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Tax Alert

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Let's get fiscal: Tax and the 2023 Election

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Let's get fiscal: Tax and the 2023 Election

By Viola Trnski and Robyn Walker

In the world of tax, 2023 has been an eventful year.

We kicked off with flood-related tax relief and FBT e-bike exemptions, before steering towards a debate around how much tax the wealthy pay, and more recently, whether chopped coriander or pre-cut frozen potato chips will fall within Labour's proposed GST exemption.

Cost of living, inflation, and the economy remain front of mind for many New Zealanders, and tax ties into all of these issues by raising revenue, redistributing wealth, and incentivising behaviour. Now, with less than six weeks to go before New Zealanders vote on their next government, the major political players have released their tax policies – and there's a lot on the (tax) table.

Income

Labour will maintain the current income tax brackets, while National will adjust the brackets to account for inflation (which has not been done since 2010).

There is bipartisan support for increasing the In-Work Tax Credit by $25 per week, and the Working for Families abatement threshold to $50,000 in 2026, with both Labour and National announcing these changes. National proposes introducing a 25% childcare rebate for households earning under $180,000 – but will scrap Labour's 20 hours of free ECE for two-year-olds, alongside free prescriptions and public transport subsidies.

ACT supports a two-rate system being phased in while the Greens propose a $10,000 tax-free threshold and a new 45% tax rate for personal income exceeding $180,000.

Proposed income tax brackets and rates (per $ amount)

<table>
<tr><th>Labour</th><th>National</th><th>Greens[2]</th><th>ACT[1]</th><th>Te Pāti Māori[2]</th><th>NZ First</th><th>TOP</th></tr>
<tr><td>0-14k
10.5%</td><td>0-15.6k
10.5%</td><td>0-10k
0%</td><td>0-70k
17.5%</td><td>0-30k
0%</td><td>0-15.6k
10.5%</td><td>0-15k
0%</td></tr>
<tr><td>14k-48k
17.5%</td><td>15.6k-53.5k
17.5%</td><td>10k-50k
17%</td><td>70k-180k
33%</td><td>30k-60k
15%</td><td>15.6k-53.5k
17.5%</td><td>15k-80k
20%</td></tr>
<tr><td>48k-70k
30%</td><td>53.5k-78.1k
30%</td><td>50k-75k
30%</td><td>180k +
39%</td><td>60k-90k
33%</td><td>53.5k-78.1k
30%</td><td>80k-180k
35%</td></tr>
<tr><td>70k-180k
33%</td><td>78.1k-180k
33%</td><td>75k-120k
30%</td><td rowspan="3">2024/25:
0-70k 17.5%
70k + 33%

From 2025:
0-70k 17.5%
70k + 28%</td><td>90k-180k
39%</td><td>78.1k-180k
33%</td><td>180k-250k
42%</td></tr>
<tr><td rowspan="2">180k +
39%</td><td rowspan="2">180k +
39%</td><td>120k-180k
39%</td><td>180k-300k
42%</td><td rowspan="2">180k +
39%</td><td rowspan="2">250k +
45%</td></tr>
<tr><td>180k +
45%</td><td>300k +
48%</td></tr>
</table>

[1] ACT's policy also includes a tax offset of up to $800 for income between $2k-$58k.
[2] Te Pāti Māori and the Greens policies also include a wealth tax.

Earlier this year, Budget documents revealed that a "tax switch" introducing a tax-free threshold coupled with a wealth tax was contemplated by the current Government (ultimately vetoed at the last minute). Despite this, the idea of a tax-free threshold remains popular among minor parties, with the Greens, Te Pāti Māori, and The Opportunities Party (TOP) all advocating for a tax-free threshold of varying amounts.

The Greens and TOP have gone further, with both proposing some form of guaranteed income. The Greens package includes a Guaranteed Minimum Income of $385 per week (and eventually aligning all benefit payments to this amount), while TOP propose a Universal Basic Income of $16,500 annually ($317.31 per week) in the second phase of its two-part plan.

Wealth

The words "wealth tax" continue to circulate as we approach the Election, following the Inland Revenue and Treasury reports in May on how much tax the wealthiest pay (by contrast, its unpopular relative "capital gains tax" has barely been whispered). Te Pāti Māori and the Greens support a wealth tax (and more comprehensive capital gains taxes), while Labour, National, and ACT have all ruled one out.

GST

GST is in the spotlight with Labour's recent election policy of removing GST from fresh and frozen fruit and vegetables.

Te Pāti Māori goes further, with a bid to remove GST from all food, and New Zealand First proposes to remove GST from "basic" food items.

A GST levy on the platform economy (short-stay/visitor accommodation providers, ride-sharing/ride-hailing providers and food/beverage delivery providers who operate through an online marketplace) was legislated in March 2023 to take effect in 2024. National have promised to repeal this if they are elected.

ACT is proposing to share 50% of GST revenue from the construction of new residential dwellings with the consenting local authority in a bid to encourage more infrastructure and houses to be built.

Company, land, and property taxes

Labour, National and ACT have not proposed changes to the company tax rate of 28%. Te Pāti Māori and the Greens want to increase the company tax rate to 33%, while Phase Two of TOP's economic plan increases it to 35% (and also matching income and trust tax rates to 35%).

Both Labour and National will remove depreciation deductions for non-residential buildings.

National has promised to roll back the bright-line test to two years, repeal interest deductibility limitations by 2026, and allow foreign home buyers back into the property market for houses worth more than $2 million, which will be subject to a 15% charge.

TOP are campaigning on a 0.75% per annum Land Value Tax on all urban residential land.

Environmental taxes

Parties differ on whether it's appropriate to tinker with tax to influence environmental behaviour. The Treasury chipped into this issue in April and an argument for Impact-Weighted Taxation won a recent tax policy prize. New Zealand hasn't implemented a comprehensive suite of "green taxes", but Clean Car rebates (and fees), petrol taxes, and the Emissions Trading Scheme ('ETS') are, to some extent, intended to change behaviour and put a price on pollution.

Support for these types of taxes falls along political lines. Labour introduced the Clean Car Discount in 2021 (dubbed the "ute tax" by the Opposition), introduced a fuel tax in Auckland to fund light rail, and established the Climate Emergency Response Fund which earmarks proceeds from the ETS to be spent on climate-change reduction. National and ACT will abolish the Clean Car Discount and redirect climate funds, with National also pledging to repeal Auckland's Regional Fuel Tax.

What happens between now and the Election?

Parliament has dissolved and the campaign is now in full swing. In Parliament's last sitting week there were a few final tax flurries, with the Digital Services Tax Bill introduced and the Taxation Principles Reporting Act receiving Royal assent.

All legislation that was passing through the House has lapsed. This includes the annual rates tax bill introduced at the Budget in May, which increased the trust tax rate to 39% (a change neither major party opposes), introduced the GloBE rules, announced rollover relief for assets damaged in the flooding events, and KiwiSaver contributions for paid parental leave recipients. The next government will decide what matters to continue with, and where to start afresh.

The pre-election economic and fiscal update (PREFU) will be released on 12 September 2023, and will provide insight into the Government's books and, depending on the forecast, may trigger further political promises.

Tax is a hot topic this Election, with plenty of campaign proposals for tax nerds to get stuck into. So, strap in tight, don't forget to cast your vote, and contact your usual Deloitte advisor if you'd like to discuss how any of these policies could affect you or your business.

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The removal of tax depreciation on non-residential buildings....here we go again...Back to the Future!!

By Iain Bradley and Denise Hodgkins

When the Labour Party first announced that part of its 2023 Election Tax Policy included a proposal to remove GST from fruit and vegetables, many people might have missed the fine print which noted this would be funded by removing the ability for businesses to claim depreciation on commercial buildings. When the National Party announced its 2023 Election Tax Policy, it was very clear the tax cut promises would be funded by additional taxes, and it was very clear that removing depreciation on commercial buildings was part of the equation.

Given that both of the major parties have announced the removal of tax depreciation, it is highly likely that the policy will be enacted, in some form, following the election on 14 October 2023.

If elected, the National Party tax package has this change taking effect from the 2024/25 income year. For Labour, this change was announced as part of a wider policy to remove GST on fruit and vegetables, which is expected to come into effect from 1 April 2024, so it is fair to assume that the depreciation change would take effect for the 2024/25 income year (or later) under a Labour government as well.

Although we do not yet know the precise details of the likely removal of tax depreciation on non-residential buildings, we do know that the tax, financial reporting, and other commercial implications of the change will be significant. We have seen this movie before.

When the removal of tax depreciation on buildings was announced back in Budget 2010, this was a significant and sudden change and it brought with it a number of complications for businesses to work through.

Many of the same issues will now need to be revisited. Here are 10 issues to think about if you are currently claiming tax depreciation on commercial buildings (or if you might purchase a commercial building in the future):

1. What is the meaning of a "building" and is your building caught by the removal of tax depreciation on non-residential buildings?
2. Have you split out the fit-out from the building structure when recording the commercial building in your tax fixed asset register? Have you got support for the split out and the values used?
3. How will the removal of tax depreciation on commercial buildings impact your decision to acquire a building? Does the decision made need to be revisited and does your view on price and/or willingness to purchase change?
4. What will the cash tax impact be for your organisation from the removal of tax depreciation on commercial buildings?
5. When is the removal of tax depreciation effective from and when is the change going to be enacted or substantively enacted for the purposes of determining the first set of financial statements that the deferred tax and tax expense impact will need to be reflected in?
6. What is the likely quantum of the adverse deferred tax and tax expense impact on your financial statements? This could depend on when the buildings were acquired and whether or not the initial recognition exception applied to the building.
7. Is the building an investment property where the rebuttable presumption that the carrying value will be recovered through sale has not been rebutted? The answer to this question could significantly alter your deferred tax outcome.
8. What are the implications of the deferred tax liability increase on banking covenants or thin capitalisation (interest deductibility) calculations?
9. How will the initial recognition exception apply to new buildings acquired or additions to existing buildings?
10. How will you determine whether future expenditure on your building is deductible repairs and maintenance or, instead, capital improvements that will now be non-deductible, non-depreciable "blackhole" expenditure?

For many taxpayers, the implications of the removal of tax depreciation on commercial buildings will be significant. Please contact your usual Deloitte tax advisor if you would like to discuss the potential implications for your organisation.

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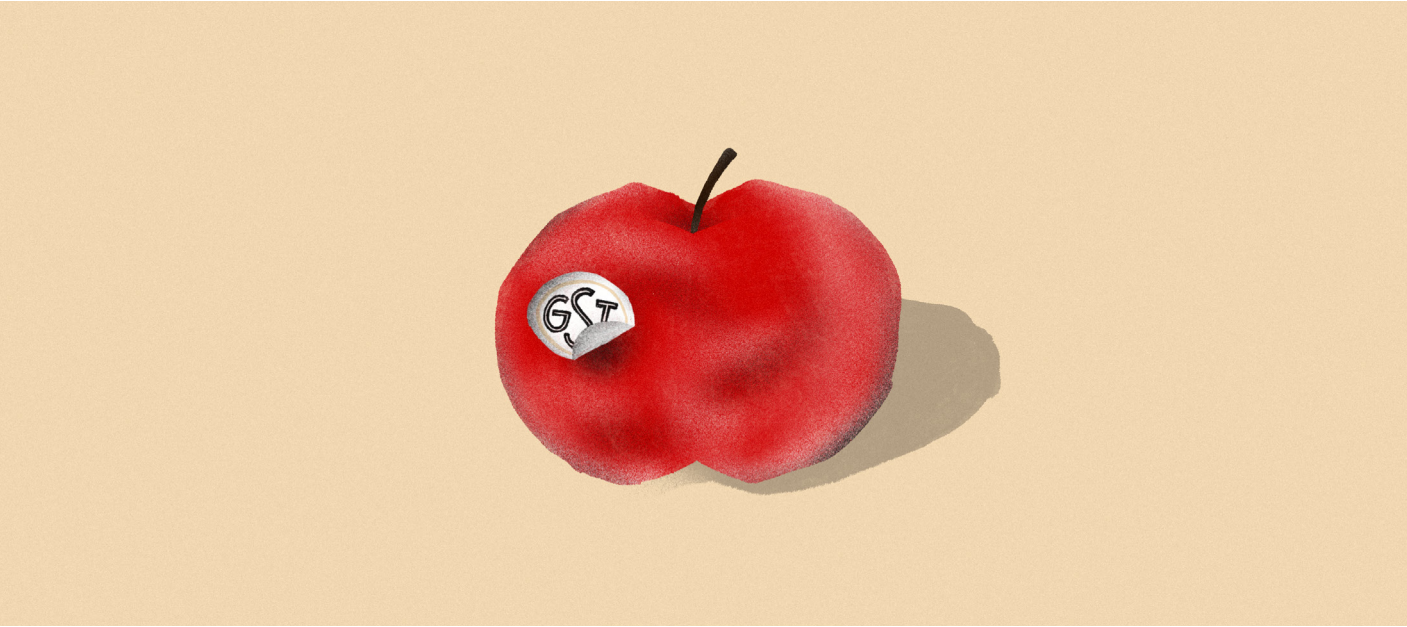
A business lens on taking GST off fruit and vegetables

By Mirei Yahagi and Jeanne du Buisson



The Labour Party's recently announced tax policy for the upcoming 2023 election includes removing GST from the sale of fruit and vegetables. This has undoubtedly been one of the key election topics discussed in the past month. While much attention, especially in the media, has been directed towards the potential benefits (or not) for consumers, there have been limited discussions in the media on the policy's likely impact on New Zealand businesses.

The proposal would align New Zealand more closely with the "Value Added Tax" rules in other countries like the United Kingdom and Australia, where there are a number of food-related exemptions. However, the implementation of Labour's GST policy will not be straightforward and represents a substantial departure from New Zealand's much envied "pure" GST legislation.

In New Zealand GST is a broadly based consumption tax, meaning that the end consumer bears its cost. Therefore, removing GST from fruit and vegetables would appear to offer a benefit to ordinary consumers by, in theory, reducing the cost of the fruit and vegetables they consume. However, like most things, in reality the situation is more complicated. When considering the broader implications for businesses this policy change is likely to lead to increased compliance costs, which in turn will erode any savings for consumers.

GST should not be a cost to businesses

One of the fundamental principles of GST is that while it is effectively collected by GST-registered persons (e.g., a business), it should not be a cost for those businesses. While GST-registered persons are generally required to charge GST on sales they make in New Zealand (output tax), they are also generally allowed to deduct the GST charged on purchases (input tax). End consumers therefore ultimately bear the cost of GST as they are not GST-registered and are not entitled to input tax credits for the GST charged on their purchases.

Simply put, removing 15% GST off fruit and vegetables (i.e., making them zero-rated supplies) has no impact on the input tax the businesses can claim in their GST returns, as businesses are doing this already (provided that they use the fruit and vegetables for their business activity). Businesses like cafes and restaurants won't see a reduction in their costs of sales. Any GST paid on the purchase of fruit and vegetables is already claimed back from Inland Revenue.

GST should not be complex

GST is intended to be a relatively simple and efficient system to tax consumption without distorting consumers' preferences between different goods and services. Currently imposed at a single rate of 15%, GST encompasses a wide range of goods and services, with few exemptions. This has resulted in GST becoming one of New Zealand's most important, widely encountered, and arguably most successful taxes. GST is New Zealand's second most important tax in terms of the revenue raised (in 2021-22 Inland Revenue collected approximately $24.7 billion in GST, around 25% of New Zealand's total tax revenue).

The proposed policy introduces complexity by distinguishing between different categories of food products. The current idea by Labour is to remove GST from fresh and frozen fruit and vegetables while maintaining it on "processed" fruit and vegetables, such as canned and dried items. While this framework may seem straightforward on paper, the reality is that classifying products can be challenging and Australian businesses' experience with classifying GST on food provides valuable insights into the potential impact on New Zealand businesses. Under the Australian GST Act, a "supply of food" is generally GST-free, unless it falls into specific categories such as "restaurant meals", "confectionery", "bakery products", and "prepared foods".

As you can imagine, boundary issues arise leading to debates over whether certain food items fit into the defined categories. One recent example is the Australian Administrative Appeals Tribunal case between a yoghurt manufacturer and the Australian Taxation Office. The yoghurt manufacturer is known for its "flip" style yogurt, which consists of the primary compartment holding flavoured yogurt, while a smaller separate compartment containing dry inclusions of cookie fragments and white chocolate chips. The determination was that these dry inclusions significantly contribute to the product's marketing and consumer experience. They are also easily identifiable and don't constitute a standalone product apart from the yogurt. Consequently, the product is regarded as a combination of flavoured yogurt, cookie pieces, and white chocolate chips.

The Australian GST Act designates yoghurt as GST-free, and cookie pieces and white chocolate chips as falling under the categories of "biscuit goods" and "confectionery", which are subject to GST at a standard rate. Given that the "flip" yogurt product combines various foods (0% and 10%), at least one of which aligns with the Australian GST Act's excluded food categories, it was decided that the entire product is ineligible for GST-free treatment.

This Australian case highlights the increased complexity of classifying food for GST purposes. The product's marketing, packaging, and consumption methods often play a pivotal role in the classification, which is likely to extend to New Zealand as well. Ongoing innovations in the food industry, particularly in plant-based products and novel food combinations, will likely also fuel this complexity.

This complexity also presents a greater risk for suppliers that sell high quantities of food products, as an incorrect GST classification can quickly become an error that will have a material financial impact. The above complexity also does not account for the necessary systems changes that food product suppliers will need to deal with, such as implementing methods to differentiate the qualifying items and non-qualifying items, as well as applying the correct GST coding treatment within accounting systems. A study conducted by an accounting software company revealed that, when compared to New Zealand, Australian businesses are spending twice the amount of time on internal costs for GST compliance, and twice the amount on external bookkeeping expenses. While Labour suggests that modern technology could alleviate compliance costs, this has not been the case internationally. It would also not eliminate the potential for costly legal disputes in the wake of such changes.

From a purchaser's perspective, often a taxpayer is only ever acquiring goods and services with GST charged at 15% or 0%. Businesses will need to get used to making purchases where the GST charged on the total supply could range between these two percentages (for example if office food supplies are being acquired with a mix of fruits, vegetables, and other products). This may lead to increased complexity around accounts payable processes and internal controls verifying GST treatments (for example, software checking that the GST on an invoice is equal to 15% may start detecting false errors).

It is important to note that, depending on the election's outcome, the proposed policy could be in legislation from 1 April 2024. This timeline does not offer suppliers adequate time to establish sufficient systems for policy implementation or seek guidance on boundary-related concerns.

Should GST be touched?

In summary, tinkering with GST will cause more headaches for New Zealand businesses which are already facing a squeeze in their margins due to inflationary cost increases. To avoid being hit with a big tax bill, impacted businesses will also need to spend more on resources to ensure that they are making the correct GST determinations.

Given the effectiveness of the current GST rules in New Zealand and the challenges presented by removing GST from fruit and vegetables, in our view a better alternative would be to consider options to promote healthier choices and support households with direct financial support.

If you have any questions on GST or how GST impacts your business, please don't hesitate to get in touch with us.

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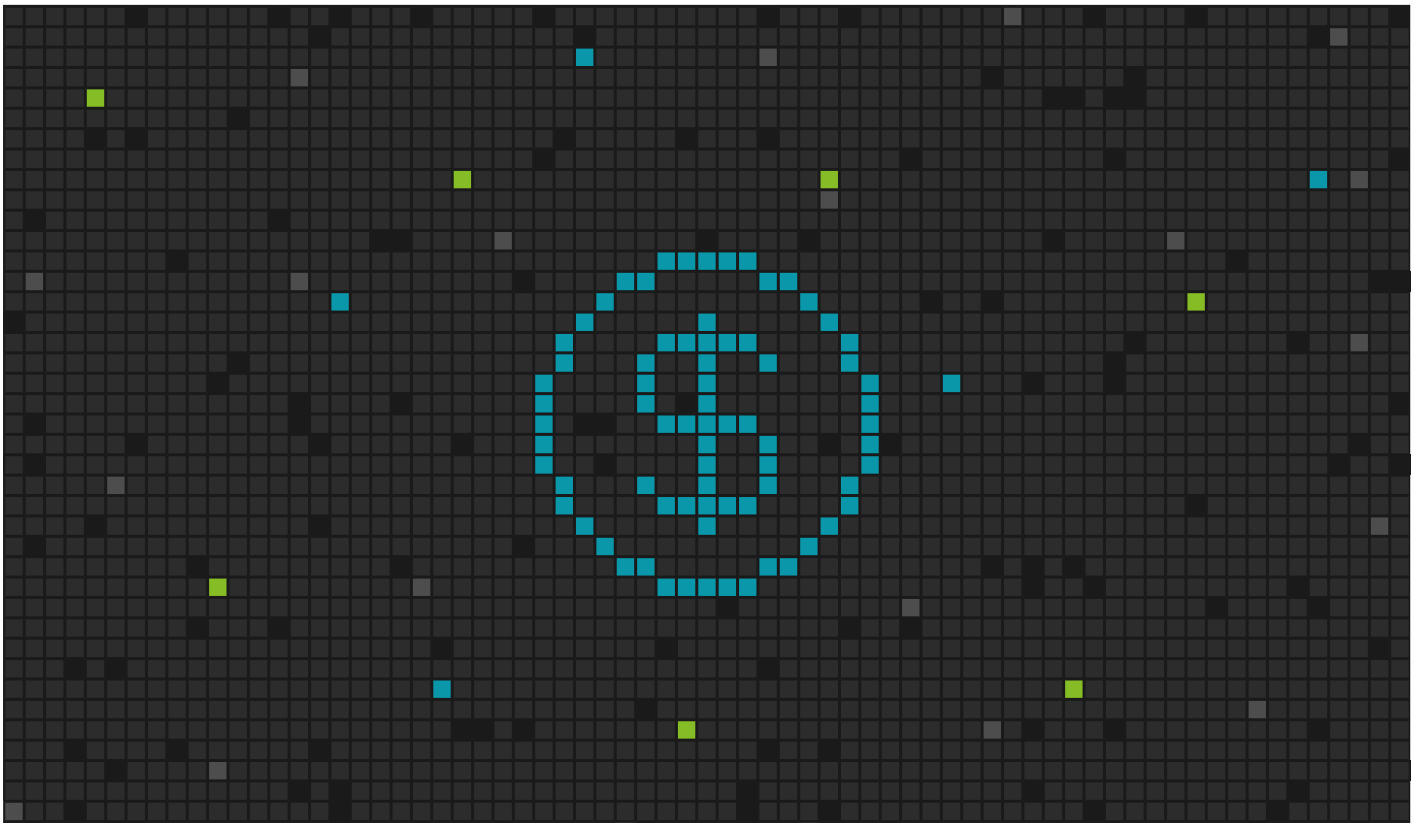
A parting gift: Digital Services Tax Bill

By Viola Trnski and Robyn Walker



The New Zealand Government introduced the Digital Services Tax Bill (Bill) on 31 August, Parliament's last sitting day before the 2023 General Election.

Given this timeframe, the Bill won't pass into law until after the election. It is unclear whether a Digital Services Tax (DST) will be implemented if there is a change in government, as other parties' election policies have remained silent on the issue.

A DST has formed part of Labour's tax policy since at least 2020, although there has been a preference for a multilateral DST to be developed and implemented by the OECD first. Consultation on a DST was undertaken by Officials in 2019.

The Government's press release stated on 29 August stated:

"We have been actively participating in negotiations at the OECD for a multilateral agreement to address these issues. This work is making slow progress. As part of these negotiations, we have agreed not to bring in a unilateral measure such as DST until 1 January 2025.

While we will keep working to support a multilateral agreement, we are not prepared to simply wait around until then to find out. That is why we have prepared legislation that is ready to go if the OECD process does not succeed."

What is the proposed DST?

The DST will apply to companies with global digital services revenue greater than €750 million per year and at least NZ$3.5 million a year from digital services provided to New Zealand users.

"Digital services revenue" includes revenue relating to intermediation platforms, social media and content-sharing platforms, internet search engines, digital advertising, and user-generated data.

The Bill will determine whether a digital service is provided to a New Zealand user by reference to the person's billing address, delivery address, IP address, bank details, phone area code, or geolocation. However, if the transaction is on an intermediation platform and also relates to a user in a foreign country with a similar DST, the DST amount will be reduced by 50%.

The DST will be imposed at a rate of 3% on the gross taxable digital services revenue connected to New Zealand users or land that is derived by groups within the threshold. By comparison, the United Kingdom imposes a 2% DST, and France, Italy and Spain have a 3% DST. New Zealand's DST is expected to raise NZ$222 million in revenue over the four-year forecast period.

The intended commencement date is 1 January 2025; however, the Bill contains a provision for Parliament to defer the commencement of the DST if the OECD makes sufficient progress towards the implementation of Pillar One within a satisfactory timeframe.

Broader context

DSTs have not been widely adopted. The United Kingdom, France, Spain, and Italy have implemented a DST and Canada has proposed one. A number of other countries have implemented various other measures to tax digital services. Australia and the European Union considered and subsequently abandoned DST proposals.

If New Zealand implements a DST, it will only apply to a very small group of multinationals. By comparison, the Regulatory Impact Assessment ('RIA') accompanying the Bill notes the UK's DST captures 18 entities. The RIA also noted there may be a risk of retaliatory tariffs from host countries of these entities if New Zealand goes ahead with a DST before the OECD framework is implemented.

As with all tax questions, whether a DST should be introduced in New Zealand is debatable. A DST is targeted towards large multinational tech companies that have historically paid low rates of tax in New Zealand. However, there is a possibility that New Zealand consumers will ultimately bear the cost of the DST, particularly if other countries do not implement one.

With the New Zealand Parliament dissolving for the election, it will be a question for the new Government to decide whether to reinstate the Bill and continue with the legislative processes. If so, the public will have the opportunity to comment on the legislation.

If you have any queries, please contact your usual Deloitte advisor.

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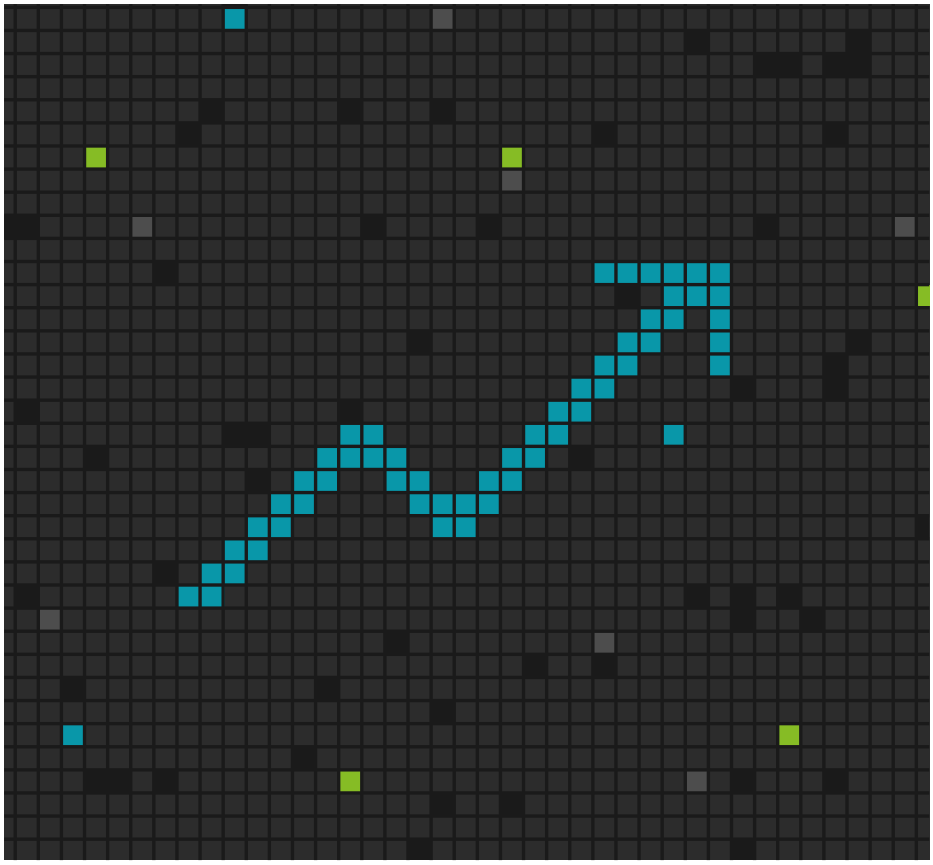

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Do you operate a Customs Controlled Area? Expect a Customs Officer to visit you soon.

By Jeanne du Buisson, Haidee Watkin and Sid Mahajan

Is your Customs Controlled Area compliant?

As part of a return to pre-COVID compliance activities, New Zealand Customs Service (NZ Customs) have had a renewed focus on Customs Controlled Areas (CCAs). NZ Customs officers are entitled to enter and investigate activities within a CCA at any time. The primary purpose of these investigations is to check whether obligations required under the CCA licence are being complied with. Businesses operating CCAs that have not had a compliance check with a NZ Customs Officer in the past five years should expect a visit within the next year, with more regular visits in the future.

There are currently around 1,500 CCAs across New Zealand in which NZ Customs monitors or conducts activities. There are several general obligations imposed on CCA licence holders, as well as specific obligations that relate directly to the area in question. Ensuring you are compliant with these obligations is crucial towards maintaining your licence.

What is a CCA?

Customs Controlled Areas are specific areas licenced for purposes relating to NZ Customs' border and excise functions. The activities undertaken in CCAs include examination areas for the manufacture of excisable items (such as alcohol), examination of imports, storage areas, and export areas, as well as airport/seaport activities. These areas play a critical role in maintaining border control and security, acting as the last point of contact before items are exported or the first point of contact when items are imported, as well as allowing for the management of duty-free or excisable items.

What are the NZ Customs officers checking for?

Valid licence – In order to operate a CCA you need to hold a valid licence, which should be renewed annually.

Licence activities within the specified area – CCA licences are granted based on the specified area(s) of your premises. It is important to ensure that all your CCA-related activities remain within this area and are consistent with the floor plan submitted to NZ Customs with the licence application/renewal. If any changes are required to this area, it should be pre-approved by NZ Customs.

No unauthorised access – Ensuring you have adequate controls in place, with only authorised people having access to your CCA. This can be supported by evidence of logs such as employee swipe cards or security cameras.

Signage – Your CCA should be clearly marked with signage. A template signage is available on the NZ Customs' website.

Inspecting of goods – NZ Customs Officers have the right to inspect goods produced or stored in a CCA. As a result, it is important to ensure that you are both able to produce goods for inspection and that goods produced are within the scope of the permission granted by your licence.

Tracking of inward and outward goods - The tracking of imported goods and manufactured excisable goods is key to demonstrating adequate controls in your CCA. For example, the ability to track goods throughout the entire lifecycle, i.e., when the good enters the CCA (import), any changes made to the inventory (damaged stock) and when the good exits the CCA (export).

Record keeping - Following this, it is equally important to ensure that records are stored for a minimum period of 7 years within New Zealand, unless other relevant authorisations have been issued by NZ Customs.

Specified conditions – any other conditions specified in the licence to operate a CCA.

If you have a licence to operate a CCA, it is crucial to check that your controls are adequate to cover your obligations. Navigating these requirements can often be complex, so now is a good opportunity to get in touch with Deloitte about checking the controls you have in place. For more information, reach out to your usual Deloitte advisor.

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Inland Revenue: Friend or foe?

By Andrea Scatchard and Samuel Eddy

Over the past few years, businesses all around New Zealand have been under pressure and feeling the economic pain. Despite tropical cyclones, New Zealand's economy entering a recession, and constant official cash rate increases, the Inland Revenue will keep knocking. This year there has been an increase in the number of companies being placed into liquidation, including some high-profile businesses in the construction industry. Not all of these liquidations will be at the instigation of Inland Revenue, but a significant number will be as the Inland Revenue is often a significant creditor in insolvencies. Inland Revenue takes a particularly dim view, and so they should, of taxpayers who don't meet their tax obligations on time.

Even when times are tough, it is important to keep your tax affairs in order as the cost of use of money interest, late payment and late filing penalties can add up quickly. So, what can you do to stay in Inland Revenue's good books?

Keep on top of filing your returns

During challenging times it may be tempting to delay filing returns, particularly if cash flow is tight. However, it is essential to meet filing deadlines to avoid late filing penalties being applied. Keeping the discipline of filing returns is essential if you want to Inland Revenue to look favourably on an instalment request.

Set up instalment arrangements

All taxpayers are required to pay their taxes in full and on time. Unpaid tax returns can quickly spiral into significant accumulated debt, particularly when penalties and interest start to be applied. If your business is unable to meet any of your tax payments on time, you may be able to apply for an instalment arrangement to pay the debt off over time. It is important to talk about this as an option with Inland Revenue early before your payments fall due. Essentially you will need to agree on an instalment amount, and payment start and end dates. Inland Revenue may ask for some financial information to support the application that tax payments can't be made. The overriding condition is that you will need to agree to pay the tax as quickly as is reasonably possible. In other words, this is not a holiday or deferral from paying taxes. A 1% penalty (instead of potentially 5%) will still be applied upfront, but the Commissioner has the discretion to remit penalties and interest down the track if the business complies with the arrangement and the core tax debt is paid.

Make sure you avoid UOMI

Use of money interest (UOMI) is paid by either the Commissioner (when tax is overpaid) or by the taxpayer (when tax is underpaid) and applies to most taxes. The current rate charged by the Commissioner on underpayments is 10.91% and the rate paid on overpayments is 4.67%. The high interest rate charged gives an incentive to taxpayers to encourage payments to be made on time and not use the taxes due as a source of business finance. Our February 2023 article has more information about UOMI.

Provisional tax payments and tax pooling

Provisional tax payments are primarily paid based on an uplift from a taxpayer's most recently filed income tax return. If you are forecasting that your results for the 2024 year will be worse than 2022 or 2023, then paying provisional tax based on the uplift method may not be best from a cash flow perspective. While you can estimate your current year's liability and pay a lower amount based on that estimate, we don't usually recommend this as it exposes you to possible penalties if that estimate turns out to not be fair and reasonable when compared to the final tax liability when the actual tax return is prepared.

Often a better option is to make use of tax pooling. Tax pooling intermediaries operate tax pooling accounts with Inland Revenue, allowing taxpayers to deposit income tax payments into their tax pooling trust accounts that are then transferred to Inland Revenue once the tax returns have been filed and the final tax liability is known. Tax pooling is particularly useful when there are decreasing profits or missed payments. It can also allow taxpayers to postpone tax payments (at a competitive interest rate) to free up working capital or better match your cash flow if you have a seasonal business.

In tough times, tax obligations can cause extra strain on business cash flow and liquidity. It is important to make sure you keep communicating open communication with your tax advisor and Inland Revenue to try to avoid penalties, interest and potential insolvency.

To make the best use of the options available, if you have any questions or would like help navigating the options available to you, please seek advice from your usual Deloitte advisor.

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You've got AIL

By Alex Kingston and Troy Andrews

"You've got AIL"

These are often the words New Zealand borrowers are hoping to hear from Inland Revenue before paying interest to a foreign lender. But it's important to make sure all the right boxes have been ticked to qualify for the Approved Issuer Levy (AIL), and that good governance is in place to ensure ongoing compliance with the regime. When it comes to AIL, there can be quite severe and unexpected outcomes for getting it wrong.

Outline of AIL regime

The AIL regime is available when interest is paid by a New Zealand resident to unrelated foreign lenders.

Broadly, once Inland Revenue has confirmed (i) the borrower has approved issuer status, and (ii) the relevant loan/security (or class of securities) have been registered, a levy equal to 2% of the interest may be paid by the borrower, instead of the Non-Resident Withholding Tax (NRWT) that would usually otherwise be payable.

The AIL regime has been around since the early 1990s and was intended to lower the cost of foreign borrowing for New Zealand residents. Foreign lenders would typically pass on the cost of withholding taxes to New Zealand borrowers (where that withholding tax was not valuable/available as a tax credit offshore), so AIL was made available as an alternative to NRWT (where it has been agreed between borrower and lender that AIL is preferred). AIL of 2% effectively results in an after-tax cost to the New Zealand borrower of 1.44% of the interest amount (whereas NRWT would otherwise commonly apply at 10% to 15%). AIL may also be reduced to 0% for certain widely offered/widely held bonds denominated in NZD.

AIL is only available where the borrower and lender are not associated (except for within certain banking groups), and rules have been tightened since it's introduction to make it more difficult to structure into the AIL regime where there is no genuine third-party lending relationship.

Common issues

While the concept of AIL is not complex, there are a number of issues that commonly arise in the application of the AIL regime by taxpayers and as mentioned above, the implications of getting it wrong can be significant. Examples of issues we've seen include:

1. Failing to register in time

There is a strict requirement that AIL registration (and registration of the relevant debt instrument) must have been made prior to an interest payment, in order to apply AIL instead of NRWT. There is no flexibility to simply register prior to the due date for AIL, the registration must be done before the interest payment. Inland Revenue generally considers the date it receives an application as the registration date. In our experience, Inland Revenue does not allow any flexibility with this, with the consequences being NRWT would apply to interest payments made up until the AIL registration date. Often foreign lenders will seek a "tax gross-up clause" in loan agreements, meaning that it is the New Zealand borrower that bears this NRWT cost.

It is therefore important to consider AIL compliance in the early stages of arranging any new foreign borrowing and (assuming the lender and borrower want AIL to apply and qualify) have a clear plan in place to undertake the necessary registrations. Some agreements will also include AIL registration as a condition precedent to being able to draw down funds.

2. Non-standard lending scenarios

The AIL rules (including Inland Revenue registration/application forms) do not always clearly contemplate some of the more complex or unique lending scenarios. We have found that early engagement with Inland Revenue is key, to ensure there is sufficient time to confirm whether AIL is available, prior to the first interest payment. For example, there can be complexity in how (or whether it is possible) to apply AIL in the context of certain cash pooling arrangements, syndicated loans, securitisations, peer-to-peer lending, amongst others. We have observed that Inland Revenue has been willing in some circumstances to allow AIL compliance to be undertaken on behalf of certain classes of borrowers, subject to certain conditions. It is essential to engage with Inland Revenue early to allow these discussions to take place.

3. Ongoing compliance

Approval to apply AIL is not always the end of the story for a particular loan or other debt instrument. For example:

- Changes in terms may be viewed as a new arrangement, which can trigger a need to re-register the security for AIL;
- Changes in lenders/the portions held by lenders in a syndicated loan scenario may also trigger a requirement to either re-register or update Inland Revenue's records. In practice, this may depend on the manner in which the loan instrument has been registered in the first place.
- For widely-held bonds that qualify for a 0% rate of AIL, information still needs to be reported to Inland Revenue following each interest payment date, with the consequence of late filing being that 2% AIL will apply instead.
- Corporate re-organisations such as company amalgamations or the novation of loans to a new borrower may result in new registrations needing to be undertaken.
- AIL must be paid by the due date. Any errors in accounting for AIL on time will result in NRWT being payable, which is an expensive mistake to make. Inland Revenue will show no leniency when it comes to administrative errors.

Robust processes and controls therefore need to be in place to ensure filings are made on time. Changes in lending arrangements also need to be monitored, with regular communication between tax and treasury teams, to ensure AIL continues to apply (and at the correct rate of 0% or 2%).

Final comment

As a concessionary regime, electing to apply AIL to a loan from a foreign lender is optional, but can be an effective way of reducing the cost of borrowing for New Zealand borrowers. Overall, the regime is seen as positive from the perspective of NZ Inc., which is usually considered a net "importer" of capital.

For taxpayers, given the consequences of not getting AIL compliance right can be a significantly higher cost of borrowing than planned, it is essential to think about AIL early in the financing process, and have good governance procedures in place to ensure compliance. With Inland Revenue's recent focus on Tax Governance, we would suggest that AIL (and withholding taxes more broadly) is thought about, in addition to other tax types that may be more front of mind.

If you have any questions about the AIL rules and how they may apply to you, please contact your usual Deloitte advisor.

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Snapshot of recent developments

Tax legislation and policy announcements

UOMI rates increased on 29 August 2023

On 24 July 2023, the Taxation (Use of Money Interest Rates) Amendment Regulations (No 2) 2023 were passed. The regulations increased, from **29 August 2023**, the taxpayer's paying rate from 10.39% to **10.91%** and the CIR's paying rate from 3.53% to **4.67%**. Inland Revenue has released a special report on these regulations.

FBT interest rate for employment-related loans increases

On 3 August 2023, the Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2023 were passed, increasing the FBT interest rate from 7.89% to **8.41%**. The new rate will apply for the quarter beginning **1 October 2023** and for subsequent quarters. Inland Revenue has released a special report on these regulations.

Emissions Trading Scheme settings updated

On 25 July 2023, Minister of Climate Change Hon James Shaw announced the Government's annual decision on unit limits and price control settings for the NZ ETS for 2023-2028. Changes included raising the trigger prices for cost containment reserve, raising the auction reserve price, and reducing the number of carbon units available for auction.

Oral submissions on Taxation (Annual Rates for 2022-23, Multinational Tax and Remedial Matters) Bill deferred until after election

On 2 August 2023, the Finance and Expenditure Committee advised oral submitters on the May tax bill that, in line with past practice, submissions will not be heard until after the election. Written submissions on the Bill are available on the Parliament website.

Government to remove bright-line test for Cyclone buyout properties

On 23 August 2023, the Government announced that a legislative amendment will be made to ensure the bright-line test will not be applied to flood-affected properties bought by the Government or local authorities.

Taxation Principles Reporting Act 2023 passed into law

After being passed through its final stages under urgency, on 30 August 2023 the Taxation Principles Reporting Act 2023 received Royal assent. The Act requires the Commissioner of Inland Revenue to publish annual reports against a schedule of defined tax system principles. The Act came into force the day after it received Royal assent with the Commissioner's first report being due at the end of 2023.

Inland Revenue statements and guidance

Tax Information Bulletin, Vol 35, No 7, August 2023

On 31 July 2023, Inland Revenue published Tax Information Bulletin Vol 35, No 7 for August 2023.

Interpretation Statements on GST Grouping

On 7 August 2023, Inland Revenue published two draft interpretation statements on GST grouping.

GST – Who can group register? clarifies the Commissioner's position on the GST treatment of groups of companies, mixed groups, and non-residents under section 55 of the Goods and Services Tax Act 1985. GST Grouping for Companies explains the consequences of GST grouping for companies.

The deadline for comment on both items is **14 September 2023**.

Income tax: Income – when gifts are assessable income

On 7 August 2023, Inland Revenue published a draft Interpretation Statement Income tax: Income – when gifts are assessable income. A gift is not usually subject to income tax. Inland Revenue have released this interpretation statement and it considers the circumstances in which a gift is subject to income tax in the recipient's hands. The statement applies both to monetary gifts and to non-monetary gifts that are convertible to money.

The deadline for comment is **18 September 2023**.

Interpretation Statement: Taxation of Trusts

On 7 August 2023, Inland Revenue published the draft interpretation statement Taxation of Trusts and accompanying reading guide. The draft explains the taxation of trusts under the rules in the Income Tax Act 2007 and acts as a general guide on how income derived by trusts and beneficiaries is taxed. The item also sets out the obligations imposed on settlors, trustees, and beneficiaries.

The deadline for comment is **13 October 2023**.

ED00249: Amortisation Rates for Listed Horticultural Plants

On 17 August 2023, Inland Revenue issued ED00249 which sets out the proposed amortisation rates (based on diminishing values) for listed horticultural plants. The Determination applies from the 1 April 2023 and subsequent income years and replaces DET 05/01 (issued May 2005).

The deadline for comment is **28 September 2023**.

Global tax news

OECD updates

How does corporate taxation affect business investment?

On 19 July 2023, the Economics Department of the OECD released working papers including looking at how corporate taxation affects business investment.

Modest recovery in Asia-Pacific tax revenues as the after-effects of Covid-19 weigh on tourism

On 25 July 2023, as part of the Revenue Statistics in Asia and the Pacific 2023 report, the OECD announced that tax-to-GDP ratios remained below pre-pandemic levels in a majority of Asia-Pacific countries in 2021.

R&D working papers

On 27 July 2023, the OECD Centre for Tax Policy and Administration released two working papers:

- Effective tax rates for R&D intangibles
- A time series perspective on income-based tax support for R&D and innovation

Note: The items covered here include only those items not covered in other articles in this issue of Tax Alert.

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