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TAX INFORMATION Bulletin

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Inland Revenue
Te Tari Taake

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YOUR OPPORTUNITY TO COMMENT

Inland Revenue regularly produces a number of statements and rulings aimed at explaining how taxation law affects taxpayers and their agents. Because we are keen to produce items that accurately and fairly reflect taxation legislation and are useful in practical situations, your input into the process, as a user of that legislation, is highly valued.

A list of the items we are currently inviting submissions on can be found at **www.ird.govt.nz**. On the homepage, click on "Public consultation" in the right-hand navigation. Here you will find drafts we are currently consulting on as well as a list of expired items. You can email your submissions to us at **public.consultation@ird.govt.nz** or post them to:

Public Consultation
Office of the Chief Tax Counsel
Inland Revenue
PO Box 2198
Wellington 6140

You can also subscribe to receive regular email updates when we publish new draft items for comment.

Below is a selection of items we are working on as at the time of publication. If you would like a copy of an item please contact us as soon as possible to ensure your views are taken into account. You can get a copy of the draft from **www.ird.govt.nz/public-consultation/** or call the Team Manager, Technical Services Unit on 04 890 6143.

Ref	Draft type/title	Description/background information	Comment deadline
ED00158	Draft depreciation general determination – Buildings with reinforced concrete (default class), Buildings with steel and timber framing (default class), Buildings with timber framing (default class)	This draft determination proposes to set general depreciation default rates for various classes of buildings	30 June 2013

IN SUMMARY

Legal decisions – case notes (continued)

Abusive tax position taken when making a family assistance claim

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The disputant accepted a re-assessment by the Commissioner of her family support entitlement because her husband was paid an artificially low salary. The disputant argued that the Commissioner had not challenged her husband's tax position and accordingly, she could not be held to have taken an abusive tax position. The Taxation Review Authority found that the dominant purpose of the arrangement was to obtain family assistance the disputant was not otherwise entitled to.

Child support primary obligation is children

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The mother successfully applied for a retrospective child support departure order in the Family Court. The High Court overturned the quantum of the departure order and the mother appealed to the Court of Appeal. The Court of Appeal found that the liable parent's primary obligation was to support his children and, after ascertaining the father's true financial ability and resources overturned the High Court's finding on quantum. The Court of Appeal left open whether a departure order could be made retrospectively, although it did substitute a retrospective departure order.

NEW LEGISLATION

This section of the *TIB* covers new legislation, changes to legislation including general and remedial amendments, and Orders in Council.

CHILD SUPPORT AMENDMENT ACT 2013

The Child Support Amendment Act 2013 introduces significant reforms to the child support scheme that will come into effect over the next two years. The intention is to make the child support scheme fairer, taking more factors into account and being more flexible. The changes will take into account a wider range of individual circumstances and reflect changes in family structure and involvement in child upbringing since the child support scheme was first introduced.

The reforms introduce:

- a comprehensive new formula that takes into account the estimated cost of raising children, a lower level of minimum shared care, and the income of both parents
- improvements to the administration of the scheme such as the compulsory deduction of child support from the employment income of liable parents, and
- a two-stage late payment penalty, reduction of the monthly incremental late payment penalties after a year, and relaxation of the circumstances under which debt can be written off.

The Child Support Amendment Act 2013 also replaces some sections of the Child Support Act 1991 to reflect changes in language and definitions.

There are some transitional provisions to allow the Commissioner to collect and update information required for the new child support formula and to allow assessments to be prepared in time for the child support year commencing 1 April 2014. Savings provisions also apply. The transitional and savings provisions came into effect from date of Royal assent.

Information relating to the formula assessment will be published on Inland Revenue's website and updated regularly. The website will also contain calculators to help people determine the level of shared care and child support liabilities.

Background

The Child Support Act 1991 is over two decades old. The child support scheme is primarily a back-up arrangement that operates when parents do not live together and cannot reach agreement over the financial support of their children. In some cases where voluntary agreements are reached, the collection and distribution of child support can be administered by Inland Revenue. It also applies when the receiving carer is receiving a social security benefit.

In September 2010, the Minister of Revenue released a government discussion document entitled *Supporting children—a Government discussion document on updating the child support scheme*. The discussion document consulted on ways to update the child support scheme and make the scheme fairer to the parents involved. Over 2,000 people participated in the consultation.

In August 2011, Cabinet agreed to a number of changes and introduced the Child Support Amendment Bill 2011. Fifty-nine submissions were received by the Social Services Select Committee, which made a number of changes. Further minor changes were made at the Committee of the Whole House by Supplementary Order paper. The bill received its third reading on 9 April 2013 and received Royal assent on 16 April 2013.

Key features

The reforms have three key features:

- a comprehensive new formula for child support assessments
- improving the way the child support regime operates, and
- improving the way penalties and debt are managed.

Changes regarding the operation of the formula include:

- recognising the income of the receiving parent as well as the liable parent
- a new definition of income that includes most of the family scheme income adjustments in the Income Tax Act 2007 such as income in family trusts and some fringe benefits
- changing how allowances relating to the living costs of the parent and their children are determined, including a multi-group allowance, and no longer including an allowance for a new partner or children who are not legally dependent children of the parent, and

- recognising minimum care levels from 28% of nights (previously 40% was required) and allowing for daily care to be considered in some cases.

Other changes to the operation of the child support scheme have also been made. These include:

- recognising re-establishment costs as an administrative review ground in some circumstances
- allowing the Commissioner to rely on parenting orders and agreements when establishing care levels
- reducing the qualifying age of children subject to child support from under 19 to under 18, unless they are aged 18 and still in secondary education, and
- changes to the way estimations of income are calculated.

Changes to the rules relating to the payment of child support, the imposition of penalties and the writing-off of penalties and debt include:

- extending automatic deduction of child support from employment income of liable parents, except where automatic deduction is considered inappropriate by the Commissioner
- introducing a Commissioner discretion to allow various prescribed payments to be recognised for child support purposes, such as payment of the child's school fees
- a two-stage initial penalty, with the current full 10% penalty only applying if the debt remains unpaid after 7 days
- reducing the incremental monthly penalty from 2% to 1% after a year
- relaxing the circumstances in which penalties can be written-off, including when a liable parent enters into an instalment arrangement or is in financial hardship, or where debt recovery is an inefficient use of the Commissioner's resources
- allowing the Commissioner to write off assessed debt on serious hardship grounds where it is owed to the Crown, and
- allowing the Commissioner discretion for further offsetting of ongoing child support payments against child support arrears.

Detailed analysis

Assumptions about parents

New section 7B says the Commissioner is entitled to assume, when making a formula assessment, that a qualifying child has two parents and that those parents are living apart. The Child Support Amendment Act 2013 is written on the basis of this assumption; however, there are situations when these assumptions will be incorrect. For example, there may be three legal parents of a qualifying child and two of those parents may be living together. The Commissioner may make any necessary modifications to the provisions of the Child Support Act 1991 to reflect the true position.

Who is a liable parent and receiving carer under a formula assessment?

The new legislation has changed some of the terminology and the associated definitions in the Child Support Act 1991. This is particularly relevant for determining, under a formula assessment, who is a liable parent and who is a receiving carer.

A parent of a qualifying child is a liable parent if the parent's income percentage is greater than or equal to their care cost percentage for that child. Likewise, a parent of a qualifying child is a receiving carer if the parent's income percentage is less than their care cost percentage for the child.

A non-parent carer of a qualifying child can also be a receiving carer if they provide at least 35% of ongoing daily care to the child. A non-parent carer is not assessed on their level of income as they cannot be liable for child support payments. A care cost percentage will be established to help determine how much child support they receive.

A liable parent may have their liability assessed as nil. This may occur if:

(a) the liable parent provides more than 65% of ongoing daily care to the child, or

(b) the liable parent provides at least 28% of ongoing daily care to the child and the liable parent's income percentage is equal to their care cost percentage, or

(c) no receiving carer provides at least 35% of ongoing daily care to the child.

A receiving carer will receive child support payments, unless they provide less than 35% of the ongoing daily care to the child.

A reassessment of child support components, for example, a change in the levels of ongoing care or income, can result in a person changing from being a liable parent to a receiving carer and vice versa.

Formula assessment of child support

The formula for assessing child support is being replaced to recognise the income levels and care levels of *both* parents, and the estimated average expenditure of raising children in New Zealand.

The current formula will be replaced, from 1 April 2014, by the following:

(i% – c%) × p

where –

i% is the parent's share of the combined child support income of the parents for a child

c% is the care cost percentage based on the recognised care levels of the person, and

p is the child expenditure amount for a qualifying child.

The liability is determined by the parent's income percentage minus the parent's care cost percentage, multiplied by the child expenditure amount for the child.

The cost of raising children is apportioned between parents according to the difference between their respective share of combined child support income as adjusted by their share of each child's care (if at least 28%). If their care cost percentage (where the care percentage is at least 28%) is the same as their income percentage, a parent is assumed to have met their financial contribution to costs for the child under the child support scheme, unless the Child Support Act 1991 says otherwise. For example, a minimum amount of child support may be payable.

Income of both parents

The child support income of the parents of a qualifying child is added together to determine the combined child support income. A parent's income percentage is derived by dividing their child support income amount by the combined child support income of all the parents of the child.

The child support income for a parent is determined by calculating the parent's adjusted taxable income and deducting:

- a living allowance
- any dependent child allowances, and
- any multi-group allowance.

When a parent has other dependent children, or is paying or receiving child support (administered by Inland Revenue) for children in other relationships, that parent's income will be reduced for their assumed expenditure on those other children.

A negative amount is not allowed, so if the allowances are greater or equal to the adjusted taxable income then the child support income for the parent is treated as being nil. This could arise with parents who are solely reliant on social security benefits.

Definition of Adjusted Taxable Income

The income used to calculate child support will be more closely aligned to the definition of family scheme income used for Working for Families tax credits. A person's adjusted taxable income is defined in new section 35, as replaced by the Child Support Amendment Act 2013. It is their taxable income adjusted as necessary to determine the person's family scheme income under subpart MB of the Income Tax Act 2007, with the following exceptions:

- child support and spousal maintenance received will not be counted as income
- income derived by a dependent child, such as interest, dividends, royalties and rent will not be counted, and
- income of a spouse who is non-resident will not be counted.

This means that the definition of adjusted taxable income for calculating child support income will now include:

- wages and salary that is exempt from income tax under a specified Act or regulation, such as the Consular Privileges and Immunities Act 1971
- PIE income that is not "locked in"
- overseas pensions that are tax exempt in New Zealand
- business and investment losses, such as losses from rental property, which have been used to reduce net income for tax purposes
- income retained in a close company where the person is a major shareholder
- distributions from superannuation schemes and retirement savings schemes (other than KiwiSaver schemes) where the person is still employed and their employer had recently made contributions to the scheme
- income derived by a trustee of a person's trust, where the person is a settlor of the trust
- fringe benefits received where the person is a major shareholder-employee
- deposits into main income equalisation accounts
- tax exempt pensions and annuities, and
- other payments received by the person and used to replace lost income or to meet their usual living expenses, where the total exceeds $5,000 a year. This can include distributions from a trust that the parent is not a settlor of.

A more extensive description of the adjustments under family scheme income can be found on Inland Revenue's website and in previous *Tax Information Bulletins*.

For the period between 1 April 2014 and 1 April 2015, a person's adjusted taxable income for a child support year will be their taxable income without any adjustments. This reflects that taxable income for a child support year usually relates to past tax year periods and the deferral of the use of adjustments for an extra year reduces the degree of effective retrospectivity that could arise from the change in definition.

If a person has no adjustments to their income, and their taxable income is solely derived from withholding income (wages, salary, interest or dividends), then a person's taxable income will be determined by their employment income in the calendar year immediately preceding the start of the child support year.

Otherwise, a person's taxable income in the tax year immediately preceding the most recent tax year will be used and inflated by the inflation percentage for the child support year. Likewise, the adjustments to the taxable income will be those relating to the tax year immediately preceding the most recent tax year.

Living allowance

A living allowance is provided for a parent based on the annual gross rate of various social security benefits. If the person has been granted a domestic purposes benefit (for care at home of the sick or infirm) at the sole parent rate or an invalid's benefit at the sole parent rate, then the appropriate rate is the living allowance for that parent. For everyone else the living allowance is set at the rate for a sole parent on the domestic purposes benefit. The living allowances will be updated annually in line with changes to the benefit rates.

The living allowances that apply to child support years will be available on Inland Revenue's website.

The names of the benefits have recently been changed by the Social Security (Benefit Categories and Work Focus) Amendment Act 2013. The name changes take effect in the Child Support Act 1991 in July 2013. The old benefit names will be reintroduced by the Child Support Amendment Act 2013 on 1 April 2014. References to old benefit names in the child support legislation, however, can be read as a reference to the new benefit names, and likewise for section references. Names and references will be updated in the Child Support Amendment Act 2013 at a later date.

Dependent child allowances

A child allowance is provided for each dependent child of the parent. A dependent child is a child of whom:

- the person is a parent under section 7 of the Child Support Act 1991, and
- who is maintained as a member of the parent's family and for whom the parent provides at least 28% of the on-going daily care, and
- is not a child for whom child support is to be paid, and
- meets the other requirements of a dependent child such as being under 19/18, not financially independent and not married, or in a civil union or a defacto relationship.

The allowance is based on the same method for calculating child support for a qualifying child. It is the parent's care cost percentage for the dependent child multiplied by the appropriate amount taken from the child expenditure table for that child based on the adjusted taxable income, less living allowance, of that parent alone.

The amount of a dependent child allowance is determined by the formula:

$$c\% \times \frac{e}{n}$$

where –

c% is the care cost percentage of the parent in relation to the dependent child

e is the amount determined by the child expenditure table in respect of the dependent child on the basis of:

- the child support income amount of the parent alone, with that amount being treated as the adjusted taxable income of the parent, minus the parent's living allowance
- the total number of the parent's dependent children, and
- the age group of those children

n is the total number of the parent's dependent children.

Multi-group allowance

A liable parent may have child support liabilities for more than one group of children. This is referred to as multi-group. A multi-group allowance is calculated based on the same method of calculation for child support and the dependent child allowance. A multi-group allowance is the sum of the multi-group costs of each child of the parent who is not in the same child support group as the child being assessed. This recognises that the parent has financial responsibility for other children outside the child support group.

Multi-child cap and multi-group cost

The amount of child support liability of a parent can be capped where a parent has qualifying children in more than one child support group. This is referred to as the multi-group cap. The purpose of the multi-group cap is to avoid liable parents paying more in child support than they would pay if all the children for whom they are liable to pay child support were living together.

The multi-group cap for a child is the amount determined as:

(100% – c%) × m

where –

c% is the parent's care cost percentage in relation to the child

m is the multi-group cost of the child

The multi-group cost of a child is the amount determined by the child support expenditure table in respect of that child divided by the number of all the children in all of the parent's child support groups. When determining the amount in the child expenditure table, the income amount is the income of that parent alone, the number of children is the total number of children of the parent in all child support groups, and as if all those children were the same age as the child being assessed.

Care percentage

The Commissioner must establish the proportion of ongoing daily care for a qualifying child. Shared care for child support purposes is currently set at a minimum of 40% of nights during the year. This has been replaced by a minimum of 28% of nights during the year. This equates to two nights per week on average. For this purpose a year is assumed to be 365 days. The proportion of care is set as a whole percentage figure, with figures rounded as set out in section 15 as replaced by the Child Support Amendment Act 2013.

The Commissioner must rely on the content of any care order or agreement relating to a qualifying child when establishing the proportion of ongoing care. This may be challenged by a parent or carer if they have evidence that the care order or agreement should not be relied upon.

If there is no care order or agreement, the Commissioner must establish the proportion of care primarily on the basis of the number of nights that the child spends with a carer. If the number of nights is not a true reflection of the proportion of care actually provided by a carer, the Commissioner can use the amount of time that the carer is the person responsible for the daily care of the child.

To be a receiving carer, a person must have at least 35% of ongoing daily care. This means that there can be no more than two receiving carers for a qualifying child at the same time.

Care cost percentage

The care cost percentage reflects the amount of costs a parent incurs supporting the care of a child, relative to the amount of time that child is in their care. The care percentage is converted into a care cost percentage using a table in Schedule 2 as inserted by the Child Support Amendment Act 2013. The table has a tiered series of thresholds determining the person's care cost percentage based on their level of ongoing recognised care. A proportion of care that is less than 28% results in a care cost percentage of 0% and a proportion of care of 73% or more results in a care cost percentage of 100%. Between 28% and 73% is a tiered level of care cost percentage. For example, if the proportion of ongoing daily care is 30% the care cost percentage is 24%. If a carer's proportion of ongoing daily care is 37% their care cost percentage is 29%.

Child expenditure amount

The amount of child support is based on the estimated average cost of children in New Zealand. The cost of children varies based on age, number of children in a child support group and the combined income of the parents. The new scale of costs reflects up to date information on the expenditure involved in raising children, after allowing for likely tax credits. The cost of children is set as a percentage of income and differs based on the level of income. Income levels are grouped in bands set relative to the annualised amount of the average weekly earnings as published by Statistics NZ. These bands will be updated annually.

As incomes rise the percentages in the table decline to reflect that the proportion of income spent on children declines as income rises. The new formula also has a cap on the amount of expenditure for a child when child support income is more than two and a half times the average weekly earnings.

The child expenditure table will be published by Inland Revenue and will be available on Inland Revenue's website.

The child expenditure amount for a qualifying child in a child support year is the relevant amount determined in the child expenditure table divided by the number of children in the same child support group as the child.

A child support group describes the qualifying children (where there is more than one) of a parent who all share the same other parent and in relation to whom child support for that time has been or is being assessed. A parent could have qualifying children in more than one child support group.

Examples

Calculators and examples will be available on Inland Revenue's website to help people understand how the new formula works and the potential impact of the new formula on their own situation. The following examples demonstrate how the new formula works in some different situations.

Example 1: Paul and Ally's situation

Paul and Ally have recently split up. They have two children, Dylan aged 10 and Nathan aged 6. Ally is the main carer for Dylan and Nathan and she is not in paid employment. She receives a benefit from Work and Income for herself and the children. When Work and Income granted Ally a benefit she was required to apply for a child support assessment.

Paul spends time looking after his children but this is not enough to be recognised for child support purposes. Ally receives a benefit of $17,429 a year before tax. Paul is currently in full time employment and earns $72,610.40 a year before tax.

Calculation	Ally	Paul
Taxable income	$17,429	$72,610.40
Less living allowance	−$17,429	−$17,429.00
Child support income	$ 0	$55,181.40
Ally and Paul's combined child support income is $55,181.40 and this will be used to calculate child support liability.		
Percentage share of combined child support income	0%	100%
Care cost percentage	100%	0%
Percentage of income less care cost percentage	−100%	100%

Because Paul's income percentage less care cost percentage is positive, he is assessed as the liable parent, and is required to pay 100% of the annual cost of raising Dylan and Nathan. The annual cost of raising Dylan and Nathan based on Ally and Paul's combined child support income and using the expenditure on children table is $12,880.

Paul's liability $12,880 × 100% is $12,880

Paul is assessed to pay an annual amount of $12,880 or $1,073.35 per month, for the care of Dylan and Nathan. Because Ally receives a sole parent benefit, this payment will be used to help cover the cost of this benefit.

Example 2: Liam and Kirsty's situation—shared care

Liam and Kirsty are separated. Together they have two children, Joshua aged 12 and Olivia aged 10. They have always agreed to share the responsibility of caring for their children. Joshua and Olivia both spend alternate weeks (Monday to Friday) at each parent's house, but they spend every weekend and the school holidays with Liam.

Liam has care of the children for 65% of the time and Kirsty has them for the remaining 35%. Because both Kirsty and Liam look after their children for more than 28% of the time, these percentages will be used when working out the child support assessment.

Calculation	Liam	Kirsty
Taxable income	$53,152	$50,292
Less living allowance	−$17,429	−$17,429
Child support income	$35,723	$32,863
Liam and Kirsty's combined child support income is $68,586		
Percentage share of combined child support income	52%	48%
Care cost percentage	75%	25%
Percentage of income less care cost percentage	−23%	23%

Because Kirsty's income percentage less care cost percentage is positive, she is assessed as the liable parent, and is required to pay 23% of the annual cost of raising Joshua and Olivia. The annual cost of raising Joshua and Olivia based on Liam and Kirsty's combined child support income and using the expenditure on children table is $15,561.

Kirsty's liability $15,561 × 23% is $3,579

Kirsty is assessed to pay an annual amount of $3,579 or $298.25 per month, for the care of Joshua and Olivia.

Example 3: Valerie, Lee and Jan's situation: non-parent receiving carer

Lee and Jan have one child together from their relationship, Sam aged 4. Lee and Jan have separated and they have asked Valerie, Sam's grandmother, to look after Sam. Valerie applies for child support for Sam. She must apply for it from both Lee and Jan.

Lee and Jan both work full-time and have no other children. Lee earns $35,212 a year before tax and Jan earns $45,092 a year before tax. Because Valerie isn't Sam's parent, her income is not used when working out the child support calculation.

Calculation	Lee	Jan
Taxable income	$35,212	$45,092
Less living allowance	−$17,429	−$17,429
Child support income	$17,783	$27,663
Lee and Jan's combined child support income is $45,446		
Percentage share of combined child support income	39%	61%
Care cost percentage	0%	0%
Percentage of income less care cost percentage	39%	61%

Both Lee and Jan's income percentage less care cost percentage is positive, so they are both assessed as liable parents. Lee is required to pay 39% of the annual cost of raising Sam and Jan is required to pay 61%. The annual cost of raising Sam based on Lee and Jan's combined child support income and using the expenditure on children table is $7,343.90.

Lee's liability $7,343.90 × 39% is $2,864.10

Lee is assessed to pay an annual amount of $2,864.10 or $238.70 per month, for Sam's care.

Jan's liability $7,343.90 × 61% is $4,479.80

Jan is assessed to pay an annual amount of $4,479.80 or $373.30 per month, for Sam's care.

Valerie will receive the amounts that both Lee and Jan have been assessed to pay. Note that Valerie can ask for either of these amounts not to be collected.

Example 4: John's situation—multi group allowance

John has two children from a previous relationship, Jade aged 16 and Emma aged 11. John looks after Jade and Emma some of the time during the year, but not enough for it to be recognised for child support purposes. John earns $82,714 a year before tax.

Because John has children with more than one other parent, he is a multi-group child support customer, so is entitled to a "multi-group allowance" for Jade and Emma. The child support for each of his children is calculated separately, but must take into account that he has another child in a separate child support calculation.

Note: Before working out the child support formula for each of John's children, we must first work out his multi-group costs for each child. This is used for the multi group allowance.

John's multi-group allowance

John earns $82,714 a year before tax. After subtracting his living allowance, John's child support income for calculating the multi group allowance is $65,285.

We use the child expenditure table to work out the multi-group allowance based on $65,285.

Annual cost of raising two children (aged 0 – 12):

$14,901 divided by two children is $7,450.50

Emma is 11 so John's multi-group allowance for Emma is $7,450.50.

Annual cost of raising two children (aged 13 and older):

$18,165 divided by two children is $9,082.50

Jade is 16 so John's multi-group allowance for Jade is $9,082.50.

Child support for Emma

Emma's mother is Kim, she is Emma's main carer. Kim earns $65,112 a year before tax.

Calculation	John	Kim
Taxable income	$82,714	$65,112
Less living allowance	−$17,429	−$17,429
Sub-total	$65,285.00	$47,683.00
Multi-group child allowance	−$9,082.50	$0
Child support income	$56,202.50	$47,683
John and Kim's combined child support income is $103,885.50		
Percentage share of combined child support income	54%	46%
Care cost percentage	0%	100%
Percentage of income less care cost percentage	54%	−54%

Because John's income percentage less care cost percentage is positive he is assessed as the liable parent, and should pay 54% of the annual cost of raising Emma. The annual cost of raising Emma based on John and Kim's combined child support income and using the child expenditure table is $14,076.45.

NEW LEGISLATION

John's formula assessed child support for Emma
$14,076.45 × 54% is $7,601.30

John's liability for Emma will be the lesser of the amount we calculated in the formula, or the multi-group cap.

Multi-group cap for Emma

$7,450.50 × (100% minus 0%) is $7,450.50

John's annual liability for Emma is $7,450.50 because the multi-group cap is less than the formula amount calculated.

Child support for Jade

Jade's mother is Mary; she is Jade's main carer. Mary earns $45,092 a year before tax.

Calculation	John	Mary
Taxable income	$82,714	$45,092
Less living allowance	−$17,429	−$17,429
Sub-total	$65,285	$27,663
Multi-group child allowance	−$7,450.50	$0
Child support income	$57,834.50	$27,663
John and Mary's combined child support income is $85,497.50		
Percentage share of combined child support income	68%	32%
Care cost percentage	0%	100%
Percentage of income less care cost percentage	68%	−68%

Because John's income percentage less care cost percentage is positive, he is assessed as the liable parent and should pay 68% of the annual cost of raising Jade. The annual cost of raising Jade based on John and Mary's combined child support income and using the child expenditure table is $15,661.65.

John's formula assessed child support for Jade is
$15,661.65 × 68% is $10,649.90

Multi-group cap for Jade

$9,082.50 × (100% minus 0%) is $9,082.50

John's annual liability for Jade is $9,082.50 because the multi-group cap is less than the formula amount calculated.

Summary

John's annual liability for both children is $16,533 or $1,377.75 per month.

Estimation of taxable income

The provisions for providing an estimation of taxable income will be replaced to reflect the new formula assessment.

A person can elect to provide an estimate of taxable income when calculating the adjusted taxable income amount if they expect their taxable income to reduce by 15% or more. An estimate may be for a full child support year or for part of the year. The Commissioner may refuse an estimate on a variety of grounds, including if the annualised estimated income is more than the original taxable income.

If the Commissioner accepts an estimate of taxable income for a period, the adjusted taxable income is recalculated for the period and the formula assessment is adjusted.

A person can give notice to revoke an estimate or can make a subsequent estimate.

Where estimates have been provided, there is an end of year reconciliation to determine if child support has been overpaid or underpaid in the estimation period. The Commissioner must take whatever steps are necessary to ensure that the correct amount of child support is assessed for the child support year.

A person will be liable to a penalty if their year to date income and their estimated taxable income for the elected period is less than 80% of their actual taxable income for the child support year. The penalty is set at 10% of the difference between the child support payable for the period under the estimated taxable income and the child support assessed for the same period through the end of year reconciliation.

Minimum annual rate of child support

The legislation sets out a minimum annual rate of child support, where a liable parent has been assessed as having to pay child support in relation to any qualifying children. The rate is currently set at $871 for the child support year commencing on 1 April 2013. The rate is adjusted each year by inflation.

Payment of child support to receiving carers

The legislation sets out how child support payments in respect of a qualifying child are distributed to receiving carers.

Where child support payment is to a sole receiving carer who is a parent

The child support liability and the amount payable to the receiving carers is usually determined by the standard formula or under the multi-group cap. Where, in respect of a qualifying child, there is only one receiving carer and that carer is a parent of the child, then the annual amount of child support payment can be calculated by reference to the receiving parent's care cost and income percentages. This only applies if the amount will be less than the amount calculated under the standard formula or under the multi-group cap.

If the criteria are met, the amount of child support payable in respect of this receiving parent is a proportion of the cost of raising the child; determined by how much their care cost percentage exceeds their income percentage. In the legislation this is expressed as an amount that the receiving parent would pay if the difference between their income percentage and the care cost percentage were a positive percentage.

Example

Alisa has 46% of the combined child support income and her care cost percentage is 100%. She is a receiving carer as the percentage of income less care cost percentage is –54%. As the sole receiving carer for the child, the amount she could receive would be 54% of the relevant annual cost of raising the qualifying child (if this is less than the amount under the standard formula or the multi-group cap).

Where child support payment is to a sole receiving carer who is not a parent

The amount payable where there is only one non-parent receiving carer is the amount of child support determined by the formula assessment.

Where there are two receiving carers and neither are parents of the child

If there are two receiving carers of a qualifying child and neither are parents of the child, the child support payment will be distributed to them based on the relative care cost percentage of each receiving carer.

Example

Patrick is assessed as having to pay child support of $5,000. His child is being cared for by Jo and Lyn. Jo provides 40% of the care cost and receives $2,000 and Lyn provides 60% of the care cost and receives $3,000.

Where one receiving carer is a parent and the other is a non-parent receiving carer

In this situation, the legislation determines how much is payable to the receiving parent, and any remaining amount of the child support payment in respect of the child goes to the non-parent receiving carer.

The amount that goes to the receiving parent is the amount that the receiving parent would pay if the difference between their income percentage and the care cost percentage were a positive percentage. If the multi-group cap applies, the amount is determined by multiplying the difference between the receiving parent's income percentage and care cost percentage (expressed as a positive percentage) by the amount payable under the liable parent's multi-group cap.

Example

William is assessed as having to pay child support of $3,000. Care of his child is being shared between the child's mother, Lisa and grandmother Kiri. Both provide more than 35% of ongoing daily care. Lisa is assessed based on the difference between her income percentage and the care cost percentage as receiving $1,900. Kiri receives the remaining $1,100.

Where the minimum annual rate is payable

Where a minimum annual rate is set as a parent's child support liability, the proportion payable in respect of each receiving carer is to be on the basis of the number of qualifying children of the liable parent that each carer provides care for.

Example

Harry is assessed as having to pay the minimum annual rate of child support of $871. He has three qualifying children. The eldest is being cared for by Belinda and the other two are cared for by Alison. Belinda will receive 1/3 of the minimum annual rate and Alison will receive 2/3 of the minimum annual rate.

Age of a qualifying child

The age at which a qualifying child ceases to qualify, and at which point child support is no longer payable, has changed. Currently the age is set at when the child turns 19 years old. This is being reduced to 18 years old, unless the child is 18 years and still enrolled at and attending a registered or overseas school. An 18 year old who is at a registered school until the end of the school's academic year will continue to be a qualifying child until 31 December in that year, as long as they continue to meet other requirements such as not being financially independent. This change brings the definition of a qualifying child closer to the maximum age for a dependent child under the Working for Families tax credits scheme.

The change takes effect from 1 April 2015, as the Child Support Amendment Act 2013 requires that in relation to the child support year commencing 1 April 2014, a qualifying child is to be read as referring to a child aged under 19 years.

Waiver of right to payment

A non-parent receiving carer may give notice to waive their right to receive child support payments yet to be paid by a liable parent for that child. This might arise, for example, where the non-parent receiving carer is a relative of one of the liable parents and does not wish to collect child support from their family member, but wishes to collect child support from the other liable parent. The non-parent receiving carer cannot waive their right if they are receiving an unsupported child's benefit for the child. Similarly, the waiver is revoked if the non-parent receiving carer begins to receive an unsupported child's benefit for the child.

Departure from formula assessment: re-establishment costs

There are currently several grounds on which a parent can seek an administrative review. The legislation will allow parents to seek an administrative review to have re-establishment costs taken into account when calculating liability. This addresses situations where a parent works additional hours to earn more income to pay costs to re-establish a home for themselves and others they have a duty to maintain. The additional income would usually lead to an additional child support liability or reduced child support entitlement, but re-establishment costs may now be taken into account through an administrative review.

Automatic deduction of child support from wages and salary

All liable parents receiving employment income will have child support deducted from their employment income. Automatic deduction of child support currently occurs where a parent has been in default or receives a social security benefit. The amendments will extend automatic deduction to parents who are:

- PAYE or ACC income recipients, which covers most wage and salary earners, or
- a student allowance recipient.

The Commissioner may consider that it is inappropriate to use automatic deductions for a person due to administrative, cultural, privacy or other exceptional reasons. Other acceptable methods must be used to pay child support.

Qualifying payments

Liable parents may be able to have some or all of their child support liability offset in recognition of qualifying payments having been made for the child's direct benefit.

Qualifying payments are payments made by or on behalf of the liable parent to a person for goods and services that directly benefit the child. An example would be the payment of school fees for the child.

Conditions exist for the recognition of a qualifying payment. These are where:

- child support is paid on time and there is no outstanding debt
- the liable parent does not qualify for shared care
- the liable parent and the receiving carer agree on the qualifying payment
- the receiving carer is not a social security beneficiary;
- the qualifying payment is at least 10% of the child support liability for the child, and
- the liable parent does not have at least 28% care of the child.

Penalty provisions

The penalty provisions have been changed. Penalties play an important role in encouraging parents to meet their child support obligations. However, excessive penalties can discourage the payment of child support to the detriment of the children concerned.

Initial late payment penalty

Currently, the initial late penalty payment applies as the greater of $5 or a 10% charge applying the day after the due date. This appears excessive if the lateness resulted from an oversight. The new provision is to apply the initial late penalty payment as the greater of $5 or a 2% charge on the overdue amount of financial support on the day after the due date. There would be a further 8% charge on the overdue amount (excluding the $5 or 2% penalty) seven days after the due date. This will provide liable parents a little bit more time to ensure their child support is paid before the full 10% penalty is applied.

Incremental late payment penalty

Currently, the incremental late payment penalty applies a 2% charge every month until the debt (including penalties) is cleared. The new provision will charge the incremental late payment penalty in two steps:

- 2% of the overdue amount each month for up to 12 months after the due date, and
- 1% of the overdue amount each month from 12 months after the due date until the debt is cleared.

The provisions relating to a liable person's financial support debt can also apply to a payee's debts arising from overpayments.

Write-off provisions

The circumstances under which penalties and debt can be written off have been expanded from 1 April 2015. The starting position for writing off penalties recognises that a liable parent who comes to Inland Revenue to arrange the payment of a debt is trying to comply.

Penalties can be fully or partly written off where a paying parent has agreed and adhered to an instalment arrangement and/or paid off the financial support debt, and where recovery of penalties would place the liable person in serious hardship or involve an inefficient use of the Commissioner's resources. The Commissioner can also decline to enter into a payment agreement where the liable person has not complied with earlier payment agreements and no reasonable cause existed for the non-compliance.

The Commissioner will be able to write off some, or all, of the benefit component of assessed child support debt (where the receiving carer was in receipt of a social security benefit). Debt would be able to be written-off on serious hardship grounds or if it was an inefficient use of the Commissioner's resources.

The Commissioner may also write off debt that is payable by the estate of a liable person if the liable person's estate is insufficient to pay the debt. Similarly, the Commissioner may write off debt that is payable by a liable person if the receiving carer has died and the Commissioner is satisfied that the amount is for any reason unlikely to be recovered.

Offsetting child support payments

Currently, if two parents are each liable to pay the other an amount of child support, the Commissioner may offset one liability against the other. In future, the Commissioner will have discretion to offset monthly child support liability against child support arrears. Offsetting of liability cannot occur for a parent, if their child support entitlement is owed to the Crown—that is, they are a social security beneficiary.

Application date(s)

Sections 6, 31, 32 and new Schedule 1 came into force on the day after the date of Royal assent. These contain transitional and savings provisions.

The rest of the Child Support Amendment Act 2013, except Part 2, comes into force on 1 April 2014; and relates mainly to the new child support formula.

Part 2 of the Child Support Amendment Act 2013 comes into force on 1 April 2015; and relates mainly to changes in penalties and debt.

STUDENT LOAN SCHEME AMENDMENT ACT 2013

The Student Loan Scheme Amendment Bill (No 2) was introduced into Parliament on 23 August 2012, receiving its first reading on 20 September 2012, its second reading on 28 February 2013 and the third reading on 28 March 2013. It received Royal assent on 29 March 2013.

The new legislation brings into effect two key measures to:

- broaden the definition of income for student loan repayment purposes to align generally with that used for Working for Families tax credits, and
- implement an on-going information-match with the New Zealand Customs Service to identify borrowers who are in serious default on their loans when they enter or leave New Zealand.

The new legislation also contains several administrative efficiency measures.

Supplementary Order Paper No 185 amended the transitional regulation-making provision in the new legislation to clarify its operation.

The Supplementary Order Paper also included several amendments to ensure clarity, alignment of terminology, and correction of certain references and cross-references to ensure the legislation operates as intended.

The new legislation amends the Student Loan Scheme Act 2011, the Accident Compensation Act 2001, the Customs and Excise Act 1996, the Privacy Act 1993, the Student Loan Scheme Amendment Act 2012, the Student Loan Scheme (Budget Measures) Amendment Act 2012, and the Tax Administration Act 1994.

All section references are to the Student Loan Scheme Act 2011 unless otherwise stated.

BROADENING THE DEFINITION OF "INCOME" FOR STUDENT LOAN REPAYMENT PURPOSES

Sections 4, 73, 74, 76, 79, 83, 114, 114A, 202, schedule 1 (clause 11) and schedule 3

The new legislation makes changes to the definition of income for student loan repayment purposes to ensure that a borrower's repayment obligation accurately reflects their ability to repay their loan by including income from sources not currently included in the definition.

Background

The student loan scheme is an income-contingent scheme, meaning that the amount that a New Zealand-based borrower has to repay in any year is dependent on their income.

The previous definition of "income" for student loan repayment purposes captured income taxed to the individual rather than to another entity. It included income such as salary and wages, New Zealand superannuation, interest, dividends, business income and rental income.

For borrowers who derive other types of income, the previous definition of income may not have reflected their actual earnings or financial resources which were available to meet their student loan repayment obligation.

Broadening the definition ensures that a borrower's repayment obligation accurately reflects their ability to repay.

The change to the definition of "income" for student loan repayment purposes follows changes signalled by the Government in 2010 relating to the way that income should be defined for the purposes of Working for Families tax credits and other social policy programmes.

Broadening the definition to better align with that used for Working for Families ensures there is greater consistency across all social policy initiatives to improve the integrity of the social assistance system. It follows initial changes made in April 2012 to excluded investment and business losses such as rental losses for student loan repayment purposes.

Key features

The definition of "income" for student loan repayment purposes has been expanded to include further adjustments to ensure repayment obligations are determined on a fair and equitable basis for all borrowers who earn different types of income. The adjustments include types of income not previously captured so that the definition of income for student loan repayment purposes is broadly aligned with the definition of "family scheme income" under the Working for Families tax credit rules.

Application date

The amendments apply from 1 April 2014, for the 2014–15 and later tax years.

Detailed analysis

Section 73 simplifies the definition of "adjusted net income" to mean "net income" as defined in section YA 1 of the Income Tax Act 2007, with adjustments set out in new schedule 3.

The new adjustments to "net income" in schedule 3 cover:

- tax-exempt salary and wages, and certain overseas pensions that are exempt from New Zealand tax (clause 5)
- PIE income that is not "locked in" (clause 6)
- main income equalisation scheme refunds (clause 7)
- income kept in a closely held company (clause 8)
- distributions from superannuation schemes that relate to contributions made by a person's employer within the last two years, when the person has not retired (excluding KiwiSaver and locked-in superannuation schemes) (clause 9)
- distributions from a retirement savings scheme when the person has retired early (clause 10)
- income from a trust and companies owned by trusts when the borrower is the settlor (clause 11)
- fringe benefits received by shareholder-employees who control the company (clause 12)
- main income equalisation scheme deposits (clause 13)
- 50% of non-taxable private pensions and annuities (clause 14), and
- payments from trusts, not being beneficiary income, when the borrower is not the settlor (clause 15).

The adjustments above, except those relating to clauses 8 and 15, are based on recent adjustments for Working for Families tax credit purposes. For more information refer to the *Tax Information Bulletin* Vol 23, No 1 (February 2011) at **www.ird.govt.nz** "Newsletters and bulletins".

Income kept in a closely held company (clause 8)

Under the new rules, if a borrower is a major shareholder in a close company a portion of the company's net income for the year will be included as the borrower's income for student loan repayment purposes.

The purpose of this adjustment is to attribute income to the borrower from a company in which they exercise a degree of control, that is they can influence the extent to which the company distributes income to its shareholders. This extends the adjustment currently used for Working for Families tax credits to apply to determining income for student loan repayment purposes.

A close company is one in which there are five or fewer shareholders and a major shareholder in a closed company is a person who controls at least 10% of the company (refer to the definitions in section YA 1 of the Income Tax Act 2007).

The portion of the company's income attributed to the borrower is a function of how many shares the borrower owns and the company's net income calculated using the formula:

$$(a / b) \times c$$

where –

a is the number of shares issued by the company and held by the borrower, excluding fixed-rate shares, on the last day of the company's accounting year

b is the number of shares issued by the company, excluding fixed-rate shares, on the last day of the company's accounting year

c is the net income of the company for the company's accounting year.

The company may have distributed dividends to the borrower in the same year. If so, these dividends are subtracted from the income attributed by the formula above. This avoids counting the income twice.

Payments from trusts, not being beneficiary income, when the borrower is not the settlor (clause 15)

Under the new rules, payments from trusts to a borrower are included as income for student loan repayment purposes in the income year in which the distribution is made where:

- the distribution is not beneficiary income in relation to the borrower, and
- the borrower is not the settlor of the trust.

The Commissioner has discretion to determine whether certain trust distributions should not be included as income for student loan purposes.

INFORMATION-MATCHING WITH NEW ZEALAND CUSTOMS SERVICE FOR BORROWERS IN SERIOUS DEFAULT

Section 208 of the Student Loan Scheme Act 2011, sections 280G, 280H and 280I of the Customs and Excise Act 1996, and section 103 of the Privacy Act 1993

The current information match between Inland Revenue and the New Zealand Customs Service ("Customs") for child support has been extended to include contact information for borrowers who are in "serious default" on their student loan obligations when they enter or leave New Zealand.

Background

A key impediment to collecting repayments from overseas-based borrowers is a lack of up-to-date contact details which prevents Inland Revenue from engaging with this group.

The information-match with Customs will enable certain borrowers who are in "serious default" on their student loan obligations to be identified by the Customs' system immediately upon their arrival or departure from New Zealand. Customs will then be able to quickly transfer to Inland Revenue any contact details obtained from the borrower.

Key features

The existing child support alerts match used by Inland Revenue and Customs has been extended to include student loan borrowers in "serious default". Inland Revenue will send Customs the names, date of birth and IRD number of borrowers who are in serious default.

Customs will then match this list against the names and birthdates of people crossing the border and transfer any contact details obtained from the borrower to Inland Revenue.

Extending the information-match will enable Inland Revenue to initiate contact with selected student loan borrowers in a more timely manner to discuss their situation and payment of outstanding arrears.

Application date

The amendments apply from the day after Royal assent, being 30 March 2013.

Detailed analysis

Section 208 has been amended to allow the exchange of information between Inland Revenue and Customs to assist the Commissioner to locate borrowers, who are in "serious default" on their student loan obligations when they enter or leave New Zealand.

"Serious default" is defined by section 280G of the Customs and Excise Act 1996 to mean having an unpaid amount due and owing, and satisfying criteria established in a manner determined by the Commissioner.

Sections 280H and 280I of the Customs and Excise Act 1996 have been amended to provide for information-matching between Customs and Inland Revenue to allow Inland Revenue to receive arrival and departure information for select borrowers in "serious default".

Section 103(1C) of the Privacy Act 1993 has been amended so Inland Revenue can take immediate action to contact student loan borrowers and recover unpaid amounts owed if they are identified as in "serious default".

ALIGNING THE END-OF-YEAR REPAYMENT OBLIGATION THRESHOLD

Sections 4, 31, 32, 54, 72 to 87, sections 88 to 100 (repealed), 115, 119, 157, 190, 191, 195, 202, schedule 3 (repealed), and schedule 4, schedule 6 clause 14, section 3 of the Tax Administration Act 1994, and section 123 of the Accident Compensation Act 2011

New Section 72 extends the $1,500 threshold that applies to borrowers with income from sources such as interest and dividends to borrowers who derive income such as self-employment and rental income. All borrowers with non-salary and wage income will now have an end-of-year repayment obligation if that income is $1,500 or more, and their total income (including salary and wages) is $1,500 or more over the annual repayment threshold (currently $19,084). This ensures that borrowers have the same repayment obligation regardless of the source of their income.

As separate rules are no longer required for the different types of non-salary and wage income, sections 88 to 100 (subpart 3 of Part 2) have been repealed and schedules 3 and 4 (relating to the application of provisional tax rules) have been amalgamated into a single schedule, schedule 4.

As a consequence of these changes, various definitions and references have also been amended.

Application date

The amendments apply retrospectively from 1 April 2012, for the 2012–13 and later tax years.

LOSSES AND PRE-TAXED INCOME

Section 73

The amendments in section 73(5) delay the application of measures that ensure borrowers cannot offset a loss from pre-taxed income (such as interest and dividends) when calculating their repayment obligations.

Application date

The amendments apply retrospectively from 1 April 2012, for the 2012–13 and 2013–14 tax years. The delayed measures will now apply from 1 April 2014 for the 2014–15 and later tax years.

WHEN END-OF-YEAR REPAYMENT OBLIGATIONS ARE DUE

Sections 4, 5, 80, 81 and 144

Sections 80 and 81 have been replaced to ensure that end-of-year repayment obligations continue to be due as one "terminal payment" on the borrower's terminal tax due date (generally 7 February for borrowers with a March balance date) instead of spread over multiple "remaining repayments" as originally provided for in the Student Loan Scheme Act 2011.

As a consequence section 144(1) has also been amended.

Application date

The amendments apply retrospectively from 1 April 2012, for the 2012–13 and later tax years.

NOTIFYING BORROWERS OF EXCESS REPAYMENTS

Sections 72, 76A, 120 and 132

The amendments in section 120 remove the requirement to notify borrowers of excess repayments if they are predominately a salary and wage earner or an overseas-based borrower. Borrowers in these situations knowingly make excess payments through voluntary payments or deductions and therefore do not need to be advised that they have made excess repayments.

Only borrowers who have an end-of-year repayment obligation assessment will be notified of excess repayments they have made. Repayment obligations for these borrowers are confirmed at the end of the tax year when their actual income is known and can sometimes be less than the interim payments originally required during the year.

The amendment in section 132 retains the ability for borrowers to request a refund of excess repayments. However a request must be made within six months or the later of:

- the date on which a borrower is notified of their end-of-year repayment obligation and excess repayment
- the day after the end of the tax year the excess repayment was made or
- the day after the due date of the final instalment of a borrowers overseas-based repayment obligation for a tax year.

Amendments in sections 72(b) and new section 76A also provide that in certain circumstances the Commissioner must assess a borrower's end-of-year repayment obligation as zero and notify the borrower of any excess repayments made. This provides a borrower six months from when the notification was made to request a refund. These circumstances can occur when a borrower was required to make interim payments or issued a default assessment of an end-of-year repayment obligation and upon confirmation of the borrower's actual income for the tax year there is no obligation for the year (eg, their non-salary and wage income is less than the $1,500 threshold).

Application date

The amendments in sections 72 and 76A apply retrospectively from 1 April 2012, for the 2012–13 and later tax years. The amendments in sections 120 and 132 apply from the day after Royal assent, being 30 March 2013.

LATE FILING PENALTIES FOR WORLDWIDE INCOME DECLARATIONS

Sections 155 and 157

Sections 155 and 157 have been amended to repeal the late filing penalty for borrowers who do not provide a declaration of their worldwide income. Borrowers required to file a declaration of their worldwide income have been given an exemption from being treated as overseas-based. These borrowers may have their exemption revoked if they do not meet their filing requirements. This acts as a deterrent for not filing as borrowers would lose their interest-free status.

The amendments apply retrospectively from 1 April 2012, for the 2012–13 and later tax years.

RETAINING THE CURRENT PENALTY INTEREST RULES ON UNPAID AMOUNTS

Sections 2, 139, 141, 221 (repealed), schedule 7 (repealed) and sections 2 and 57 (repealed) of the Student Loan Scheme Amendment Act 2012

Changes to the late payment interest regime due to come into force on 1 April 2013 have been repealed thereby retaining the existing late payment interest rules to:

- charge on the amount outstanding the day after the due date and monthly thereafter
- only charge if each repayment obligation in default is $334 or more, and
- only charge if a borrower fails to make full payment by the final instalment date of the obligation.

Changes have also been made to link the late payment interest rate to the annual loan interest rate. The annual loan interest rate is based on an average of the 10-year government bond rate. Linking late payment interest with the annual interest rate ensures that it reflects current interest rates. The late payment interest rate will now be the annual loan interest rate plus 4% calculated at an equivalent monthly rate. For the 2013–14 tax year, the monthly late payment interest rate reduces from 0.843% to 0.789%.

The late payment interest rate has also been reduced for borrowers who are under agreed instalment arrangements to repay overdue amounts. For each month that a borrower keeps to an instalment arrangement, late payment interest will be charged at the annual loan interest rate plus 2% calculated at an equivalent monthly rate. For the 2013–14 tax year, the monthly reduced late payment interest rate is 0.635%.

Application date

The amendments apply from 1 April 2013.

RE-INSTATEMENT OF THE UNDER $20 OBLIGATION WRITE-OFF

Section 144

The treatment of writing off small repayment obligation amounts previously provided under the Student Loan Scheme Act 1992 has been re-instated. Section 144 has been amended so that an amount of a repayment obligation (or part of a repayment obligation) of less than $20 that the Commissioner has refrained from collecting will be written-off rather than remaining part of the borrower's loan balance.

Application date

The amendments apply retrospectively from 1 April 2012, for the 2012–13 and later tax years.

RE-INSTATEMENT OF THE UNDERESTIMATION PENALTY

Sections 4, 5 and 161A

The underestimation penalty that applied under the Student Loan Scheme Act 1992 has been re-instated. As the existing late payment interest rules are retained, late payment interest will only be charged if full payment of a borrower's interim payments is not made by the final interim payment due date for the tax year. Re-instating the underestimation penalty provides an incentive for borrowers who use the estimation method for calculating their interim payments for a tax year to ensure their estimate is not significantly lower than their actual end-of-year repayment obligation.

Application date

The amendments apply from 1 April 2013.

RETAINING THE CURRENT LOAN INTEREST CALCULATION AND INTEREST-FREE WRITE-OFF

Sections 2, 196, 221 (repealed), schedule 7 (repealed) and sections 2 and 57(repealed) of the Student Loan Scheme Amendment Act 2012

Changes to the way loan interest is calculated, charged, and compounded have been repealed.

The changes were to come into force on 1 April 2013. Repealing these changes thereby retains the existing rules so that loan interest continues to be accrued daily, charged and compounded annually. This also means that loan interest will continue to be charged for all borrowers and the interest-free write-off applied for New Zealand-based borrowers only.

As a consequence of this change, section 196 has been amended to ensure borrowers who repay their loan in full within 30 days of the Commissioner notifying them of their outstanding balance continue to receive the previous treatment of writing off loan interest that has accrued from the date of notification to the date the loan is repaid.

Application date

The amendments apply from 1 April 2013.

PAYMENT ALLOCATION

Sections 2, 117 (repealed), 194, 221 (repealed), schedule 7 (repealed) and sections 2 and 57 (repealed) of the Student Loan Scheme Amendment Act 2012

Changes to the order in which payments and deductions are allocated to obligations, unpaid amounts, and the loan balance have been repealed.

The changes were to come into force on 1 April 2013. Repealing these changes thereby retains the existing payment allocation rules of offsetting payments and deductions first against any interest charged, and secondly, any remainder against any principal outstanding.

Section 117 has also been repealed to ensure that all compulsory student loan deductions satisfy a borrower's salary and wage repayment obligation on a pay-period basis regardless of whether the borrower is New Zealand-based or overseas-based. Previously, compulsory deductions made from New Zealand salary and wages during the period a borrower was overseas-based could be used to satisfy the borrower's overseas-based borrower repayment obligation.

An amendment to section 194 also ensures that compulsory deductions must not be used to satisfy other repayment obligations, unpaid amounts, or penalties.

Application date

The amendments apply from 1 April 2013.

REPAYMENT OBLIGATIONS FOR FIRST-TIME BORROWERS

Sections 4, 72 and schedule 6, clause 2A

Changes have been made so that students who become a "new borrower" in the period from 1 January to 31 March of a tax year will not have an end-of-year student loan assessment for any non-salary and wage income they derive, such as business income, rental income, interest and dividends.

Background

Before 1 January 2012, the annual loan transfer from StudyLink to Inland Revenue occurred in February each year. This was replaced with a near real-time transfer, which allowed StudyLink to transfer loan information to Inland Revenue daily.

This near real-time transfer had an unintended consequence that means a "new borrower" would receive an end-of-year student loan assessment that would not have been issued were it not for the near real-time transfer. In effect, borrowers who have student loans for as little as two or three weeks in a tax year will be sent assessments based on their income for the whole tax year.

The Student Loan Scheme Act 2011 (Transitional Provisions) Regulations 2012 provided relief from repayment obligations for borrowers affected in this way for the 2011–12 tax year. The regulation expires on 1 April 2015.

Key features

Students who become a "new borrower" after 31 December will not have an end-of-year repayment obligation assessment for their non-salary and wage income derived in the tax year they become a borrower. Repayment deductions will continue to be made from the salary and wages of borrowers, but only from the date they first draw down a loan. This will provide similar treatment to that provided under the previous annual loan transfer process.

Relief from repayment obligations provided under the Student Loan Scheme Act 2011 (Transitional Provisions) Regulations 2012 for similarly affected borrowers for the 2011–12 tax year is provided for in the Student Loan Scheme Act 2011 and continues to be available in relation to the 2011–12 tax year assessment after 1 April 2015.

Application date

The amendments relating to the repayment obligation of a "new borrower" applies from 1 April 2012, for the 2012–13 and later tax years.

The amendments relating to continuing the relief provided by transitional regulations for the 2011–12 tax year apply from the day after Royal assent, being 30 March 2013.

Detailed analysis

First-time borrowers who draw down a loan after 31 December

For the 2012–13 and future tax years, students who become a "new borrower" on or after 1 January in a tax year will not be subject to the end-of-year assessment. Borrowers who draw down a loan on or after 1 January will not face an end-of-year repayment obligation for any income that comes from sources *other than* salary and wages, such as business, rental or interest income they earn in that tax year.

New borrowers who draw down loans on or after 1 January will continue, as before the near real-time loan-transfer changes, to have deductions made from any salary and wage income they earn after the first draw-down.

A "new borrower" is defined as:

- a person who becomes a borrower for the first time under the student loan scheme in the period starting on 1 January of the tax year and ending on the close of the last day of the tax year, or
- a person to whom all of the following apply:
  - the person had been a borrower under the student loan scheme before the tax year, and
  - the person fully repaid his or her loan before the start of the tax year, and
  - in the period starting on 1 January of the tax year and ending on the close of the last day of the tax year, the person again became a borrower under the student loan scheme.

Borrowers who draw down a loan before 31 December

Since the start of the student loan scheme in 1992 new borrowers who drew down loans before 31 December generally had their loans transferred to Inland Revenue in the next February transfer. Their end-of-year repayment obligations were assessed on the basis of their income from that tax year, which may have included income earned prior to their borrowing.

As these borrowers are not affected by the earlier transfer of student loans from StudyLink to Inland Revenue, the treatment of these borrowers does not change. They will continue to have an end-of-year repayment obligation for the tax year based on all their non-salary and wage income for that tax year. They will continue to have deductions made from any salary and wage income they earn after the first draw-down.

Continuing relief provided for the 2011–12 tax year

Transitional regulations introduced to address a similar situation for the 2011–12 tax year will expire on 1 April 2015. However to ensure that relief continues to be available for that tax year, the relief from repayment obligations provided under those regulations is now included in schedule 6 so that it continues to be available in relation to assessments for the 2011–12 tax year after 1 April 2015 if necessary.

TRANSITIONAL REGULATIONS

Schedule 6, clause 17

Regulations may be made by Order in Council to remedy unforeseen transitional matters relating to the transition to the changes made by the Student Loan Scheme Amendment Act 2013.

Background

Numerous changes have been made to the Student Loan Scheme Act 2011. Many are very complex, involving changes to amendments made by previous legislation that were not yet in force, the repeal of existing provisions and inter-relationships between provisions that are being amended at different times.

Due to the complexity of the changes, there may be potential for situations to arise, in the course of transitioning to the changes made by the Student Loan Scheme Amendment Act 2013 that are unintended or not provided for.

Providing for transitional regulations similar to those provided under the Student Loan Scheme Act 2011 for the transition from the Student Loan Scheme Act 1992 will enable these situations to be remedied quickly.

Key features

Regulations may be made by Order in Council on the recommendation of the Minister of Revenue for the smooth transition to the changes made to the Student Loan Scheme Act 2011.

Regulations can only be made if the Minister is satisfied that the proposed regulations:

- are reasonably necessary for the purpose of facilitating or ensuring an orderly transition to the changes made by the amendment Act, and
- are consistent with the purposes of the Student Loan Scheme Act 2011.

Any transitional regulations made must be revoked the earlier of:

- 3 years after the date the regulations are made, and
- the close of 31 March 2018.

Transitional regulations may only be made before 1 April 2018.

Application date

The amendments apply from the day after Royal assent, being 30 March 2013 and will be repealed on 1 April 2018.

LEGISLATION AND DETERMINATIONS

This section of the *TIB* covers items such as recent tax legislation and depreciation determinations, livestock values and changes in FBT and GST interest rates.

CPI ADJUSTMENT 13/01 FOR DETERMINATION DET 09/02: STANDARD-COST HOUSEHOLD SERVICE FOR CHILDCARE PROVIDERS

In accordance with the provisions of Determination DET 09/02, as published in *Tax Information Bulletin* Vol 21, No 4 (June 2009), Inland Revenue advises that, for the 2013 income year:

(a) The variable standard-cost component will increase from $3.34 per hour per child to $3.37 per hour per child, and

(b) The administration and record keeping fixed standard-cost component will increase from $326 per annum to $329 per annum, for a full 52 weeks of childcare services provided.

The above amounts have been adjusted in accordance with the annual movement of the Consumers Price Index for the twelve months to March 2013, which showed an increase of 0.9%. For childcare providers who have a standard 31 March balance date, the new amounts apply for the period from 1 April 2012 to 31 March 2013.

CPI ADJUSTMENT 13/02 FOR DETERMINATION DET 05/03: STANDARD-COST HOUSEHOLD SERVICE FOR BOARDING SERVICE PROVIDERS

In accordance with the provisions of Determination DET 05/03, as published in *Tax Information Bulletin* Vol 17, No 10 (December 2005), Inland Revenue advises that the weekly standard-cost component for the 2013 income year, is retrospectively adjusted as follows:

(a) The weekly standard-cost for one to two boarders will increase from $247 each to $250 each.

(b) The weekly standard-cost for third and subsequent number of boarders will increase from $202 each to $204 each.

The above amounts have been adjusted in accordance with the annual movement of the Consumers Price Index for the twelve months to March 2013, which showed an increase of 0.9%. For boarding service providers who have a standard 31 March balance date, the new amounts apply for the period from 1 April 2012 to 31 March 2013.

NATIONAL AVERAGE MARKET VALUES OF SPECIFIED LIVESTOCK DETERMINATION 2013

This determination may be cited as "The National Average Market Values of Specified Livestock Determination, 2013".

This determination is made in terms of section EC 15 of the Income Tax Act 2007 and shall apply to specified livestock on hand at the end of the 2012–13 income year.

For the purposes of section EC 15 of the Income Tax Act 2007 the national average market values of specified livestock, for the 2012–13 income year, are as set out in the following table.

National average market values of specified livestock

Type of Livestock	Classes of Livestock	Average Market Value per Head $
Sheep	Ewe hoggets	78.00
	Ram and wether hoggets	69.00
	Two-tooth ewes	121.00
	Mixed-age ewes (rising three-year and four-year old ewes)	102.00
	Rising five-year and older ewes	82.00
	Mixed-age wethers	63.00
	Breeding rams	273.00
Beef cattle	*Beef breeds and beef crosses:*	
	Rising one-year heifers	456.00
	Rising two-year heifers	724.00
	Mixed-age cows	872.00
	Rising one-year steers and bulls	546.00
	Rising two-year steers and bulls	837.00
	Rising three-year and older steers and bulls	1,048.00
	Breeding bulls	2,098.00
Dairy cattle	*Friesian and related breeds:*	
	Rising one-year heifers	892.00
	Rising two-year heifers	1,560.00
	Mixed-age cows	1,873.00
	Rising one-year steers and bulls	442.00
	Rising two-year steers and bulls	736.00
	Rising three-year and older steers and bulls	1,007.00
	Breeding bulls	1,337.00
	Jersey and other dairy cattle:	
	Rising one-year heifers	668.00
	Rising two-year heifers	1,343.00
	Mixed-age cows	1,627.00
	Rising one-year steers and bulls	342.00
	Rising two-year and older steers and bulls	597.00
	Breeding bulls	1,091.00
Deer	*Red deer:*	
	Rising one-year hinds	188.00
	Rising two-year hinds	369.00
	Mixed-age hinds	416.00
	Rising one-year stags	235.00
	Rising two-year and older stags (non-breeding)	414.00
	Breeding stags	1,298.00

Type of Livestock	Classes of Livestock	Average Market Value per Head $
Deer *(continued)*	*Wapiti, elk, and related crossbreeds:*	
	Rising one-year hinds	227.00
	Rising two-year hinds	409.00
	Mixed-age hinds	585.00
	Rising one-year stags	286.00
	Rising two-year and older stags (non-breeding)	464.00
	Breeding stags	1,492.00
	Other breeds:	
	Rising one-year hinds	97.00
	Rising two-year hinds	189.00
	Mixed-age hinds	214.00
	Rising one-year stags	127.00
	Rising two-year and older stags (non-breeding)	223.00
	Breeding stags	608.00
Goats	*Angora and angora crosses (mohair producing):*	
	Rising one-year does	68.00
	Mixed-age does	90.00
	Rising one-year bucks (non-breeding)/wethers	49.00
	Bucks (non-breeding)/wethers over one year	60.00
	Breeding bucks	318.00
	Other fibre and meat producing goats (Cashmere or Cashgora producing):	
	Rising one-year does	64.00
	Mixed-age does	93.00
	Rising one-year bucks (non-breeding)/wethers	51.00
	Bucks (non-breeding)/wethers over one year	62.00
	Breeding bucks	311.00
	Milking (dairy) goats:	
	Rising one-year does	500.00
	Does over one year	620.00
	Breeding bucks	300.00
	Other dairy goats	20.00
Pigs	Breeding sows less than one year of age	189.00
	Breeding sows over one year of age	255.00
	Breeding boars	344.00
	Weaners less than 10 weeks of age (excluding sucklings)	68.00
	Growing pigs 10 to 17 weeks of age (porkers and baconers)	133.00
	Growing pigs over 17 weeks of age (baconers)	196.00

This determination is signed by me on the 14th day of May 2013.

Rob Wells

LTS Manager Technical Standards

QUESTIONS WE'VE BEEN ASKED

This section of the *TIB* sets out the answers to some day-to-day questions people have asked. They are published here as they may be of general interest to readers.

QB 13/01: DEPRECIATION OF COMMERCIAL FIT-OUT

Question

Following changes in the depreciation rules for buildings, the Commissioner has been asked whether a taxpayer can re-characterise a part of a commercial building into components of commercial fit-out in order to claim depreciation on those items when those items had not been identified as separate depreciable property at the time the taxpayer acquired the property.

Answer

The Commissioner considers that in circumstances where taxpayers have depreciated items of commercial fit-out that were acquired with a building, as part of that building, section DB 65 of the Income Tax Act 2007 sets out the way these items of commercial fit-out may continue to be depreciated. Because of this it is not possible to re-characterise part of a commercial building into components of commercial fit-out.

In circumstances where taxpayers have at all times depreciated items of commercial fit-out that was acquired with a building separately from the building, these items of commercial fit-out may continue to be depreciated using the most appropriate rate for the items. Where these separately identified items of commercial fit-out have historically not been depreciated using the depreciation rate most appropriate to that item, the Commissioner will consider amending the appropriate assessments, using the criteria set out in the standard practice statement ("SPS") 07/03: *Requests to amend assessments.*

Explanation

Background

With effect from the 2011–12 income year the depreciation rate for buildings with an estimated useful life of 50 years or more has been set at 0%. The 0% rate applies to all buildings regardless of when they were acquired. The definition of "building" was amended and a definition of "commercial fit-out" was introduced to clarify that commercial fit-out would continue to be depreciable.

In the past some commercial building owners had not been depreciating the building fit-out components separately from the building. That is, the building and the fit-out has been identified as a single asset at the time of acquisition and depreciation deductions have been claimed based on the total cost of the building, without any fit-out costs being separately identified. For these taxpayers, because the depreciation rate for buildings is reduced to 0%, this rate would also apply to any fit-out that has been treated as part of the building.

Inland Revenue has recently received enquiries from taxpayers seeking to retrospectively re-characterise a part of the building into various items of commercial fit-out in order to claim depreciation deductions on those items. Any retrospective re-characterisation and depreciation of fit-out would require the Commissioner to exercise her discretion under section 113 of the Tax Administration Act 1994 to adjust the depreciation deductions in previous assessments.

Section DB 65 of the Income Tax Act 2007 to be applied in these circumstances

In order to claim a depreciation deduction on an item of depreciable property, a taxpayer is required to identify what the depreciable property is. In their issues paper *Post-budget depreciation issues* of December 2010, officials noted that for a commercial building, a taxpayer may have chosen to identify and depreciate the building as one single item of depreciable property and that this was likely to have occurred where taxpayers had sought to minimise tax compliance costs. Alternatively, they may have identified items of fit-out and depreciated those items separately from the cost of the building.

To acknowledge that some taxpayers may not have separately identified items of commercial fit-out, section DB 65 of the Income Tax Act 2007 was enacted as a transitional rule so that these taxpayers can depreciate a commercial fit-out, despite not having done so separately in the past.

Section DB 65 sets specific limits for dealing with "commercial fit-out", which is a widely defined term extending to any non-structural item "attached to a building". The issues paper acknowledges that where an item of commercial fit-out has been acquired at the same time as the building and has always been depreciated as part of the commercial building, there may have been other ways in which taxpayers could separate out commercial fit-out from the cost of the building. However, the issues paper makes it clear that instead of allowing this to be done section DB 65 sets out the only way in which these items may now continue to be depreciated.

Section DB 65 allows a taxpayer to depreciate a portion of the building's tax book value as a pool of fit-out. This new deduction provision permits an annual deduction based on a one-off adjustment calculation that is available from the 2011–12 income year.

To qualify for the section DB 65 allowance, the following must apply:

- the taxpayer owns a commercial building that has a depreciation rate of 0% (ie, the building has an estimated useful life of 50 years or more)
- the building was acquired in the 2010–11 or earlier income year
- the building was depreciated in the 2010–11 income year and the building has not been disposed of since, and
- the commercial fit-out was not separately depreciated if the fit-out was acquired at the same time as the building.

The starting pool is 15% of the building's adjusted tax value as at the end of the 2010–11 income year. This starting pool is reduced by the adjusted tax value of all items of commercial fit-out that had been separately depreciated (ie, the items of commercial fit-out that were acquired after the building was acquired, or items of commercial fit-out acquired as part of the building where the taxpayer has chosen to treat these as separate items of depreciable property). The starting pool is depreciated at a rate of 2% in the 2011–12 and later income years.

No loss or recovery rules apply to the value of the pool when the building or fit-out is disposed of.

A practical example of how section DB 65 is applied was provided in the *Tax Information Bulletin* Vol 23, No 1 (February 2011) "Clarifying that certain building fit-out is depreciable property". The example is reproduced here:

> *Company ABC acquired a warehouse on 1 April 1999 for $1 million. Items of commercial fit-out within the building were not separately identified and depreciated at the time the building was acquired. Twelve months later a refurbishment of the warehouse was completed. The refurbishment was itemised and depreciation was applied to the various items of commercial fit-out.*
>
> *At the end of the 2010–11 income year the adjusted tax book value of the warehouse is $640,000 and the adjusted tax book value of the associated commercial fit-out is $64,000.*
>
> *The starting pool value is:*
>
> - *(15% × 640,000) – 64,000 = $32,000*
>
> *The annual deduction, assuming that the building is held for the 2011–12 income year is:*
>
> - *$32,000 × 2% × 12/12 = $640.*

Treatment of separately depreciated commercial fit-out

As stated previously, the owner of a commercial building can identify items of fit-out and depreciate those items separately from the cost of the building. In this circumstance commercial building owners have the option of depreciating various items of building fit-out under the asset category "Building fit-out (When in books separately from building cost)" in the Commissioner's Table of Depreciation Rates. This asset category lists the rates and the items in a building that are commonly found in a commercial building.

Section DB 65 does not apply in circumstances where commercial fit-out has always been depreciated separately from the building and taxpayers are therefore able to continue to depreciate building fit-out separately using the most appropriate depreciation rate for that fit-out. Where a taxpayer has previously used an incorrect depreciation rate or asset class to depreciate commercial fit-out that taxpayer is able to request that the Commissioner's discretion under section 113 be exercised to issue an amended assessment that corrects the error.

In exercising this discretion, the Commissioner will follow the criteria set out in SPS 07/03 *Requests to amend assessments*. This states that the Commissioner's discretion will only be exercised to correct genuine errors. With respect to the depreciation of separately identified commercial fit-out, the Commissioner accepts that a genuine error will have occurred when a taxpayer has not used the most appropriate depreciation rate or asset class for that fit-out.

By contrast, if taxpayers choose to take particular tax positions under tax laws where legitimate alternatives had been available and later regret that choice, no error has occurred and the Commissioner's discretion will not be exercised.

Voluntary disclosure

Taxpayers who have filed a tax return that incorrectly re-characterises a commercial building into components of commercial fit-out, after the building has been depreciated as one single asset previously, should make a voluntary disclosure to the Commissioner and new assessments will be issued.

ITEMS OF INTEREST

2013 REVIEW OF THE COMMISSIONER'S MOTOR VEHICLE MILEAGE RATE DELAYED

Operational Statement OS 09/01 published in the *Tax Information Bulletin* Vol 21, No 3 (May 2009) provides the Commissioner's statement of a mileage rate for expenditure incurred for the business use of a motor vehicle. OS 09/01 can viewed at the Inland Revenue website **www.ird.govt.nz/technical-tax/op-statements/**

Inland Revenue undertakes a review of the mileage rate at least once a year. That review relies on data setting out the costs of owning and operating a motor vehicle which is supplied to us by an independent organisation. Unfortunately we have been advised there will be a delay in providing the information for the 2013 income year. As a result, the 2013 review has been delayed and we expect to be able to provide the Commissioner's mileage rate for the 2013 income year in early July.

Taxpayers who are required to file a tax return in the meantime should use the current (2012) mileage rate of 77 cents per kilometre (applicable to both petrol and diesel fuel vehicles) to calculate their motor vehicle running costs for completion of their 2013 income tax return.

Employers may continue to use the 2012 mileage rate as a reasonable estimate of motor vehicle expenditure when reimbursing employees.

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, Court of Appeal, Privy Council and the Supreme Court.

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.

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.

SUMMARY JUDGEMENT APPLICATION

Case	Peter William Mawhinney v Commissioner of Inland Revenue
Decision date	4 April 2013
Act(s)	High Court Rules, Goods and Services Tax Act 1985
Keywords	Summary Judgment, High Court Rules Part 12, GST refunds, section 46 of the GST Act

Summary

The plaintiff made a summary judgment application which was unsuccessful on the grounds that the Commissioner has an arguable defence to both of the plaintiff's arguments.

Impact of Decision

Reiterates the position that summary judgment applications will not be successful when the defendant has an arguable defence.

Facts

This is a summary judgment application by Mr Mawhinney as trustee of the Forest Trust.

The plaintiff contends that the Commissioner has omitted to pay $594,210.48 in respect of Goods and Service Tax ("GST") refunds for the GST periods ended 31 May 2009 to 31 December 2011 (inclusive). The Commissioner has withheld payment under section 46 of the Goods and Services Tax Act 1985 ("the GST Act") while the returns are investigated. Mr Mawhinney argues that the refunds are payable as the Commissioner is relevantly satisfied that the returns are in order; and alternatively that the refund is payable because the Commissioner did not initiate an investigation within 15 working days of receiving the information requested under section 46(4) of the GST Act.

Decision

For his first argument, Mr Mawhinney says that the Commissioner is satisfied as a result of sending the taxpayer two letters. The first letter dated 2 May 2012, enclosed documents called "Notice of assessment for the Forest Trust" and sets out how the GST for each period from 31 May 2009 to 29 February 2012 has been treated. The second letter dated 20 June 2012 also enclosed documents but this time headed up "Acknowledgement of return for the Forest Trust". Apart from the change in title, they were similar to the documents sent with the letter of 2 May 2012.

Mr Mawhinney says that these documents are "assessments" under the Tax Administration Act 1994 and represent decisions made by the Commissioner under section 46(1)(b) of the GST Act that she is "relevantly satisfied" with the trust's GST returns.

The Commissioner refers to the self-assessment system for GST, when taxpayers lodge tax returns they self-assess their tax liability. The Commissioner admits that it was confusing that the documents attached to the 2 May 2012 letter were headed "notice of assessment". However, the Commissioner explains that the documents were generated to address a complaint made to Inland Revenue by Mr Mawhinney. The second letter dated 20 June 2012 notified the plaintiff of the errors in the documents and issued amended versions. The Commissioner submits that on the basis of that evidence, the documents were no more than responses to the taxpayer's requests for information about the GST returns and the label put on the documents is not decisive.

The Court accepted that the Commissioner had an arguable defence that these documents were not assessments and went on to note at [41]:

> Mr Mawhinney's argument does not just turn on whether there were assessments. His claim is that the Commissioner was relevantly satisfied under section 46(1)(b) of the GST Act. For this decision, I assume that the Commissioner may be relevantly satisfied under that section and communicate his satisfaction without making an assessment or giving a notice of assessment as those terms are used in the tax

> legislation. Mr Mawhinney's reliance on the assessment provisions of the Tax Administration Act is not essential to his argument.

The Court concluded that the case law in *Paul Finance Ltd v Commissioner of Inland Revenue* (1995) 17 NZTC 12,379 (CA) and *Contract Pacific Ltd v Commissioner of Inland Revenue* (1995) 17 NZTC 12,379 (CA) go towards the Commissioner's defence that the documents are not evidence that she had made assessments and therefore, the Court cannot say that the defence is hopeless.

The second argument run by Mr Mawhinney focuses on section 46 of the GST Act. In particular, the Commissioner's request for information, the provision of that information by Mr Mawhinney and the absence of any notification of an investigation or communication within 15 days by the Commissioner of Mr Mawhinney providing that evidence.

The Court recognised in *Contract Pacific Ltd v Commissioner of Inland Revenue* that there are only two occasions when the Commissioner must refund. Neither of those situations applies here. The Court again concluded that the Commissioner has an arguable defence in regards to the interpretation of section 46 of the GST Act.

ABUSIVE TAX POSITION TAKEN WHEN MAKING A FAMILY ASSISTANCE CLAIM

Case	TRA 18/11
Decision date	27 March 2013
Act(s)	Income Tax Act 2004, Tax Administration Act 1994
Keywords	Abusive tax position, accountancy practice, artificially low salary from company, family trust, viewed objectively, dominant purpose, tax avoidance, family assistance

Summary

The disputant accepted a re-assessment by the Commissioner of her family support entitlement because her husband was paid an artificially low salary. The family had also received the benefit of distributions from a family trust which was a shareholder in the company her husband worked for. The disputant argued that the Commissioner had not challenged her husband's tax position and accordingly, she could not be held to have taken an abusive tax position.

The Taxation Review Authority found that the dominant purpose of the arrangement was to obtain family assistance the disputant was not otherwise entitled to.

Impact of Decision

This judgment makes it clear that where a party enters into an arrangement with another party that creates a favourable tax position for both by reducing the income of the second party and allowing the first party to claim family assistance, the Commissioner can challenge the first party's tax position directly under section GC 28 of the Income Tax Act 2004 (the Act), even though they have not challenged the second party's income under general anti-avoidance provisions.

Facts

The disputant, who had nil income, began claiming family assistance based on her husband's income following the birth of her first child.

The disputant and her husband were trustees of a family trust which held shares in two companies, one of which was an accounting practice. The husband was the settlor, sole appointee and primary beneficiary of the trust and worked for one of the companies, with his salary paid through the other. The husband's salary was artificially low.

The disputant and her husband moved funds from the accountancy practice to the family trust and used those funds for family expenses.

The Commissioner reduced the disputant's claim for family assistance for the 2006 to 2008 income years (inclusive) and imposed an abusive tax position shortfall penalty in relation to the 2007 income year. The disputant initially challenged the Commissioner's tax assessments. This challenge was subsequently withdrawn. This proceeding solely concerned the imposition of an abusive tax position shortfall penalty.

Decision

Sinclair J found that an abusive tax position shortfall penalty will apply if (at [14]):

(a) a tax shortfall arises from the disputant's tax position

(b) the disputant took a tax position which is an unacceptable tax position

(c) viewed objectively the disputant took a tax position in respect of or as a consequence of an arrangement that is entered into with a dominant purpose of avoiding tax, whether directly or indirectly, and

(d) The resulting tax shortfall exceeds $20,000.

It was found on the facts that the requirements in paragraphs (a) and (d) above were satisfied.

The focus of the inquiry was on the application of section GC 28 of the Act which allowed the Commissioner to decrease the tax credits a person was entitled to where they had entered into an arrangement with another person to give a more favourable effect.

The disputant claimed section GC 28 of the Act did not apply. She claimed that her reliance on the income of her husband to claim family assistance was not an abusive tax position to take, because the Commissioner had not challenged the husband's income.

Sinclair J found that the disputant had taken an unacceptable tax position. She did not accept that the interpretation adopted by the disputant was "about as likely as not to be correct". Sinclair J made it clear that for the Commissioner to rely on the specific avoidance provision in section GC 28 of the Act, she does not first have to attack the taxable income of another party to the arrangement under the general anti-avoidance provisions.

Sinclair J found that when viewed objectively, the dominant purpose of the arrangement was to obtain family assistance that the disputant was not otherwise entitled to. She did not accept that there were any commercial reasons (other than tax) for the arrangement.

Sinclair J found that the disputant had not satisfied the onus of proof that the Commissioner's assessment was wrong and to what extent. She found that the disputant was liable for an abusive tax position shortfall penalty for the 2007 income year.

CHILD SUPPORT PRIMARY OBLIGATION IS CHILDREN

Case	D v B & Commissioner of Inland Revenue
Decision date	12 April 2013
Act(s)	Child Support Act 1991
Keywords	Retrospective departure order, true financial resources and ability of liable parent

Summary

The mother successfully applied for a retrospective child support departure order in the Family Court. The High Court overturned the quantum of the departure order and the mother appealed to the Court of Appeal. The Court of Appeal found that the liable parent's primary obligation was to support his children and, after ascertaining the father's true financial ability and resources overturned the High Court's finding on quantum. The Court of Appeal left open whether a departure order could be made retrospectively, although it did substitute a retrospective departure order here.

Impact of Decision

The Court of Appeal did not express a view whether a departure order may be made retrospectively and left it open that the Court may be called upon to address the issue in a future case.

The Court set out helpful guidance on identifying a liable parent's true financial ability and resources and affirmed that the liable parent's primary obligation is to support their children.

Facts

Ms D (the mother and custodial parent) and Mr B (the father and liable parent) were married, had three children and subsequently separated in 1996.

Following the separation, Mr B established a trust, transferred his business to the trust along with the majority of his other assets, including his house. Mr B paid himself a reduced salary whilst the profits of the business were paid to the trust as dividends. Mr B had access to the funds in the trust as the trust was indebted to him. Also, Mr B effectively used the business as his bank account, obtaining advances from the business and then repaying them, recorded in the "Director's loan account".

Ms D applied to the Family Court for a departure order and the Family Court held that the primary purpose of the company and trust structures was to avoid a higher child support liability. The Family Court ordered retrospectively an increase in the child support payable by Mr B to Ms D and awarded Ms D $297,300.94 ($146,676 plus $150,624.94 interest).

Mr B appealed to the High Court which found that there was jurisdiction to award retrospective child support but set aside the Family Court order and awarded Ms D $29,538 ($15,442 plus $14,096 interest).

The Commissioner had intervened in the High Court on the issue of retrospectivity.

Ms D appealed to the Court of Appeal. The Commissioner remained a party to the appeal but only took an interest in whether a departure order could be made retrospectively. The Commissioner did not make any submissions on the substantive issue of the amount of child support payable under the departure order.

Decision

On the issue of retrospectivity, both Ms D and Mr B agreed in the Court of Appeal that a departure order under the Child Support Act 1991 ("the CSA") could be made retrospectively.

As it was no longer an issue in the appeal, the Court of Appeal declined to express any views on it:

> [25] Fogarty J's finding that there is jurisdiction to award retrospective child support is not challenged on this appeal. It is therefore both unnecessary and inappropriate for this Court to express a view.
>
> …
>
> [27] We have set out this summary because, as Ms Deligiannis noted, there is an equally balanced difference of opinion in the High Court on the retrospectivity issue. This Court may therefore be called upon in some future case to resolve that difference and decide the issue.

The Court did, however, in allowing the appeal, order that a retrospective departure order be substituted at [108].

On the substantive issue whether to grant a departure order, the Court confirmed sections 105(4)(d) and (5)(a) of the CSA empower a court to ascertain the "true financial ability and resources of the parent of a child" and this includes the "ability to go behind or … to 'look through' company, trust and other structures" at [55].

A court's task is to "identify what financial resources, additional to the salary the father received from [the business], which he had available to pay child support". Repayment of the father's loan account (to the business) was an improvement in his asset position and was relevant to the Court's task. Further, something which is unable to be taken into account in a formula assessment, "such as the use of a car or interest free loans", can be taken into account on a departure order.

The Court of Appeal held the following were to be added to Mr B's income for the first period 1997 to 2003 (inclusive):

1. The difference between the open and closing balance of the "Director's loan account" with the business, $71,855
2. The agreed vehicle expenses and interest charged, $57,398
3. Further advances to/drawings by Mr B, $89,750.

These were to be spread equally over the seven years, increasing Mr B's income available for the assessment of child support by $31,286 for each year.

For the second period, 2004 to 2010 (inclusive), the position is different because the drop in Mr B's income was due to his embarking on a large software development. The issue was whether and to what extent Mr B was entitled to decide to embark on this development to the detriment of his ability to make child support payments.

The Court of Appeal was attracted to the submission that Mr B took an "involuntary grant" from Ms D when Mr B embarked on the development because by paying less child support he could undertake it whilst not expecting to share any of the gains with Ms D. The Court's four main reasons for such analysis are:

1. "It factors in what the father rather overlooked when he embarked on the software development project: that his primary obligation was to support his children" [88].
2. It is consistent with section 105 of the CSA and what is just and equitable between the parties and the children.
3. The evidence that the work Mr Bevis undertook for the software development would have commanded a salary of $100,000 per annum, whilst not the single basis for fixing the child support, was relevant to his "earning capacity" in terms of section 105(4)(d) of the CSA.
4. It appropriately reflects that it is a retrospective departure order being made. As an "involuntary investor" in the project, Ms D should enjoy the returns from the project in the form of, retrospectively, proper child support.

The Court of Appeal reinstated the Family Court order that Mr B pay the maximum child support for the years 2004 to 2010 (inclusive).

The Court of Appeal ordered interest and reserved leave to apply to the Family Court for supplementary orders dealing with enforcement should there be difficulty enforcing the retrospective departure order.

The Court of Appeal subsequently declined an application to redact the names of the parties from published reports of the judgment, finding that it is neither necessary nor appropriate and the children, now all adults, are not identified in the judgment.

REGULAR CONTRIBUTORS TO THE TIB

Office of the Chief Tax Counsel

The Office of the Chief Tax Counsel (OCTC) produces a number of statements and rulings, such as interpretation statements, binding public rulings and determinations, aimed at explaining how tax law affects taxpayers and their agents. The OCTC also contributes to the "Questions we've been asked" and "Your opportunity to comment" sections where taxpayers and their agents can comment on proposed statements and rulings.

Legal and Technical Services

Legal and Technical Services contribute the standard practice statements which describe how the Commissioner of Inland Revenue will exercise a statutory discretion or deal with practical operational issues arising out of the administration of the Inland Revenue Acts. They also produce determinations on standard costs and amortisation or depreciation rates for fixed life property used to produce income, as well as other statements on operational practice related to topical tax matters.

Legal and Technical Services also contribute to the "Your opportunity to comment" section.

Policy Advice Division

The Policy Advice Division advises the government on all aspects of tax policy and on social policy measures that interact with the tax system. They contribute information about new legislation and policy issues as well as Orders in Council.

Litigation Management

Litigation Management manages all disputed tax litigation and associated challenges to Inland Revenue's investigative and assessment process including declaratory judgment and judicial review litigation. They contribute the legal decisions and case notes on recent tax decisions made by the Taxation Review Authority and the courts.

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