section provides that a superannuation fund with a late balance date that derives gross income from a withdrawal in the period 31 July 2000 to 30 September 2000 has that gross income treated as being derived in the 2001/2002 income year. This measure is intended to ensure that early payment is not required as a result of these entities having late balance dates.

A late balance date is one falling between 1 April and 30 September inclusive.

ELECTION OF 39% SSCWT RATE

Section NE 2AA: Election of 39% SSCWT rate

Section NE 2AA allows an employee, with the agreement of the employer, to elect that a 39% SSCWT rate apply to employer contributions made on the employee's behalf. The employer's agreement is required because deducting SSCWT at 39% may impose compliance costs on employers.

Subsection (2) requires the employer to apply the 39% SSCWT rate if the employee has made an election. The election continues to be valid until revoked in writing. This is specified by subsection (3).

An amendment is made to the First Schedule of the Income Tax Act 1994 to provide for both a 33% and a 39% SSCWT rate.

The application date for these provisions is 1 October 2000.

WITHHOLDING AND RECOVERY

Section NEA 1 Income Tax Act 1994 and section 165AA of the Tax Administration Act 1994

The purpose of these sections is to allow trustees to pass on any withdrawal tax liability they incur to the person making the withdrawal. If this measure were not adopted, all the members of a superannuation fund would bear costs imposed by the decision of one member.

Section NEA 1 provides that a trustee may withhold from a withdrawal an amount equal to the withdrawal tax imposed on that withdrawal.

Section 165AA provides for a recovery ability if a withdrawal is paid out with insufficient or no withdrawal tax deducted. This section also makes it clear that this recovery power may be applied irrespective of a superannuation fund's trust deed.

INFORMATION PROVISION SECTIONS

Three new sections have been added to the Tax Administration Act 1994 to provide authority for the information transfers necessary if the withdrawal tax rules are to work smoothly. They provide those who require information to make the withdrawal tax work effectively, with the ability to get that information.

Trustees of superannuation funds and employers need to be in a position to provide the information that may be requested. Failure to provide the information requested is an offence under the Tax Administration Act.

Although the Act places obligations on employers and trustees, they may in some cases be able to establish alternative systems to minimise compliance costs. For example, a trustee requesting information regularly from an employer so, if a withdrawal is made, the trustee can determine application of the withdrawal tax without approaching the employer for details. In that case, the trustee would already know the extent of employer superannuation contributions on behalf of an employee over the last four years so the under $60,000 income exemption could be applied correctly without requiring additional information from the employer.

Requests must be made in writing given that a time period for a response is set and penalties may apply. There is, however, no specification that any response must be in writing. This is a matter for the person making the request and the person receiving the request to resolve.

Sections 32A to 32C Tax Administration Act 1994

Section 32A requires an employer to provide a record of all specified superannuation contributions made by the employer on a member's behalf in the four years before a withdrawal by the member. A member may request this information directly or a trustee of a superannuation fund may make the request on the member's behalf.

Example

A member of a superannuation fund makes a withdrawal of employer contribution to his superannuation fund. This is allowed under the superannuation fund's trust deed.

The member had taxable income of $45,000 four years ago, $50,000 three and two years ago, and $55,000 for the last year. This was his only source of income. The income for the current year is not relevant for determining the application of the exemption.

On the basis of this information, under section 32A, the member requests the level of the employer superannuation contributions made on his behalf in the last four years.

The employer is required to provide those details for each year and to reply within 20 working days.

Note:

- The request could have been made by the trustee of the superannuation fund on the member's behalf.
- The superannuation fund may hold the details requested by the member in any case so no request would need to have been made to the employer.
- If the employer's rate of contribution was 10% of salary, the exemption will be met for the first three years, with only specific information being needed for the fourth year to determine whether the exemption applies for that year.

Section 32B provides a trustee of a superannuation fund with the authority to request information from a member or a member's employers (both past and present). This information is required by a superannuation fund to determine the extent to which the various exemptions apply.

The information covered by either of these sections may be requested at the time a member makes a withdrawal or by a trustee of a superannuation fund in anticipation of a possible withdrawal. The latter approach reduces the risk that a request may be made for information covering a number of, possibly distant, income years. The flexibility around the request process is intended to allow superannuation funds and employers to determine processes that work effectively for them.

Section 32C allows a trustee receiving a transfer of funds from a second superannuation fund to request from the trustee of that fund that information necessary to determine the nature of the money transferred.

In the case of all these sections:

- Requests must be made in writing.
- A trustee is entitled to rely on the information provided as being correct unless the trustee has reasonable grounds to believe it is not correct.
- The information provided is treated as correct if reasonably relied on by the trustee. If the information provided is not correct, the criminal penalty sections of the Tax Administration Act 1994 may be applied to the person providing that incorrect information.

In the case of sections 32A and 32B, the person receiving the request for information must reply within 20 days, while in section 32C a 40-day response period is allowed. The extension recognises that a trustee receiving an information request may in turn have to request information from a third party.

AMENDMENT TO SECURITIES ACT 1978

A new section 7A was inserted into the Securities Act 1978. This section provides that an advertisement, registered prospectus or investment statement does not trigger any penalty or response under the Securities Act if:

- the advertisement, prospectus or investment statement was printed before 14 September 2000, and
- the member making an investment is informed in writing of the withdrawal tax before making that investment.

The purpose of the provision is to reduce compliance costs on trustees, who would otherwise have to reprint their documents at considerable cost. The goal of ensuring informed decision-making is considered to be met by the requirement that the member sees, in writing, information relating to the withdrawal tax.

MULTI-RATE FRINGE BENEFIT TAX RULES

Sections CF 2(11)(b)(ii), CI 1, CI 2A(4), CI 3, CI 4, CI 5, CI 7, CI 8, CI 11, ND 1 – 16, OB 1 and Schedule 2 of the Income Tax Act 1994; sections 3(4)(b) and 120C(1) of the Tax Administration Act 1994; and section 21(4) of the Goods and Services Tax Act 1985

Introduction

The fringe benefit tax (FBT) rules in Part ND of the Income Tax Act 1994 have been amended to implement the new multi-rate FBT. Under these rules employers can either pay FBT at the flat rate of 64% on the taxable value of all the fringe benefits provided, or elect the new multi-rate FBT.

Under the multi-rate system, benefits that are attributed to an individual employee are subject to FBT at a rate that takes into account cash remuneration such as salary or wages received from the employer as well as the taxable value of those attributed fringe benefits. Fringe benefits that are not attributed to an individual employee are taxed at a flat rate of 49% (or 64% if a major shareholder-employee is one of the recipients of the non-attributed benefit).

The amendments create optional rules for all employers and relate only to calculating the FBT payable on benefits provided or granted. They do not change other aspects of the FBT rules, such as valuation provisions or what constitutes a fringe benefit.

Background

The FBT rate increased to 64% from 1 April 2000, to prevent high-income employees substituting fringe benefits for monetary remuneration to avoid the increase in the top personal tax rate to 39%, also from 1 April 2000. Since their introduction in 1985, the FBT rules have overtaxed low-income employees. The Government announced late last year, when the FBT rate was increased to 64%, that it would look at ways to reduce the over-taxation of low and middle-income employees receiving fringe benefits. Without these amendments, the 64% rate would have further exacerbated the over-taxation of low-income employees and would have overtaxed middle-income employees subject to a 33% personal tax rate.

Key features

A new Part ND, which deals with the calculation and payment of FBT and filing of returns, has been inserted into the Income Tax Act 1994 to implement the new multi-rate FBT rules. The new multi-rate FBT system requires employers to attribute certain benefits to the individual employee to whom the fringe benefit is provided or granted. The FBT tax payable on these attributed benefits is calculated on the basis of the cash remuneration, such as salary or wages, paid during the year by that employer and the annual taxable value of those attributed benefits. Non-attributed benefits are pooled and taxed a flat rate of 49% or 64%, depending on whether a major shareholder-employee is a recipient of the non-attributed benefit. This is an annual calculation undertaken as part of calculating the FBT payable for the fourth quarter. FBT payable in the first three quarters of the year is calculated in the same way as in previous years.

Application date

The amendments apply to fringe benefits provided or granted on or after 1 April 2000. For employers who pay FBT on fringe benefits provided to shareholder-employees on an income year basis, the amendments apply to benefits provided or granted during the 2000–2001 income year.

Detailed analysis

FBT rate options

Employers have the option of paying FBT on the value of fringe benefits provided or granted to all employees at a flat rate of 64% or using the multi-rate rules. New sections ND 1 and ND 2 set out the options available to employers in calculating and paying FBT. An employer who pays FBT on a quarterly basis must elect:

- to pay FBT at either the 64% or the 49% rate for the first three quarters of an income year on the taxable value of the fringe benefits provided or granted during the respective quarters, and calculate and pay FBT for the final quarter using the multi-rate FBT calculation (new sections ND 5 and 6), or
- to pay FBT at the 64% rate for the first three quarters of an income year on the taxable value of the fringe benefits provided or granted during the respective quarters, and either pay FBT for the final quarter using the multi-rate FBT calculation, or pay FBT for that quarter at the rate of 64% on the taxable value of the benefits provided in that final quarter.

An employer who pays FBT on an annual or an income year basis must either use the multi-rate FBT calculation for the fringe benefits provided or granted during that year or pay FBT at the 64% rate on the taxable value of the all fringe benefits provided or granted during that year.

Table 2 – Options for paying FBT

<table>
<tr><th>Return period</th><th colspan="2">Rate to use (quarters 1 to 3 apply only to quarterly filers)</th></tr>
<tr><td>Quarter 1</td><td colspan="2">49% or 64%</td></tr>
<tr><td>Quarter 2</td><td colspan="2">49% or 64%</td></tr>
<tr><td>Quarter 3</td><td colspan="2">49% or 64%</td></tr>
<tr><td>Quarter 4</td><td>If 49% was used in any of the first three quarters, the employer must use the multi-rate calculation.</td><td>If 64% was used in every quarter, the employer may use the multi-rate calculation or use the 64% rate for the benefits provided or granted during that quarter.</td></tr>
<tr><td>Annual or income year</td><td colspan="2">The employer must either use the multi-rate calculation or use the 64% rate year for all benefits provided during the year.</td></tr>
</table>

An employer makes an election to pay FBT by filing an FBT return and paying the FBT at the rate elected. The FBT return will be designed so that the employer can indicate the rate elected on the form. If no rate is indicated on the FBT return, the election will be based on the rate used to calculate the FBT payable for that quarter. Once an election is made it is irrevocable.

As the legislation to enact the new multi-rate FBT rules was not enacted until late September, all employers who file quarterly FBT returns are required to pay FBT at the 64% rate for the first two quarters of the 2000–2001 year, being the quarters beginning on 1 April 2000 and 1 July 2000 respectively. If an employer elects to use the multi-rate calculation, a credit for this tax will be taken into account as part of that calculation and any overpayment refunded.

Attributed benefits

If an employer is required to calculate FBT using the new multi-rate FBT rules, the new section ND 3 provides the rules for what benefits must be attributed to the employee to whom the benefit was provided or granted. The following categories of benefits must be attributed:

- the private use or enjoyment of a motor vehicle or the availability of the private use or enjoyment of a motor vehicle (section CI 1(a) and (b) benefits)
- a low-interest loan (section CI 1(c) benefits), except a low-interest loan provided by a life insurer to a policy holder or an associate, which is treated as a non-attributed benefit
- any subsidised transport (section CI 1(d) benefits) with annual taxable value of $1,000 or more except if the employer elects to treat the benefit as a non-attributed benefit under the provisions in the new section ND 4 (explained later)
- any contribution to a sick, accident, or death fund approved by the Commissioner for the purposes of section CB 5 (section CI 1(e) benefits) if the annual taxable value of contributions is $1,000 or more
- any specified insurance premium (premiums paid for a policy of life insurance, a policy of pension insurance or a policy of personal accident or sickness insurance), or a contribution to an insurance fund of a friendly society (section CI 1(f) benefits) if the annual taxable value of premiums and contributions is $1,000 or more
- any contributions to a superannuation scheme (section CI 1(g) benefits) if the annual taxable value of contributions is $1,000 or more, and
- any benefit of any other kind granted or provided by an employer (section CI 1(h) benefits) if the combined annual taxable value of all such benefits is $2,000 or more.

If a fringe benefit is provided or granted to more than one employee, the employer must attribute that benefit to the employee who had the principal use, enjoyment or availability of that benefit, or who principally received that benefit during the quarter. In the case of an employer who files FBT returns on an income year basis, the period is the income year rather than the quarter. This rule ensures that fringe benefits are only attributed to one employee. If no employee has the principal use, enjoyment or availability, the benefit is treated as a non-attributed benefit. For example, four employees had the private use of a motor car during the period. Employees A and B each had the car for 27 days and employees C and D each had the car for 16 days. As no one employee had the principal use of the fringe benefit, it is treated as a non-attributed benefit.

If employee A had the car for 30 days and employee B for 26 days, the fringe benefit would be attributed to employee A as he or she had the principal use.

Employers can choose to attribute benefits with an annual taxable value below the monetary thresholds if they wish. However, if any benefits below the monetary threshold are attributed, all benefits in that category must be attributed. In other words, an employer cannot decide to attribute an insurance premium with an annual taxable value of $500 only to low-income employees and not to all other employees.

New section ND 4 allows employers to treat subsidised transport benefits with an annual taxable value of $1,000 or more as non-attributed benefits if all their employees have the same or similar entitlement to such benefits. This rule does not apply if the employer is a close company (controlled by five or fewer natural persons).

New section ND 16 allows these monetary thresholds to be amended by Order in Council.

Non-attributed benefits (pooled benefits)

The new section ND 6 sets out the rules for the calculation of FBT payable on non-attributed benefits. The following benefits are treated as non-attributed benefits:

- fringe benefits that have a taxable value of less than $1,000 per category per year, being benefits to which paragraphs (d) to (g) of section CI 1 apply, and have not been attributed to an individual employee
- fringe benefits that have a taxable value of less than $2,000 per year, being benefits to which paragraph (h) of section CI 1 applies (benefits of any other kind) and have not been attributed to an individual employee
- subsidised transport benefits to which section ND 4 applies
- fringe benefits that cannot be attributed to an individual employee
- fringe benefits that are provided or granted to a former employee, and
- low-interest loans provided by life insurers to a policyholder or an associate (loans to which either section CI 2(8) or CI 2(9) applies).

An employer is required to create two pools and allocate the non-attributed benefits to each pool according to whether or not a recipient of the benefit is a major shareholder-employee or an associate of a major shareholder-employee. For the purposes of the Income Tax Act 1994, a major shareholder-employee is a person who owns or has in any way the power to control (whether directly or indirectly) or has the right to acquire, 10% or more of the ordinary shares, voting rights or control of a close company and is also an employee of that company. This means that the requirement to maintain two pools for non-attributed benefits applies only if the employer is a close company (controlled by five or fewer natural persons).

If a major shareholder-employee or an associate of the major shareholder-employee is a recipient of the non-attributed benefit, the annual taxable value of the whole benefit is allocated to one pool and taxed at a flat rate of 64%. This rule does not apply to an associate of the major shareholder-employee if that person receives the fringe benefit as an employee of the employer. If the non-attributed benefits are received by employees, other major shareholder-employees or associates, such benefits are allocated to the second pool and taxed at a flat rate of 49%.

Cash remuneration

The new section ND 7 sets out the rules for determining an employee's cash remuneration for the purposes of the multi-rate calculation. The cash remuneration of an employee other than a major shareholder-employee is the amount of remuneration for the year in which the fringe benefit is provided or granted, that is paid to, credited to or applied on account of the employee by the employer who provided or granted the fringe benefit, or a related employer. Cash remuneration does not include the taxable value of fringe benefits provided or granted by the employer or a related employer. The value of employer superannuation contributions subject to specified superannuation contribution withholding tax is not included in the calculation of an employee's cash remuneration as it is excluded from the definition of salary or wages.

"Remuneration" is defined to include the following:

- salary or wages as defined in section OB 1 of the Income Tax Act 1994
- salary, wages or gross income to which section OB 2(2) applies (such as salary or wages paid to a shareholder-employee that is not subject to PAYE)
- extra emoluments such as bonuses
- withholding payments, and
- payments to a specified office holder (a judicial officer whose salary and principal allowances are determined by the Higher Salaries Commission or a Member of Parliament).

An employer (employer A) is related to another employer (employer B) for the purposes of the FBT rules if employer B is treated as a separate employer from employer A and is a branch or division of employer A or a person associated with employer A.

For a major shareholder-employee the amount of cash remuneration also includes the amount of interest or dividends received from the employer who provided or granted the fringe benefit, or a related employer.

If the employee works only part of the income year, the employer is not required to annualise the cash remuneration received by the employee.

Multi-rate calculation for attributed benefits

The new section ND 5 provides for the multi-rate calculation of the FBT payable on attributed benefits to individual employees. The calculation for an employee who is not a major shareholder-employee is as follows:

Step 1: For each employee who receives attributed benefits, the employer must calculate that employee's fringe benefit-inclusive cash remuneration using the following formula: cash remuneration minus the tax on that cash remuneration plus the taxable value of fringe benefits.

- The cash remuneration is the amount determined in accordance with section ND 7 (see explanation on page 26 on cash remuneration).
- The amount of tax on the cash remuneration is the tax calculated by using the statutory tax rates set out in Schedule 1, Part B of the Income Tax Act 1994 as if the cash remuneration was the only taxable income received by the employee, and taking into account the low-income rebate. It is not the amount of PAYE deducted by the employer on that remuneration. This amount is subtracted from the cash remuneration to determine the net-of-tax cash remuneration. Table 3 sets out the current personal tax rates to be used.
- The taxable value of all fringe benefits attributed to that employee in the year is added to the net-of-tax cash remuneration.

Table 3 – Tax rates to be used to calculate tax on cash remuneration

Cash remuneration (such as salary, wages and extra emoluments) paid to employee	Rate: cents/$
$9,500 or less	15
More than $9,500 and less than or equal to $38,000	21
More than $38,000 and less than or equal to $60,000	33
More than $60,000	39

Step 2: The employer then must calculate the tax on each employee's fringe benefit-inclusive cash remuneration (step 1) using the rates specified in Schedule 2, Part B of the Income Tax Act 1994. Table 4 sets out the tax rates to be used.

Table 4 – Rates for attributed benefits

Fringe benefit-inclusive cash remuneration	Rate: cents/$
$8,075 or less	17.65
More than $8,075 and less than or equal to $30,590	26.58
More than $30,590 and less than or equal to $45,330	49.25
More than $45,330	63.93

Step 3: The FBT liability for each employee on the value of attributed benefits is calculated by deducting from the amount of tax calculated in **step 2**, the amount of tax calculated on the cash remuneration in **step 1**. The resulting amount is the FBT payable on the attributed fringe benefits to that employee for the year.

For a major shareholder-employee, the taxable value of attributed benefits to be included in step 1 of the calculation of the employee's fringe benefit-inclusive cash remuneration includes, in addition to attributed fringe benefits received by the major shareholder-employee, the value of attributed benefits received by an associate of that employee. This only applies if the fringe benefits received by the associated person are not received by virtue of that person being an employee of the employer.

Filing and payment requirements

Quarterly filers

The new sections ND 9, 10 and 11 apply to employers who pay FBT on a quarterly basis. The new section ND 11 deals with the return filing requirement of employers who have not provided or granted a fringe benefit during a quarter, and reinstates the legislation contained in replaced section ND 2(3) and (4), which required a nil return to be filed and allowed the Commissioner to waive this return filing requirement. The only change to these provisions is that final quarter returns are now due on 31 May following the end of the quarter, rather than 20 April.

Section ND 9 requires an employer who is required to pay FBT for each of the first three quarters of a year to file an FBT return and pay the tax calculated by the 20th of the month following the end of the quarter.

If an employer has elected to use the multi-rate calculation in accordance with new sections ND 5 and ND 6, the employer's FBT liability for the final quarter of the year is:

- the sum of all amounts calculated in step 3, under the heading "Multi-rate calculation for attributed benefits", plus
- the amount of FBT payable on the non-attributed benefits (pooled benefits), less
- the amount of FBT assessed in the previous three quarters of the year.

If the amount calculated is a negative amount, the employer is entitled to a refund. If the amount calculated is a positive amount, it is due for payment by 31 May following the end of the quarter. The FBT return for the final quarter is also due by 31 May.

An employer who has elected to pay FBT at the flat rate of 64% for the first three quarters of the year may pay FBT at 64% on the benefits granted or provided during the final period. The return and payment is due by 31 May following the end of that quarter.

Annual filers

The new section ND 13 deals with employers who file FBT returns on an annual basis for employees who are not shareholder-employees. This section reinstates the provisions in the old section ND 3, which has been replaced. If such an employer elects to use the multi-rate calculation, the employer is required to undertake the calculation of the FBT payable on the value of attributed benefits provided to each employee during the year and the FBT payable on the non-attributed benefits (pooled benefits). The amount payable is the total of all amounts calculated in **step 3**, under the heading of "Multi-rate calculation for attributed benefits" plus the amount of FBT calculated on the non-attributed benefits (pooled benefits). This amount and the FBT return is due by 31 May (two months after the end of the year).

Alternatively, such employers can choose to pay FBT at the flat rate of 64% on the taxable value of all fringe benefits provided or granted during the year. The FBT payable and the return are due by 31 May (two months after the end of the year).

Income year filers

The new section ND 14 deals with employers who file FBT returns on an income year basis for employees who are shareholder-employees. This section reinstates the provisions in old section ND 4, which has been replaced. If such an employer elects to use the multi-rate calculation, the employer is required to undertake the calculation of the FBT payable on the value of attributed benefits provided to each shareholder-employee during the year and the FBT payable on the non-attributed benefits (pooled benefits). The amount payable is the total of all amounts calculated in **step 3**, under the heading "Multi-rate calculation for attributed benefits", plus the amount of FBT calculated on the non-attributed benefits (pooled benefits). This amount and the FBT return are due by the terminal tax date of the employer.

Alternatively, such employers can choose to pay FBT at the flat rate of 64% on the taxable value of all fringe benefits provided or granted to shareholder-employees during the year. The FBT payable and the return are due by the terminal tax date of the employer.

Table 5 sets out the options available to employers for FBT and the return and payment obligations.

Table 5 – Options for FBT payment and return filing

Return period and return	Rate to use (quarters 1 to 3 apply only to quarterly filers)		Due date for payment
Quarter 1	49% or 64%		20 July
Quarter 2	49% or 64%		20 October
Quarter 3	49% or 64%		20 January
Quarter 4	If 49% was used in **any** of the first three quarters, the employer **must** use the multi-rate calculation.	If 64% was used in **every** quarter, the employer **may** use the multi-rate calculation or use the 64% rate for the benefits provided or granted during that quarter.	31 May
Annual basis	The employer must either use the multi-rate calculation or use the 64% rate for all benefits provided during the year		31 May
Income year basis	The employer must either use the multi-rate calculation or use the 64% rate for all benefits provided during the year		Terminal tax date of employer

Employer ceasing employment

The new sections ND 8 and ND 12 deal with an employer who stops employing staff during the year. The rules require an employer who stops employing staff and does not intend to replace them during the year (1 April to 31 March), to use the multi-rate calculation in the quarter in which the employer stopped employing staff as if that quarter were the final quarter for the year. The FBT return and any tax payable are due two months after the end of that quarter.

This provision does not apply if the employer continues to provide or grant fringe benefits to a former employee. Also, it only applies to employers who file on a quarterly basis.

Transitional provisions for the 2000–2001 year

Transitional rules apply for benefits provided or granted in the 2000–2001 year, as the legislation was not enacted until 25 September 2000. All employers are required to use the 64% rate for the returns due for the first and second quarters (1 April 2000 to 30 June 2000 and 1 July 2000 to 30 September 2000 respectively). Therefore the first opportunity in this year to choose between the 49% and 64% rates is the third quarter (1 October 2000 to 31 December 2000).

Section ND 10(6) and (7) allows an employer who has elected to pay FBT at the 49% rate for the third quarter (1 October 2000 to 31 December 2000) and is therefore required to use the multi-rate calculation for the final quarter, to pay FBT at the flat rate of 64% on all benefits provided during that year. This provision applies if the employer does not have the necessary records and system to use the multi-rate calculation.

Use-of-money interest

Section 120C(1) of the Tax Administration Act 1994 has been amended to provide a specific "date interest start" definition for any overpayment of FBT resulting from the multi-rate calculation. Use-of-money interest on any such overpayment starts from the later of 31 May next following the end of the final quarter and the date on which the return for the final quarter is filed. For example, if an employer was entitled to a refund of overpaid FBT for the final quarter and that return was filed on 20 June, interest would start running from that date rather than 31 May, when the return was due.

If an employer ceases to employ during the year and new sections ND 8 and ND 12 apply, this provision applies as if 31 May were two months immediately following the end of the quarter in which the employer stops employing staff.

Consequential amendments

A number of consequential amendments have been made to provisions in the Income Tax Act 1994, the Tax Administration Act 1994 and the Goods and Services Tax Act 1985 as a result of provisions in Part ND being renumbered as part of the enactment of the multi-rate FBT rules.

The new section ND 15 of the Income Tax Act 1994 reinstates the provisions in the replaced section ND 5.

Detailed example of how the multi-rate FBT rules will apply

JM Ltd is a close company owned and controlled by the CEO and spouse. The CEO is a major shareholder of the company as he or she owns 50% of the shares of the company. The following schedule shows the fringe benefits provided to the employees of the company on a quarterly basis. The same benefits are provided each quarter.

Fringe benefits received by employees (quarterly filing employer)

	Cash remuneration for year $	**Taxable value ($) of fringe benefits received per quarter**			
		Motor vehicles	Foreign superannuation scheme[1]	Medical insurance[2]	Discounted goods[3]
CEO	$80,000 (includes dividends received of $5,000 from JM Ltd)	$1,800*	$750	$200	$100
Employee 1	$50,000	$1,800*	$750	$200	$100
Employee 2	$40,000			$200	$100
Employee 3	$37,500			$200	$100
Total benefit		$3,600	$1,500	$800	$400
				Total value of all benefits	$6,300

* based on a $30,000 vehicle used every day in the quarter (90 days).

1 The contributions to a foreign superannuation scheme are covered by paragraph (g) of section CI 1 and therefore is a category of benefits.

2 The medical insurance premiums are covered by paragraph (f) of section CI 1 and therefore is a category of benefits.

3 The discounted goods are covered by paragraph (h) of section CI 1 and therefore are a category of fringe benefits.

FBT obligations for the first three quarters of the year

JM Ltd would aggregate the taxable value of all fringe benefits provided in a quarter and then apply either the 49% or 64% flat rate to this quarter. The company elects the 49% rate.

The FBT liability for quarters 1 to 3 is as follows:

Quarter	**Taxable value of benefits**	**FBT rate**	**FBT payable**	**Due date for return and payment**
Quarter 1	$6,300	49%	$3,087	20 July
Quarter 2	$6,300	49%	$3,087	20 October
Quarter 3	$6,300	49%	$3,087	20 January
Total			$9,261	

The example ignores the transitional requirement to pay 64% in the first two quarters of the 2000–2001 year.

As JM Ltd has chosen to pay FBT at the 49% rate in any of the first three quarters of the year, it must undertake the multi-rate calculation for the final quarter of the year.

Multi-rate calculation for the final quarter of the year

Attributed benefits

In undertaking this calculation JM Ltd needs to determine which benefits must be attributed to the individual employee receiving them and which may be attributed. Under the new rules, the following benefits must be attributed:

- the private use or enjoyment of a motor vehicle or the availability of the private use or enjoyment of a motor vehicle (section CI 1(a) and (b) benefits)
- a low-interest loan (section CI 1(c) benefits), except a low-interest loan provided by a life insurer to a policy-holder or an associate which is treated as a non-attributed benefit
- any subsidised transport (section CI 1(d) benefits) with annual taxable value of $1,000 or more except if the employer elects to treat the benefit as a non-attributed benefits under the provisions in the new section ND 4 (explained later)
- any contribution to a sick, accident, or death fund approved by the Commissioner for the purposes of section CB 5 (section CI 1(e) benefits) if the annual taxable value of contributions is $1,000 or more
- any specified insurance premium (premiums paid for a policy of life insurance, a policy of pension insurance or a policy of personal accident or sickness insurance) or a contribution to an insurance fund of a friendly society (section CI 1(f) benefits) if the annual taxable value of premiums and contributions is $1,000 or more
- any contributions to a superannuation scheme (section CI 1(g) benefits) if the annual taxable value of contributions is $1,000 or more, and
- any benefit of any other kind granted or provided by an employer (section CI 1(h) benefits) if the combined annual taxable value of all such benefits is $2,000 or more.

JM Ltd must attributed the following benefits to the employee who received the benefit:

- The CEO's motor vehicle. The annual taxable value of this benefit is $7,200.
- The CEO's superannuation scheme contributions, as the annual taxable value of this benefit category is more than $1,000. The annual taxable value is $3,000.
- Employee 1's motor vehicle. The annual taxable value of this benefit is $7,200.
- Employee 1's superannuation contributions, as the annual taxable value of this benefit category are more than $1,000. The annual taxable value is $3000.

Non-attributed benefits (pooled benefits)

JM Ltd may attribute the medical insurance premiums (annual taxable value of $800) and benefits of any other kind (the discounted goods—annual taxable value of $400). If JM Ltd decides to attribute either of these categories of benefits, it must attribute them to all employees who received them. In deciding whether to attribute these benefits, JM Ltd would need to assess the tax cost or savings of attributing and the compliance costs associated. If JM Ltd decides not to attribute these benefits it must either allocate these non-attributed benefits to one of two pools according to whether the recipient of the benefit is a major shareholder-employee or an associate.

The non-attributed benefits are allocated to the respective pools as follows:

Pool 1 (major shareholder-employee a recipient of the benefit—medical insurance and discounted goods provided to the major shareholder-employee)—annual taxable value $1,200

Pool 2 (major shareholder-employer not a recipient of the benefits—medical insurance, cards and flowers and discounted goods provided to all other employees)—annual taxable value $3,600.

If JM Ltd decided to attribute these benefits, it could decide only to attribute the medical insurance benefits, the benefits of other kind category or both. If it decided to attribute all these benefits, the annual taxable value of attributed fringe benefits would be:

	Annual taxable value ($) of attributed fringe benefits received per category				
Employee	**Motor vehicles**	**Superannuation**	**Medical insurance**	**Benefits of other kind**	**Total**
CEO	$7,200	$3,000	$800	$400	$11,400
Employee 1	$7,200	$3,000	$800	$400	$11,400
Employee 2			$800	$400	$1,200
Employee 3			$800	$400	$1,200

Calculation of FBT liability for the final quarter

Example 1

In this example of the calculation, JM Ltd attributes only the benefits that must be attributed to the employees who received them, and the other benefits are treated as non-attributed benefits and pooled.

Step 1: Calculate the fringe benefit-inclusive remuneration for each employee who received attributed benefits. The calculation is the cash remuneration minus the tax on the cash remuneration plus the annual value of fringe benefits attributed.

Employee	Cash remuneration	**Less** tax on the cash remuneration	**Plus** annual value of fringe benefits attributed	**Equals** fringe benefit inclusive remuneration
CEO	$80,000	$22,470[1]	$10,200	$67,730
Employee 1	$50,000	$11,370[2]	$10,200	$48,830

Step 2: Calculate the tax on the fringe benefit-inclusive remuneration from step 1 for each employee. Schedule 2, Part B is the tax rates used for this calculation.

Employee	Tax on fringe benefit-inclusive remuneration
CEO	$28,989.48[3]
Employee 1	$16,906.71[4]

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[1] Tax on cash remuneration for CEO is as follows: ($38,000 * 19.5%) + (($60,000 - $38,000) * 33%) + (($80,000 - $60,000) * 39%) = $22,470

[2] Tax on cash remuneration for employee 1 is as follows: ($38,000 * 19.5%) + (($50,000 - $38,000 * 33%) = $11,370

[3] Tax on fringe benefit-inclusive remuneration for CEO is as follows: ($8,075 * 17.65%) + (($30,590 - $8,075) * 26.58%) + (($45,330 -$30,590) * 49.25%) + (($67,730 - $45,330) * 63.93%) = $28,989.48

[4] Tax on fringe benefit-inclusive remuneration for employee 1 is as follows: ($8,075 * 17.65%) + (($30,590 - $8,075) * 26.58%) + (($45,330 -$30,590) * 49.25%) + (($48,830 - $45,330) * 63.93%) = $16,906.71

Step 3: Calculate the FBT liability of the taxable value of attributed benefits. This calculation is the tax on the fringe benefit-inclusive remuneration (step 2) **less** the tax calculated on the cash remuneration in step 1.

Employee	Tax on fringe benefit inclusive remuneration	**Less** tax on the cash remuneration	**Equals** FBT liability on attributed benefits
CEO	$28,989.48	$22,470	$6,519.48
Employee 1	$16,906.71	$11,370	$5,536.71
Total			$12,056.19

Step 4: Calculate the FBT on the non-attributed benefits. This amount is calculated by applying the 49% flat rate or the 64% flat rate to the respective pools depending on whether the recipient of the benefit is a major shareholder-employee or an associate.

Pool	**Value of non-attributed benefits**	**FBT rate**	**FBT liability**
Pool 1 (major shareholder-employee a recipient)	$1,200	64%	$768
Pool 2 (major shareholder-employee not a recipient)	$3,600	49%	$1,764
Total			$2,532

Step 5: Calculate the final FBT liability for the final quarter. This amount is the total of FBT liability calculated in step 3 (FBT on attributed benefits) **plus** the FBT liability calculated in step 4 (FBT on non-attributed benefits) **less** the FBT assessed in the first three quarters of the year.

FBT liability calculated in step 3 (FBT on attributed benefits)	**Plus** the FBT liability calculated in step 4 (FBT on non-attributed benefits)	**Less** the FBT assessed in the first three quarters of the year	FBT liability for the final quarter
$12,056.19	$2,532	$9,261	$5,327.19

JM Ltd's FBT liability for the final quarter is $5,327.19. The tax and the return are due 31 May following the end of the quarter.

Calculation of FBT liability for the final quarter

Example 2

In this example of the calculation, JM Ltd attributes all the fringe benefits provided to each employee.

Step 1: Calculate the fringe benefit-inclusive remuneration for each employee that received attributed benefits. The calculation is the cash remuneration minus the tax on the cash remuneration plus the annual value of fringe benefits attributed.

Employee	Cash remuneration	**Less** tax on the cash remuneration	**Plus** annual value of fringe benefits attributed	**Equals** fringe benefit inclusive remuneration
CEO	$80,000	$22,470[5]	$11,400	$68,930
Employee 1	$50,000	$11,370[6]	$11,400	$50,030
Employee 2	$40,000	$8,070[7]	$1,200	$33,130
Employee 3	$37,500	$7,305[8]	$1,200	$31,395

Step 2: Calculate the tax on the fringe benefit-inclusive remuneration from step 1 for each employee. The tax rates used for this calculation are in Schedule 2, Part B.

Employee	Tax on fringe benefit-inclusive remuneration
CEO	$29,756.64[9]
Employee 1	$17,673.87[10]
Employee 2	$8,660.66[11]
Employee 3	$7,806.17[12]

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[5] Tax on cash remuneration for CEO: is as follows: ($38,000 * 19.5%) + (($60,000 - $38,000) * 33%) + (($80,000 - $60,000) * 39%) = $22,470

[6] Tax on cash remuneration for employee 1 is as follows: ($38,000 * 19.5%) + (($50,000 - $38,000 * 33%) = $11,370

[7] Tax on cash remuneration for employee 2 is as follows: ($38,000 * 19.5%) + (($40,000 - $38,000 * 33%) = $8,070

[8] Tax on cash remuneration for employee 3 is as follows: ($9,500 * 15%) + (($37,500 - $9,500 * 21%) = $7,305

[9] Tax on fringe benefit-inclusive remuneration for CEO is as follows: ($8,075 * 17.65%) + (($30,590 - $8,075) * 26.58%) + (($45,330 -$30,590) * 49.25%) + (($68,930 - $45,330) * 63.93%) = $29,756.64

[10] Tax on fringe benefit-inclusive remuneration for employee 1 is as follows: ($8,075 * 17.65%) + (($30,590 - $8,075) * 26.58%) + (($45,330 -$30,590) * 49.25%) + (($50,030 - $45,330) * 63.93%) = $17,673.87

[11] Tax on fringe benefit-inclusive remuneration for employee 2 is as follows: ($8,075 * 17.65%) + (($30,590 - $8,075) * 26.58%) + (($33,130 - $30,590) * 49.25%) = $8,660.66

[12] Tax on fringe benefit-inclusive remuneration for employee 3 is as follows: ($8,075 * 17.65%) + (($30,590 - $8,075) * 26.58%) + (($31,395 - $30,590) * 49.25%) = $7,806.17

Step 3: Calculate the FBT liability of the taxable value of attributed benefits. This calculation is the tax on the fringe benefit-inclusive remuneration (step 2) **less** the tax calculated on the cash remuneration in step 1.

Employee	Tax on fringe benefit inclusive remuneration	**Less** tax on the cash remuneration	**Equals** FBT liability on attributed benefits
CEO	$29,756.64	$22,470	$7,286.64
Employee 1	$17,673.87	$11,370	$6,303.87
Employee 2	$8,660.66	$8,070	$590.66
Employee 3	$7,806.17	$7,305	$501.17
Total			$14,682.34

Step 4: Calculate the FBT on the non-attributed benefits. No calculation is required as all fringe benefits have been attributed to the employees who received them.

Step 5: Calculate the final FBT liability for the final quarter. This amount is the total of FBT liability calculated in step 3 (FBT on attributed benefits) **plus** the FBT liability calculated in step 4 (FBT on non-attributed benefits) **less** the FBT assessed in the first three quarters of the year.

FBT liability calculated in step 3 (FBT on attributed benefits)	**Plus** the FBT liability calculated in step 4 (FBT on non-attributed benefits)	**Less** the FBT assessed in the first three quarters	FBT liability for the final quarter of the year
$14,682.34	nil	$9,261	$5,421.34

JM Ltd's FBT liability for the final quarter is $5,421.34. The tax and the return are due 31 May following the end of the quarter. By attributing all the fringe benefits, JM Ltd has an additional FBT cost of $94.15.

FBT – REMOVAL OF INTEREST ON ANNUAL AND YEARLY PAYMENTS

Section 120S of the Tax Administration Act 1994

Introduction

Use-of-money interest will no longer be charged on fringe benefit tax (FBT) paid either on an annual basis or an income year basis.

Background

The discussion document *Less Taxing Tax,* released in September last year, considered a number of tax simplification proposals aimed at small businesses. Removing the interest on FBT that is paid yearly is the first of those proposals to be enacted.

FBT is generally paid on a quarterly basis. However, some taxpayers have the option to pay it once a year, either on an annual basis or on an income year basis. Use-of-money interest is applied to yearly payments to compensate the Government for the tax deferral.

This application of use-of-money interest is a disincentive to choosing to pay FBT yearly. Removing its application will increase the number of taxpayers who choose to make one payment and return each year, rather than quarterly returns and payments.

Like other overdue tax payments, overdue yearly payments of FBT will still attract use-of-money interest.

Key features

Section 120S of the Tax Administration Act imposes interest on FBT paid yearly. It has been repealed. Consequential amendments have been made to the definition of "employer" in section 3(1) and to section 3(4) of the Tax Administration Act 1994.

Application date

The amendment applies from 1 April 2001, for taxpayers who pay FBT on an annual basis, and to the 2001–2002 and subsequent income years for taxpayers who pay FBT on an income year basis.

REMEDIAL ISSUES

FOREIGN INVESTMENT FUNDS – CORPORATE MIGRATION AND OTHER ISSUES

Sections CG 14(1)(ca), CG 15(2)(b) CG 23(7A) to (7D), CG 17(3)(b)(ii), CG 17(9)(b)(iii)(A), CG 19(2)(b) and CG 19(3)(b), Income Tax Act 1994

Introduction

The foreign investment fund (FIF) rules have been amended to cater for a New Zealand entity becoming a foreign entity, or corporate migration as it is commonly known. Increases have also been made to the minimum threshold (*de minimis* exemption) of investment before the rules apply, from $20,000 to $50,000, as well as to the maximum threshold for using the deemed rate of return method of calculating FIF income, from $100,000 to $250,000. A further amendment has been made to clarify that trustees are not eligible for the *de minimis* exemption.

Background

The FIF rules are part of New Zealand's international tax rules, which are designed to reduce distortions in the investment decisions of our residents. They do this by ensuring that as far as practicable, the worldwide income of New Zealand residents is taxed as it accrues.

The FIF rules were enacted in 1992 and predate the 1993 company law amendments that allow for transfers of incorporation. As a consequence, the FIF rules have now been amended to clarify how they should operate with respect to New Zealand resident investors in companies that migrate from New Zealand.

A recent example of corporate migration is Brierley Investments Limited (BIL), which transferred its place of incorporation to Bermuda but has its head office and, therefore, tax residence in Singapore. Upon its migration BIL became a foreign company for the purposes of the FIF rules and is treated as resident in Singapore. The examples set out below use the BIL scenario to illustrate the effect of the changes to the FIF rules.

Key features

- Under new subsection CG 14(1)(ca), the cost or expenditure incurred in acquiring the holding is to be the market value on the date of the change of residence. For the purposes of the *de minimis* exemption the cost of the interest will, therefore, be the market value on the day of migration rather than original cost.
- Under new subsections CG 23(7A) to (7C), the shares are considered to have been sold and reacquired on the date of the change in residence. Entry to the rules will then be at market value of the holding on the day of migration. A further consequence is that gains and losses will be crystallised at that date for tax purposes for holders of shares on revenue account.
- New subsection CG 23(7D) removes the requirement for separate financial accounts to be prepared for an entity up to the date of migration if the accounting profits method is to be used in that year by its shareholders. Apportionment of the consolidated after-tax accounting profits in the year of migration is now possible.
- Section CG 15(2)(b) has been amended for the purposes of the FIF rules generally and not just in relation to migrations:
  - to increase the *de minimis* exemption from $20,000 to $50,000. This means that shareholders whose total FIF holdings are below $50,000 cost (as outlined above in the case of corporate migrations "cost" is market value on the day of migration) are excluded from the FIF rules but will continue to be required to return their income from these foreign investments under ordinary principles—for example, return dividend income received from the company, or realised gains on disposal of investments held on revenue account, and
  - to clarify that "natural persons" excludes those acting in their capacity as trustees.
- Sections CG 17(3)(b)(ii), CG 17(9)(b)(iii)(A), CG 19(2)(b) and CG 19(3)(b) have been amended to increase the maximum level of FIF holdings, from $100,000 to $250,000, able to use the deemed rate of return method for calculating FIF income.

Application date

The amendments apply retrospectively to the 1999–2000 and subsequent income years.

Specific details for shareholders of Brierley Investments Limited

Brierley Investments Limited (BIL) ceased to be a New Zealand company on 5 January 2000.

The share price at the end of that day was $NZ0.40c (40 cents per share). This is the share price to be used for calculating both the *de minimis* exemption and the value at entry to the rules if using the comparative value method or the deemed rate of return method.

The share price at the end of 31 March 2000 was $NZ0.39c. This is the share price that should be used for calculating FIF income if using the comparative value method.

Note that these share prices are those quoted for the New Zealand share register. If you held your shares on either the Singaporean, Australian or United Kingdom share register you should use the prices relevant to your register.

With the increase in the level of the *de minimis* exemption threshold to $50,000, most New Zealand resident BIL shareholders will not be affected by the FIF rules. In particular, BIL shareholders who are natural persons (individuals) who hold 125,000 or fewer BIL shares on 5 January 2000 will be exempted from the FIF rules as long as they do not also hold other foreign investments not covered by one of the other FIF exemptions.

Note, however, that the cost threshold applies at all times during an income year, so if further BIL shares (or shares in another foreign company not otherwise exempted) were acquired after 5 January, taking the investor over the cost threshold, then all the shares would be subject to the FIF rules.

For further details on the application of the FIF rules refer to Inland Revenue's booklet *Foreign investment funds (IR 275B)*. You can order a copy by phoning INFOexpress on 0800 257 773.

For BIL shareholders that are companies, if the comparative value or deemed rate of return methods are used to calculate FIF income or loss, no foreign dividend withholding payments need be made in respect of the dividends received from BIL after 5 January 2000. If, however, either the branch equivalent or accounting profits methods are used in calculating the FIF income or loss, foreign dividend withholding payments must be made to Inland Revenue.

For further details about the foreign dividend withholding payments rules refer to Inland Revenue's booklet *Foreign dividend withholding payments (IR 274A)*. You can order a copy by phoning INFOexpress on 0800 257 773.

Obligations if you are NOT subject to the FIF rules

If you hold BIL shares but are not subject to the FIF rules you are still required to account for income from your investment according to ordinary tax rules. In particular you are required to account for:

- dividend income received before and after migration, and
- realised gains or losses on disposal if the shares were held on revenue account.

If, for example, you did not file an income tax return including the dividend income received after BIL migrated, or you did not otherwise advise Inland Revenue of the dividend income received, you need to file an *IR 3*. To order an *IR 3* you can phone INFOexpress on 0800 257 773.

To contact us with any other general business queries you can phone us on 0800 377 774.

The de minimis *exemption*

All examples assume that the taxpayer is neither trading on revenue account nor a trustee.

Example 1

Taxpayer A owns 50,000 BIL shares and no other foreign shares. At 40c, her holding had a market value at migration of $20,000. As this is below the $50,000 threshold, she will not be subject to the FIF rules.

She will, however, still have to return any dividend income every year and pay New Zealand tax on it.

Example 2

Taxpayer B owns 150,000 BIL shares and no other foreign shares. At 40c his holding has a market value of $60,000. He will therefore be subject to the FIF rules.

Example 3

Taxpayer C owns 50,000 BIL shares, as well as Australian shares that cost $50,000, British shares that cost $20,000 and American shares that cost $10,000.

He is not subject to the FIF rules as:

- Australia, United Kingdom and United States are grey-list countries (along with Canada, Norway, Japan, and Germany) and investments (excluding superannuation schemes and life insurance policies) are generally exempt from the FIF rules, and
- the market value of the BIL shares, $20,000, is less than the *de minimis* exemption of $50,000.

This illustrates that, in practice, the *de minimis* exemption is applied last after any other available exemptions.

Example 4

Taxpayer D has the same holdings as Taxpayer C, except she also owns Malaysian shares with an initial cost of $40,000.

She is subject to the FIF rules as:

The market value of the BIL shares at the time of migration is $20,000 plus the original cost of the Malaysian shares of $40,000 is $60,000. As $60,000 exceeds the *de minimis* exemption of $50,000, the holding of both the BIL and the Malaysian shares are subject to the FIF rules. The Australian, British and American shares remain outside the FIF rules, with only the dividends being taxable.

SUPERANNUATION CONTRIBUTIONS TREATED AS SALARY OR WAGES

Section NE 6 of the Income Tax Act 1994

Introduction

An amendment removes a technical problem in the specified superannuation contribution withholding tax (SSCWT) rules. It ensures that the payment of PAYE deducted from an employer's contribution to a superannuation fund, if the employee and the employer have agreed to treat the employer's contribution as salary or wages, will satisfy the employer's obligation to pay the contribution to the superannuation fund.

Background

The SSCWT rules were amended by the Taxation (Tax Credits, Trading Stock, and Other Remedial Matters) Act 1998 to allow an employee and employer to agree to have specified superannuation contributions treated as salary or wages and therefore made subject to PAYE rather SSCWT. However, the legislation did not allow the PAYE deducted and paid from the employer's superannuation contribution to be treated as satisfying the employer's obligation to pay contributions to the superannuation fund.

Section NE 6 of the Income Tax Act 1994 is the provision that deals with this technical issue in relation to SSCWT deducted from contributions.

Key features

Section NE 6 of the Income Tax Act 1994 has been amended to allow the PAYE deducted and paid to satisfy an employer's obligation to pay contributions to the superannuation fund, if the employee and the employer have agreed to treat the superannuation contribution as salary or wages. The amendment ensures that the SSCWT rules reflect the original policy intent and is consistent with the current treatment afforded to contributions subject to SSCWT.

Application date

The amendment applies retrospectively from 26 November 1998 to coincide with the enactment date of the rules that allow an employee and employer to agree to treat employer contributions to a superannuation fund as salary or wages of the employee.

LEGAL DECISIONS – CASE NOTES

This section of the *TIB* sets out brief notes of recent tax decisions made by the Taxation Review Authority, the High Court, the Court of Appeal and the Privy Council.

We've given full references to each case, including the citation details where it has already been reported. Details of the relevant Act and section will help you to quickly identify the legislation at issue. Short case summaries and keywords deliver the bare essentials for busy readers. The notes also outline the principal facts and grounds for the decision. Where possible, we have indicated if an appeal will be forthcoming.

These case reviews do not set out Inland Revenue policy, nor do they represent our attitude to the decision. These are purely brief factual reviews of decisions for the general interest of our readers.

DOUBLE DEDUCTION CLAIMED FOR TRADING LOSSES AND LOSS ON SALE OF SUBSIDIARY

Case:	*AMP Life v CIR*
Decision date:	26 October 2000
Act:	Income Tax Act 1976
Keywords:	*Double deduction, section 204C, section 191, group of companies, life insurers, section 99 avoidance arrangement*

Summary

The CIR was unsuccessful in his attempt to deny AMP a $27 million deduction under section 204C Income Tax Act 1976.

Facts

The plaintiff, AMP Life Limited ("AMP"), incorporated a subsidiary, AMP Financial Services Limited (AFS) in 1979 to conduct, through further subsidiaries, financial and investment activities. After the sharemarket crash in 1987 the group suffered losses in excess of $82 million. The companies grouped the losses under section 191 and AMP offset the loss against its income.

In December 1989 AMP subscribed for 25 million $1 shares in AFS who repaid the bulk to AMP in clearance of debt. The next day AFS transferred its shares in all subsidiaries to AMP. This left AFS without assets or function.

Having initially decided in April 1992 to liquidate the moribund AFS, AMP decided to sell the company to another subsidiary, AMP Discounts Corporation Limited ("ADC"). AFS was sold in August 1992 to ADC for $6,500 and was subsequently dissolved. In the 1993 tax year, AMP claimed a deduction for the loss on sale of AFS of $27 million, citing section 204C of the Act.

Decision

Double deduction

The Commissioner submitted that the section 204C claim by AMP was a second deduction for one economic loss. His Honour agreed (as did AMP) that in essence, there was "…only one leak from the group's resources" however, for the purposes of income tax legislation, there were two events, both of which were permitted as deductions by AMP under specific sections of the Act. In what was largely an exercise in statutory interpretation, McGechan J held that AMP was entitled under both sections 191 and 204C to a deduction and, *ipso facto*, the losses were two separate events, each capable of giving rise to a separately based deduction. His Honour, following AMP's submissions, held also that there is no "overarching principle" in tax law that proscribes double deductions and that section 106(1)(o), which was applicable at the time, only related to double deductions of the same amount. As the trading losses of AFS (deducted under section 191 by AMP) and the loss on sale of AFS were not "the same amount" there was no such double-dipping.

Section 99

The Commissioner submitted that the "arrangement" to which section 99 applied in this matter was:

- AMP offsetting and claiming the losses under section 191
- subscribing for capital in AFS
- the sale of AFS to ADC
- claiming a deduction for the loss on sale.

His Honour held that this did not amount to a "contract, agreement, plan, or understanding" but that they were a mere sequence of events each with knock-on causative consequences. To be an "arrangement" there needed to be some prior planned linking or sequencing, or both. Further, it was held that, as the capitalisation scheme was a "… normal commercial solution to an actual problem" there was no artificiality or impropriety (the hallmarks of avoidance). His Honour stated, *obiter*, that had the four steps been conceived as such from the outset, it probably would have been caught by section 99 as it ".. could well have been viewed as a claim for a deduction based on a chimera, producing a correspondingly 'magic' result."

Also *obiter*, his Honour stated that section 99 did not apply as a section 204C deduction would have been available to AMP had they liquidated AFS as initially proposed—such dissolution also amounting to a "disposal" for the purposes of the section. That being so, the "arrangement" had there been one, would not have had any tax avoidance effect.

WITHHOLDING TAX NOT DEDUCTED ON PAYMENTS TO NON-RESIDENT

Case:	TRA Number 043/99. Decision Number 20/2000
Decision date:	27 October 2000
Act:	Income Tax (Withholding Payments) Regulations 1979
Keywords:	*Double tax agreement*

Summary

The Commissioner's assessments were confirmed.

Facts

The disputant entered into three distinct transactions under which leases were entered into for (i) shipping containers, (ii) two barges, and (iii) a tug boat. The owner of the equipment in each case was a non-resident. The disputant made no deductions in respect of payments made to the owners of the equipment as required under the Income Tax (Withholding Payments) Regulations 1979.

The Commissioner, after investigation, assessed the disputant for withholding tax not deducted. The disputant issued a NOPA and initiated a challenge under the disputes resolution procedure. The adjudication process found in favour of the Commissioner and the disputant chose to have the matter heard by the Courts.

Decision

Judge Willy found that the general scheme of the regulations was to bring to tax at prescribed rates withholding payments as prescribed in regulation 4. Included are all payments to "non-resident contractors". Exemptions include payments to employees.

The disputant put forward an argument described as having "an Alice in Wonderland" quality about it. Essentially, it was that as "employees" were defined as those entitled to receive source deduction payments, and as withholding payments were source deduction payments, non-resident contractors were therefore "employees" and not subject to the regulations due to the exemption. In response, the Commissioner argued that the Income Tax Act definition is to be used "unless the context otherwise requires" and that the regulations themselves make a distinction between non-resident contractors and employees. The term employee should, therefore, bear its ordinary meaning so as to give effect to the regulations. A further point was that, to accept the disputant's argument would mean that all non-resident contractors would be excluded from the regulations, which was clearly not intended.

The argument put forward in respect of the definition of "contract activity" was similar to that used in interpreting the term "employee". It was also rejected.

Judge Willy stated that the legal onus of proof remains throughout on the disputant. The argument put forward, that they did not know the property owners were non-residents and it was therefore up to the Commissioner to prove that they were, was simply seen as an attempt to try and reverse this onus.

Judge Willy did not address directly whether the Commissioner must seek recovery from the recipient. It can be inferred quite strongly, however, that the Commissioner may seek recovery from the recipient or the payer.

REGULAR FEATURES

DUE DATES REMINDER

December 2000

5 **Employer monthly schedule**

Employer deductions

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *Employer monthly schedule (IR 348*) due
- *Employer deductions* (*IR 345*) or (*IR 346*) form and payment due

20 **Employer deductions**

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *Employer deductions* (*IR 345*) or (*IR 346*) form and payment due

Employer deductions and Employer monthly schedule

Small employers (less than $100,000 PAYE and SSCWT deductions per annum)

- *Employer deductions* (*IR 345*) or (*IR 346*) form and payment due
- *Employer monthly schedule (IR 348*) due

January 2001

15 **Employer monthly schedule**

Employer deductions

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *IR 348 Employer monthly schedule* due
- *IR 345* or *IR 346 Employer deductions* form and payment due

GST return and payment due

22 **Employer deductions**

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *IR 345* or *IR 346 Employer deductions* form and payment due

Employer deductions and Employer monthly schedule

Small employers (less than $100,000 PAYE and SSCWT deductions per annum)

- *IR 345* or *IR 346 Employer deductions* form and payment due
- *IR 348 Employer monthly schedule* due

FBT return and payment due

31 **GST return and payment due**

These dates are taken from Inland Revenue's Smart business tax due date calendar 2000–2001