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Tax Alert

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Inland Revenue focus areas: Get your house in order

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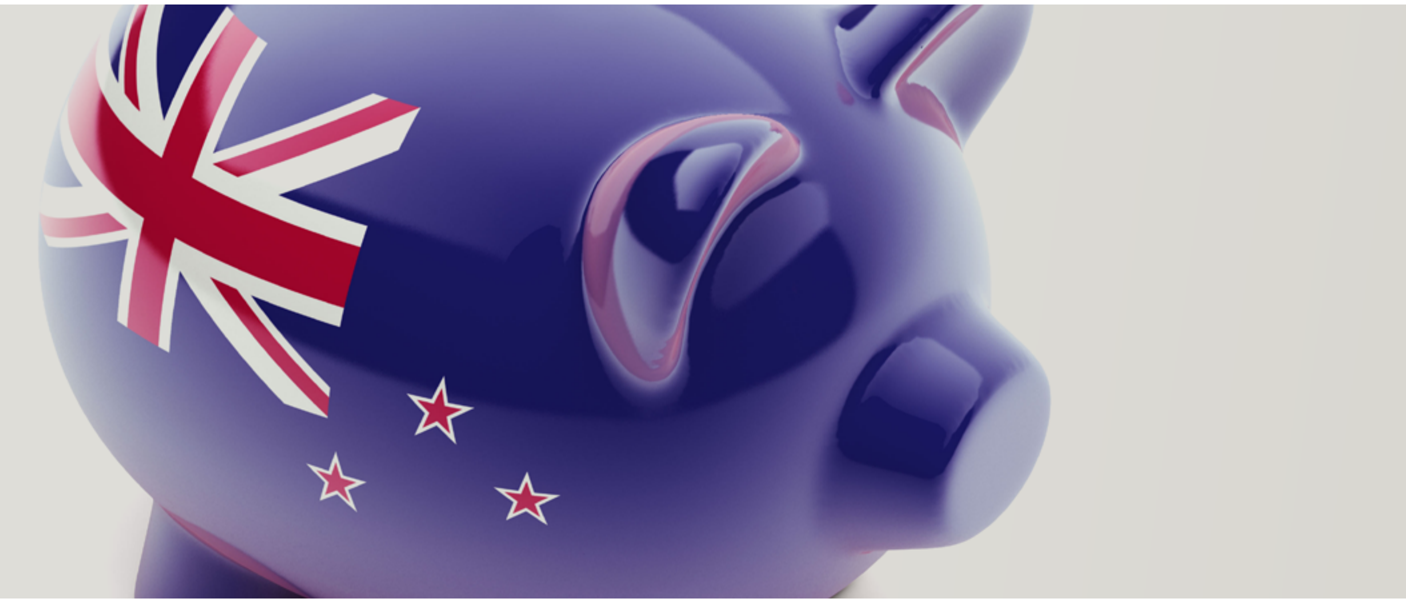
Inland Revenue focus areas: Get your house in order

By Campbell Rose and Robyn Walker



The additional Inland Revenue (IR) funding for "investment in compliance activities" in Budget 2024 and the subsequent press releases from both the Minister of Revenue and the Commissioner of Inland Revenue should leave taxpayers and their advisors with little doubt that IR is going to become considerably more visible. This approach follows a significant period of time during which IR's focus was less on checking compliance, and more on bedding in a significant technology transformation (and associated workforce changes) and then dealing with the need to support taxpayers through the COVID period (particularly through administering associated relief packages).

This period of diverted focus has meant that many taxpayers have not had much or any contact from IR, or if they have it's been a request for information which never seemed to result in any follow-up questions or actions. Add to that a feeling that there has been a blind eye turned to non-compliance with fringe benefit tax (FBT), and some taxpayers may have become more complacent or even less "voluntarily compliant" with tax laws, and more willing to take a gamble on whether IR will "ever find it". The need for IR to enforce tax rules and for voluntary compliance to prevail is key to the integrity of the tax system. Anyone wanting a greater appreciation of current perceptions of the tax system and enforcement activity should read the draft first report under the Taxation Principles Reporting Act (now repealed): you can find the data on pages 17-22.

In terms of recent IR activity, we are already seeing a clear increase in requests for information, more extensive information requests and the use of questionnaires, as well as letters advising that matters have been put straight into audit. Over recent years audit activity (and funding for it) has waned, but IR is back and planning to make up for lost time.

Both the Minister and Commissioner have indicated particular areas of immediate focus, but the clear message for all taxpayers is that if there are skeletons in your tax closet, then you should be clearing them out and getting your tax affairs tidied up – both in terms of high-level governance as well as focussing on relevant areas from an operational perspective.

Compliance focus areas announced to date:

- Hidden economy
- Trusts
- Retail sector
- Construction sector
- Property
- Crypto-currency
- Electronic sale suppression software
- Corporate restructures
- Overseas student loan borrowers
- Small business cashflow loans
- Multinationals

Voluntary compliance

It's a much better outcome when taxpayers voluntarily comply with tax laws. However, there will always be occasions where a taxpayer either makes a genuine error, or there is a dispute over how the law is intended to operate. IR's new computer system, combined with much more extensive data collection, data analytics capability and cross-government information exchanges, have significantly increased the ability of IR to detect genuine errors, other anomalies or focus areas, and more deliberate non-compliance.

To encourage compliance, the IR has a range of penalties it can impose on taxpayers who have taken tax positions at odds with the law. These can range from 20% to 150% of the tax shortfall. However, the IR can also reduce these penalties, sometimes by as much as 100%, if the taxpayer makes a voluntary disclosure. Voluntary disclosures can be made at any time, but making them before you've been notified of an audit materially improves the opportunity to secure a penalty reduction.

Making voluntary disclosures also has the potential to lower the risk of audit selection. A voluntary disclosure can demonstrate to IR that the taxpayer is undertaking some form of self-review, has governance processes in place, and is making efforts to voluntarily comply.

Other forms of assurance

When it comes to complex commercial arrangements, or just really big value transactions, the only way to get absolute certainty on how the tax rules apply is to apply for a binding ruling from IR. The binding ruling regime allows taxpayers to provide IR with all the details of an arrangement and to have IR rule on how the tax legislation applies. As the name suggests, provided a taxpayer has been accurate (and not misleading) in the application and has complied with any conditions, the ruling will be binding on the IR for the stipulated timeframe (unless there is a law change). Advance pricing agreements in a transfer pricing context also fall into this category.

Another approach is to seek professional advice and review, and regular tax "health checks". While this doesn't have the same level of assurance as a binding ruling, following the advice of a specialist tax advisor is a mitigating factor when it comes to penalties if the IR subsequently disagrees with the approach taken. IR is also undertaking a pilot programme, whereby if certain tax compliance processes are reviewed by accredited specialists using a methodology agreed with IR, then IR generally won't also seek to undertake their own review of those processes. This puts the taxpayer more in control of the experience and timeframes for resolution, and is most effectively undertaken proactively ahead of a potential IR review.

Get your house in order

With the expected (and already experienced) increase in IR activity, taxpayers should take a few essential steps to prepare in case IR should knock at their door. These include:

- Make sure your business records are up to date. Filing and administration can be a drag, but it is essential to have well maintained tax records.
- Check your facts. If you've been relying on historical tax advice or rulings, its good to dust these off periodically and confirm your facts (or the law) and assumptions/ conditions have not changed and you are still complying with the rules. Frequent law changes mean you can't assume a position taken years ago is still applicable today.
- Review any contentious positions. How comfortable are you that your position is reasonable and fully documented? Would obtaining more certainty via a binding ruling be a valuable investment?
- Undertake a review. Having an independent review is a good way to get comfort that you're doing the right thing (FBT, payroll and GST reviews are popular choices), or identify issues (and potential opportunities if you've been overpaying tax) that can be disclosed to IR before an audit.

For more advice on any of these topics, or guidance on what to do if you've received an audit notification, please get in touch with your usual Deloitte tax advisor.

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Identifying assets for tax depreciation: What makes a computer, a computer?

By Hiran Patel and Navroz Singh

Most taxpayers are comfortable with identifying assets and tracking them in a fixed asset register. However, in some cases it might be unclear whether an item is a separate asset, or part of another larger asset. To provide guidance, Inland Revenue has released a [draft interpretation statement] on how to identify the relevant item of property when applying the depreciation rules in the Income Tax Act 2007 (the Act).

While the draft guidance is largely consistent with how the rules have been understood to operate, it is a useful reminder of the complexities that can arise when analysing whether an item of property is a separate asset or if it forms part of another asset.

The draft guidance also provides some useful practical examples to make the principles easier to understand.

Let's take a step back

The Act provides that a taxpayer can claim a depreciation deduction for depreciable property owned by that taxpayer that is used or available for use in an income year.

Depreciation deductions are spread over the useful life of the depreciable property based on a depreciation rate determined by the Commissioner in line with the item of property and the industry in which it operates.

But why does this matter?

At the core of the depreciation rules is the need to identify the relevant item of property. This involves consideration of whether the item of property is its own separate asset, or if it forms part of a different asset. This consideration dictates the depreciation rate that is applied to the asset, and also whether the item of property meets the low-value asset thresholds to qualify for an immediate deduction in the year of acquisition.

While you might think it is clear what an item of depreciable property is, it is not always so simple. The draft guidance is a useful reminder of what to consider when you purchase an asset.

When a new asset is acquired, the first consideration should be if the asset is its own separate asset or if it forms part of a bigger asset. The focus here is on identifying a physical thing that satisfies a particular notion: is the asset an entirety by itself or is it a subsidiary or secondary part of something else?

The draft guidance outlines the considerations that support that an item of property is its own separate asset:

- The item is physically distinct from a wider asset from which the item might be a part.
- The item is (to some degree) functionally complete on its own.
- The item varies the function of another item.

In contrast, the following indicators suggest that an item is not an item of property on its own:

- The item has a physical connection with other items.
- The item is part of an integrated system.
- The item is a necessary part of completing some other item.

The above factors should be considered as a whole to determine whether an item is a separate asset or not. Helpfully, Inland Revenue has provided a useful summary of how these principles operate:

Figure | Hoahoa 1: Determining whether something is an item of property

Source: PUB00274: Income tax – identifying the relevant item of property for depreciation purposes (ird.govt.nz)

How does this work in practice?

For many taxpayers, their first thought when acquiring a new asset might be: "Can I immediately expense it?" (i.e. does it fall under the $1,000 low-value asset threshold?). However, if the item forms part of any other item that is depreciable property, it is not eligible for an immediate write-off, even if it is below the low-value threshold, as it would be considered an improvement. Instead, the item of property should be considered an addition to the existing depreciable property and depreciated in line with the rate used for the existing depreciable property.

An example in the guidance suggests that a desktop computer package consisting of a computer, a wireless keyboard and mouse are one item of depreciable property for tax depreciation purposes.

Inland Revenue's rationale behind this outcome is that the keyboard and mouse have no practical purpose or use without the computer and are intended to function as a single integrated system. This is the case despite the computer, keyboard and mouse all performing a separate function of their own. The conclusion reached is that the three items serve no practical purpose without the other components and cannot be considered to satisfy a particular notion by themselves. As such, they comprise one single item of property (the computer).

This has minimal implications on the amount of tax depreciation that will be claimed as the depreciation rate for the three components is the same in most situations. However, there are practical considerations when, for example, a business purchases a keyboard for $150. Given this keyboard forms part of another item that is depreciable property (the computer), the keyboard would be depreciated rather than being written off as a low-value asset.

This highlights the importance of correctly identifying an item of property at acquisition.

In contrast, the example distinguishes between the purchase of a printer and that of a keyboard and mouse. The guidance argues that a printer is a separate item as the computer can function without the printer and that the printer provides a separate function of printing, copying and scanning.

While the above examples might be relatively clear-cut, what if a keyboard was purchased to accompany a touchscreen tablet? A tablet with a touchscreen can ordinarily be used without a keyboard. Would your analysis change in this circumstance? The draft guidance also states that an additional screen or an ergonomic mouse would also form part of the computer. This example illustrates some of the practical difficulties taxpayers will face in determining where an asset starts and stops.

As with the capital/revenue distinction, the analysis of identifying the relevant item of depreciable property can operate in a grey area where the answer is often not clear-cut. Given this complexity, we would recommend reaching out to your Deloitte tax adviser if you are unsure the next time you purchase a new item of property.

Application to existing published guidance

For completeness, where the Commissioner has already published specific guidance, that guidance should be referred to instead of the guidance for identifying the relevant item of property. This guidance includes:

- Dairy farming – Deductibility of certain expenditure (IS0025)
- Can owners of existing residential rental properties claim deductions for costs incurred to meet Healthy Homes standards? (QB 20/01)
- Residential rental properties - Depreciation of items of depreciable property (IS 10/01)
- Claiming depreciation on buildings (IS 22/04)

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Investing in cryptoassets? It's time to think about your tax obligations…

By Joe Sothcott and Ian Fay

Cryptoassets, once the unregulated Wild West of currency, have come a long way since they first appeared on the internet in 2009. As of 2023, there were more than 25,000 cryptoassets in the marketplace. Despite a steep drop in values during 2022, the cryptoasset bounce-back in has continued into 2024.

Two recent developments serve as a reminder to taxpayers that if they have cryptoassets, they need to ensure they have their tax affairs in order – or, they may face an unpleasant surprise when Inland Revenue comes knocking.

Let's take a quick refresher on these tax rules before diving into the latest developments.

Cryptoassets 101

Cryptoassets, also known as crypto token, cryptocurrencies, virtual currency and a number of other 'crypto' terms, are cryptographically secured digital representations of value that can be transferred, stored or traded electronically, and utilise distributed ledger technologies such as blockchain.

Generally, selling, trading, or exchanging cryptoassets is taxable on realisation. This means that if a person buys a cryptoasset, the amount received upon selling the cryptoasset is taxable with a deduction allowed for the purchase cost of the asset. A sale may be for fiat currency (i.e., Government-issued currency such as NZD) or the sale proceeds may be used to purchase another cryptoasset. However, this is only a rule of thumb and specific tax rules may apply depending on the circumstances.

When there is taxable income from a cryptoasset activity, it must be included in your income tax return. For New Zealand tax residents, this includes cryptoassets acquired or disposed of overseas — for example, using a non-New Zealand-based crypto exchange.

Development #1: Inland Revenue's pivot to cryptoassets

In early July 2024, Inland Revenue announced a new investigation focus on taxpayers who are not declaring income from cryptoassets in their tax returns. Inland Revenue warned that, contrary to popular belief, people are not invisible on the blockchain, and Inland Revenue has the tools and analytic capabilities to identify cryptoasset activities.

In light of Inland Revenue's additional funding for compliance activities ($116 million over the next four years) allocated in Budget 2024, taxpayers should anticipate a ramp-up in questions and information requests. The Commissioner of Inland Revenue has confirmed reducing systemic risks in areas such as cryptoassets will be part of the increased compliance activity. The Commissioner also said Inland Revenue will be progressively approaching crypto traders to let them know about the information Inland Revenue has and give them a final chance to report their income. In other words…no more Mr Nice Guy!

Inland Revenue's computer system has already identified 227,000 New Zealanders holding cryptoassets who undertook 7 million transactions with a value of $7.8 billion. But this may only be the tip of the iceberg with the amount of data Inland Revenue has available set to increase with a second cryptoasset-related development…

Development #2: Crypto-Asset Reporting Framework

As part of Budget 2024, Inland Revenue received additional funding to develop a Crypto-Asset Reporting Framework (CARF). The Regulatory Impact Statement (RIS) notes that, due to the decentralised nature of cryptoassets and limited regulation, tax authorities have limited visibility about income derived from cryptoassets. While Inland Revenue may have the tools to identify some cryptoasset activities, a statutory tax reporting regime would be more comprehensive and provide data that is easier to police.

Enter CARF. CARF is an OECD initiative we first discussed in our November 2022 Tax Alert. The idea is for international jurisdictions to exchange information about cryptoasset activity. The framework is intended to be a quid pro quo information exchange. CARF will be a global minimum standard, meaning all OECD countries will be required to implement it. As of May 2024, fifty jurisdictions have signed up.

So, how will it work? CARF will require crypto intermediaries to provide tax authorities with information about users on their crypto platform. The information will then be automatically exchanged with other CARF jurisdictions. Information collected and provided by the intermediaries will include personal information (i.e., name, address, date of birth, and tax identification number) as well as user and aggregate level data on relevant cryptoasset transactions.

The aggregate level data includes crypto-to-crypto transactions, crypto-to-fiat transactions, and transfers of relevant cryptoassets (such as to a unique identifier in the blockchain "a wallet address") broken down by the relevant cryptoasset. CARF will also include valuation and currency translation rules. For example, the amount paid or received must be reported to the CARF in the fiat currency in which it was reported or received.

CARF will potentially apply from the 2026/27 tax year. The first information exchange relating to 2026 data will take place in 2027. Additional tax revenue is estimated at $50 million per annum from 2027/28 onwards.

The RIS highlights that Inland Revenue may consider pre-populating income tax returns with cryptoasset income and that this could be easier if tax changes were made to simplify how tax is calculated on cryptoassets. This mean that there could be legislative changes to how cryptoassets are taxed; watch this space.

If you have any questions regarding tax obligations on cryptoassets, please contact your usual Deloitte advisor.

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Australian non-resident CGT changes begin consultation

By Robyn Walker and David Watkins

Across the ditch, more details about the potential changes to the Australian capital gains tax (CGT) regime, which were heralded in the Australian Federal Budget, have been published. The Australian Treasury has released a consultation paper proposing to, amongst other things, expand the type of assets foreign residents are subject to CGT on and require foreign residents to notify the Australian Taxation Office (ATO) if they are disposing of shares and other membership interests exceeding AUD 20 million.

Needless to say, this has the potential to be a massive change for foreign residents investing in certain types of assets in Australia. To save you reading the lengthy Treasury documents, our Deloitte Australia colleagues have prepared a handy overview of the consultation paper:

On 23 July 2024, the Australian Treasury released the following documents:

- A consultation paper titled Strengthening the foreign resident capital gains tax regime, which is open for consultation until 20 August 2024; and
- Exposure draft legislation titled Improving the foreign resident capital gains withholding tax regime, on which comments are invited by 5 August 2024.

The paper follows the government's announcement in the 2024–25 Budget to broaden the application of the capital gains tax (CGT) regime to foreign residents. This measure is estimated to increase receipts by AUD 600 million over the five years from 2023–24.

In addition, the exposure draft on foreign resident CGT withholding tax changes follows the government's announcement in the Mid-Year Economic and Fiscal Outlook 2023-24. This measure is estimated to increase receipts by AUD 150 million over the four years to 2026–27.

Strengthening the foreign resident CGT regime

As a general position, a capital gain made by a non-resident is disregarded except where the relevant asset is "taxable Australian property" which includes (i) taxable Australian real property (TARP) and (ii) certain shares and other interests in entities that own TARP, referred to as indirect Australian real property interests (IARPI).

The paper comprises three complementary elements which apply to CGT events on or after 1 July 2025:

- Clarifying and broadening the types of assets to which foreign residents are subject to CGT;
- Amending the IARPI point-in-time principal asset test (PAT) to a 365-day look-back testing period; and
- Requiring foreign residents disposing of shares and other membership interests exceeding AUD 20 million in value to notify the Australian Taxation Office (ATO).

Clarifying and broadening the types of assets included in the CGT base

The proposed changes aim to address "ongoing uncertainty by clarifying and broadening" the types of land-related assets on which foreign residents are subject to CGT. The objective is stated as being to ensure Australia can tax gains on assets that have a close economic connection to Australian land and/or natural resources, while balancing broader foreign investment considerations.

The paper lists the following types of assets with a close economic connection to Australian land and/or natural resources:

- Leases or licenses to use land situated in Australia, including (but not limited to) pastoral leases and licenses, e.g., an agreement to lease land that is used in a manner that gives rise to the creation of emissions permits;
- Australian water entitlements in relation to land situated in Australia;
- Infrastructure and machinery installed on land situated in Australia, including land subject to a mining, quarrying, or prospecting right of an entity, e.g.:
    - Energy and telecommunications infrastructure, such as wind turbines, solar panels, batteries, transmission towers, transmission lines, and substations;
    - Transport infrastructure, such as rail networks, ports, and airports; and
    - Heavy machinery installed on land for use in mining operations, such as mining drills and ore crushers;
- An option or right to acquire one of the above assets (or similar asset types with a close economic connection to Australian land and/or natural resources); and
- A non-portfolio membership interest in an entity where more than 50% of the underlying entity's market value is derived from the above assets.

It is expected that the current rules relating to TARP and IARPI will be amended to include the additional assets as set out above. No consultation questions are raised with respect to the above.

Economic interests in TARP and other integrity matters

The paper poses two consultation questions relating to the application of the CGT regime in respect of "economic interests" in TARP. This is directed at how the Australian tax rules should deal with interests such as total return swaps which may generate an economic return with reference to TARP but do not necessarily involve the acquisition and disposal of TARP.

Extending the testing period for the PAT

The PAT in the IARPI definition currently operates at a point-in-time (the time of the CGT event). This will be extended to also require a look-back testing over the preceding 365 days.

That is, if more than 50% of the underlying asset value of the entity is attributable to TARP at the time of the CGT event or at any time during the preceding 365 days, the interest in the entity will satisfy the PAT requirement in the IARPI definition. This will more closely align the Australian tax law test with the equivalent treaty concepts in recent treaties.

No consultation questions are raised with respect to the above.

ATO notification of non-IARPI vendor declarations

Purchasers of TARP and IARPI from foreign resident vendors are required to withhold and remit to the ATO 12.5% (increasing to 15%) of the transaction proceeds. Currently, a purchaser does not need to withhold if the foreign resident has provided a vendor declaration to the purchaser that the membership interests to be disposed of are not IARPI, and the purchaser does not know this vendor declaration to be false at the time it is provided.

The paper addresses the proposal to introduce an ATO notification process for non-IARPI vendor declarations, for transactions with a value of greater than AUD 20 million. The paper proposes that if the ATO "disagrees with a vendor notification," the ATO can "recommend" to the vendor and purchaser that the non-IARPI vendor declaration be "withdrawn."

The objective is to give visibility to the ATO of such transactions, presumably so that the ATO can potentially disrupt the ordinary way in which the transaction is otherwise proceeding, where the ATO considers that the disposal may involve a disposal of IARPI.

In the absence of the provision of detailed information to the ATO, it is not clear how the ATO can form a view as to whether the non-IARPI vendor declaration is appropriate. Further, it is not clear how the proposed compliance process will sit alongside the normal conduct and completion of in-scope transactions.

Five consultation questions are raised with respect to this matter.

Improving the foreign resident capital gains withholding tax regime

The foreign resident capital gains withholding (FRCGW) tax regime imposes a non-final withholding obligation on the purchaser of TARP and IARPI acquired from a foreign resident vendor. Currently, the FRCGW does not apply where the market value of TARP or IARPI (relating to company title interests) is less than AUD 750,000

The measure would:

- Increase the withholding rate from 12.5% to 15%; and
- Remove the AUD 750,000 threshold.

These changes are expected to apply to acquisitions of relevant CGT assets made on or after 1 January 2025.

Impact on New Zealand

Under this proposed change, anyone investing in Australia, who is not an Australian tax resident, and sells an asset after 1 June 2025, could be affected by the expansion of the CGT net. While non-residents have been taxable on the sale of residential property (with limited ability to use a main home exemption), the rules are being expanded to capture a much wider range of land-related assets. For New Zealander's who are usually sheltered from the need to consider CGT, this consultation provides a glimpse of the additional complexities and boundary issues that can arise under a CGT.

The Australian tax landscape is changing rapidly, so if you currently invest in Australia, have assets in Australia, or are looking to invest or purchase assets in Australia in the future, we recommend discussing the tax implications with your usual Deloitte advisor.

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Cause for celebration? Minister uses modification power for GST remedial

By Viola Trnski and Allan Bullot

In the exciting and ever-changing world of tax, 26 July 2024 marked a historic day. The Minister of Revenue, for the first time, exercised a remedial power to modify an unintended outcome in the GST legislation.

Wait, what superpower?

Sections 6C-6G of the Tax Administration Act 1994 (the Act) were introduced in 2019 as an extension to the Commissioner's care and management powers. While it will be no surprise to anyone who has seen the size of a hard copy Income Tax Act 2007, Officials' acknowledged in a 2019 Regulatory Impact Statement:

> *"New Zealand's tax system is very complex, and it undergoes significant change regularly. The nature and volume of the tax law changes mean that unforeseen or unintended outcomes (legislative anomalies) arise often. This is likely to continue to be the case into the future given the increasing complexity of tax law and rapidly evolving business practices."*

On average, under the current approach, it takes 670 days after being identified for such "legislative anomalies" to be remedied through primary legislation. In that almost two-year period, taxpayers are required to continue filing returns, sometimes as often as every month for certain GST taxpayers, under the existing rules even if an unintended drafting error means the rules cannot or are not being interpreted as Parliament intended.

The solution? Sections 6C – 6G. These sections provide that the purpose of the modification power is to:

> *"...provide flexibility to temporarily remedy or mitigate the effect of a provision...by making a modification or granting an exemption when it is reasonably necessary –*
>
> a. *Due to an obvious error in the provision:*
> b. *To give effect to the intended purpose or object of the provision, to resolve ambiguity, or to reconcile inconsistencies."*

The word "reasonably" requires that an objective and reasonable third person would consider the modification necessary. The modification must also not be inconsistent with the intended effect of the provision.

This is one of many legislative safeguards that exist in the legislation to protect the rule of law (from, say, a hypothetical evil Minister of Revenue who wants to change all the "obvious errors" in the legislation to benefit their personal tax affairs).

Other restrictions and requirements of the amendment power include:

- **Limited time period** – a modification can not be effective for more than two years from the income year it comes into force (and, if retrospective, no more than five years prior)
- **Optional application** – taxpayers must have a choice to not apply the modification
- Must be the **most appropriate** way of addressing or resolving the issue at the time

- The extent of the modification must **not be broader than is reasonably necessary**
- A **consultative process** must be undertaken (generally, this will be six weeks of public consultation unless truncated or removed completely).

So, what's the process?

Generally, the main avenue for a remedial amendment is the annual rates tax legislation, which needs to be passed by 31 March of each year in order to enable tax collection for the following year.

However, from the time a legislative anomoly is identified, the road to include it in a remedial legislative amendment can be long and winding.

The modification powers bypass the usual legislative process by allowing the Minister to amend primary legislation using secondary legislation. In this case, the modification is made via an Order in Council and subsequently reported in the New Zealand Gazette. It is expected that a remedial amendment will also be included in the August tax bill, therefore, the modification that will act as a "band-aid" or temporary fix during the period before the next tax act is passed. In this case (the actual modification is summarised at the end of this article) the modification is revoked on 31 March 2025.

These clauses are also referred to as "Henry VIII clauses" as King Henry VIII was said to have an affinity for legislating via Royal Proclamations rather than through passing laws through Parliament (such a power to do so was conferred on him by the Statute of Proclamations 1539). While such clauses have been subject to criticism (or, in other words, been labelled as "constitutionally eyebrow-raising") for the power they confer to the executive branch of government, in this case, sections 6C-6G constrain these risks and allow necessary remedial amendments to be made in an efficient and timely manner – a welcome celebration for taxpayers.

What was the modification power actually used for?

The modification power is being used to amend an application provision regarding the GST apportionment rules where there has been a permanent change in use of the asset. The original wording, which was introduced by the Taxation (Annual Rates for 2022-23, Platform Economy, and Remedial Matters) Act 2023, stipulated that the provision applies "from a registered person's adjustment period starting on or after 1 April 2023".

However, due to a complex interplay between a number of sections in the Goods and Services Tax Act 1985, this potentially prevented some taxpayers who acquired an asset before 1 April 2023 from using the simplified adjustment calculation when there was a permanent change in use for that asset on or after 1 April 2023. The new wording makes it clear that the legislation should work as originally intended, by changing the provision so it applies "to a registered person's adjustment made in returns for taxable periods starting on or after 1 April 2023".

Inland Revenue is welcoming submissions on the proposed modification. Consultation closes on 12 August 2024. We expect that, following the two-week consultation period, the change will come into effect shortly thereafter.

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

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Royalties and your customs value: What does the Country Road decision mean for New Zealand importers?

By Jeanne du Buisson, Haidee Watkin and Sid Mahajan

After a long deliberation period, Justice Becroft has delivered his judgment in the High Court case Chief Executive of New Zealand Customs Service v Country Road Clothing (NZ) Limited [2024] NZHC 1696. This decision quashes an earlier 2022 Customs Appeal Authority decision, and rules in favour of New Zealand Customs (see below for a summary of the case).

The key issue in this case was whether the calculation of the price paid or payable by Country Road Clothing (NZ) Limited (CRNZ), for imported goods, should include certain licensing and royalty payments that relate to post importation activities. New Zealand Customs' view was that the royalties and licencing fees paid for intellectual property (shop layout, design and marketing) were sufficiently linked to the imported goods, as the royalty payments would not have been made if the goods were not imported, regardless of the mechanism for their calculation. CRNZ argued that the payments were for 'post-importation support' and did not relate to the price paid or payable for the imported goods. The Court found that the royalties paid by CRNZ to its parent company, Country Road Clothing Pty Ltd (CRAU) should have been included in the customs value of the imported goods. At the time of writing this we are not aware of any appeal to the decision, but this may still be in process.

It follows that New Zealand importers that pay for post-importation support under royalty/licence arrangements similar to those in the case should consider the impact of this High Court decision on their individual circumstance as this is likely to now be a focus area for New Zealand Customs. Furthermore, this decision may also come to the attention of other Customs Authorities around the world.

Therefore, if your business makes any royalty/licence payments and these payments are not included in the calculation of the customs value of the imported goods, now is a good time to get in touch with Deloitte to discuss the impact of this High Court decision.

Case summary

The summary facts are set out below:

- CRNZ is a wholly owned subsidiary of CRAU, an Australian company.
- CRNZ operates retail stores in New Zealand, primarily selling clothing.
- There is a commercial arrangement between CRNZ and CRAU, whereby CRNZ makes a payment to CRAU that relates to a comprehensive bundle of intellectual property governing aspects of CRNZ's retail operations (i.e., shop layout, design and marketing).
- Under the above arrangement, if CRNZ net profit exceeds the routine return, 75% of the excess is returned to CRAU as a royalty payment.
- Between 2015 and 2018, CRNZ did not include these payments in the customs value of the goods imported when self-assessing their customs duties.

Customs Appeal Authority - 2022

The Customs Appeal Authority (the Authority) accepted that in order to determine which payments made by CRNZ reflected the true value of the goods (and therefore what the customs value of the goods should be), each category of payment under the commercial arrangement between CRNZ and CRAU needs to be considered separately. In assessing the nature of the payments, the Authority also considered how those payments were quantified.

The Authority ultimately found that the price paid by CRAU to CRNZ for the actual goods were set by a transfer pricing regime, and therefore satisfied the obligation to calculate and pay the value received at an arm's-length. The Authority also found that there was 'no quantifiable nexus' between the value of the royalty payments and the cost or value of the imported goods. Accordingly, the Authority concluded that the royalty payments were a form of post-importation profit sharing, unconnected to the 'true value' of the goods, and therefore, they should be excluded from the customs value.

The decision was not accepted by New Zealand Customs and the matter was appealed to the High Court.

High Court - 2024

The High Court considered the key point in the case to be whether the three prior Court of Appeal decisions (*Adidas New Zealand, Avon Cosmetics and Nike*) adequately resemble the facts of the present case. Upon analysing these decisions, the High Court noted the decision was a 'finely balanced one', but ultimately ruled that the Authority adopted the incorrect test.

The High Court concluded that the royalty payments are within the scope of the 'true value' of the imported goods and therefore CRNZ's customs value should be adjusted to include the royalty payments. Four reasons for the decision were given:

1. The reality of the contractual arrangements between CRNZ and CRAU did not support clear separation between the royalty payments and the goods themselves;
2. Even if relying on the facts found by the Authority, the application of the three Court of Appeal decisions would indicate that the royalty payments should be considered part of the 'true value' of the imported goods;
3. Including the royalty payments as part of the 'true value' of the imported goods is consistent with the legislative purpose of the Customs and Excise Act 2018; and
4. Allowing the exclusion of some royalty/licensing payments would invite others to draft similar agreements/contracts to reduce customs duties, creating further uncertainty.

For more information, please reach out to your usual Deloitte advisor.

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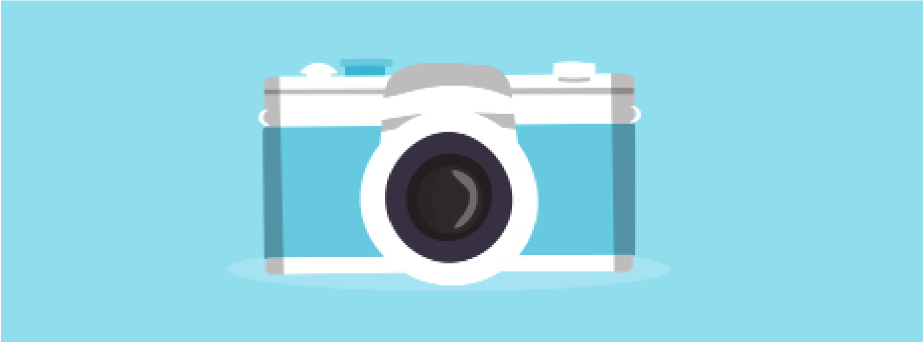
Snapshot of recent developments



Tax legislation and policy announcements

Information Release: Ministerial response to a petition on the increase of the GST threshold

On 3 July 2024, Inland Revenue released the Minister of Revenue's response to a petition to increase the GST threshold from $60,000 to $130,800. The response noted no increase would be made to the GST threshold as doing so is not the most effective way to support small businesses facing cost pressures.

Tax changes in effect from 1 July 2024

On 15 July 2024, Inland Revenue updated its website to reflect 1 July 2024 policy changes. The changes that have now been passed into law include:

- FamilyBoost
- 3% Government contribution to KiwiSaver for paid parental leave recipient
- Bright-line test reduced to two years
- Offshore Gambling Duty registration now available
- Paid parental leave rates change (from 15 July)

Inland Revenue statements and guidance

FamilyBoost

On 1 July 2024, Inland Revenue reminded parents that they should start collecting their early childhood education invoices to claim FamilyBoost later in the year. From mid-September, parents or caregivers can register for FamilyBoost in myIR. From the beginning of October, eligible households will be able to claim FamilyBoost for the July-September quarter, and every three months after that. More information on FamilyBoost is available here.

Determination: A type of attributing interest in a foreign investment fund for which a person may not use the fair dividend rate method

On 1 July 2024, Inland Revenue published FDR 2024/02: A type of attributing interest in a foreign investment fund for which a person may not use the fair dividend rate method (Colchester Multi-Strategy Global Bond Fund PLC – The Colchester Global Green Bond Enhanced Currency Fund- NZD Hedged Accumulation Class Z Shares).

The Determination states that section EX 46(10)(c) of the Income Tax Act 2007 would not apply to prevent the use of the fair dividend rate method for interests in the NZD Share Class (NZD denominated class of the Fund) but would apply if the Fund represented a separate foreign company and the NZD Share Class was the only class of share on issue.

The Determination applies for the 2024-2025 income year and subsequent income years.

Tailored tax codes

On 3 July 2024, Inland Revenue advised they will calculate and issue new certificates to existing tailored tax code taxpayers and their employees. This will affect around 7,700 taxpayers. Inland Revenue notified affected taxpayers (or their tax agent) on 9 July.

Technical Decision Summary: Interest-free loan and dividends (private ruling)

On 3 July 2024, Inland Revenue issued TDS 24/14: Interest free loan and dividends.

Company A was incorporated in New Zealand by Company C (a non-resident company) with nominal equity. Following its incorporation, Company A acquired all the shares in Company B from Company C in consideration for Company A issuing shares to Company C. The arrangement included an interest-free shareholder loan from Company C to Company A and the ongoing repayments of that loan.

At issue was: (1) whether the interest free loan gave rise to dividends to Company C from Company A; (2) whether repayment of the interest free loan was subject to withholding; and (3) whether sections BG 1 and GA 1 of the Income Tax Act 2007 apply to negate the outcomes of the above two issues.

The Tax Counsel Office concluded that: (1) The interest free loan from Company C to Company A does not give rise to a dividend from Company A to Company C under section CD 1 at any point in time, including as a result of the issue or repayment of the loan; (2) Company A was not required to withhold or pay an amount of tax under section RA 6 in relation to the interest free loan repayments made to Company C; and (3) sections BG 1 and GA 1 do not apply to negate or vary the above two tax outcomes.

Public Guidance Work Programme 2023-24

On 4 July 2024, Inland Revenue updated the Public Guidance Work Programme 2023-24. This is the final update for the 2023-24 year.

Recent tax fraud sentencing decisions

On 8 July 2024, Inland Revenue published a number tax fraud sentencing decisions:

- An individual with control over three companies was sentenced to community detention on tax fraud charges. Over a three-year period, PAYE was taken from employee's wages, but the money was never paid to Inland Revenue.
- An individual, who tried to get nearly $60,000 in COVID relief money, was sentenced to 11 months home detention. The person applied for three Small Business Cashflow Scheme Loans (SBCS)

for unrelated taxpayers (including one for their own company and one in their own name) when they knew they were not entitled to any of the money. The person also illegally accessed myIR accounts without authority.

- The owner of a food vending business was sentenced to a year's home detention for tax fraud. In 2019, the individual was charged with aiding and abetting two companies to file false or misleading GST returns, aiding and abetting two companies that failed to make PAYE deductions when required, and filing false personal tax returns. In 2021, they were charged again for evading or trying to evade the assessment or payment of GST, failing to make PAYE deductions and not providing information to Inland Revenue with the intention of evading the assessment or payment of tax. The Court was told the offending was not a temporary slip. It was premeditated, repetitive and prolonged with the conscious decision to provide false revenue information for tax returns for straightforward financial self-interest.

On 18 July 2024, Inland Revenue announced that an Auckland couple was sentenced to three years in prison on tax evasion charges. The couple, whose business activities were primarily housing construction, were found guilty of jointly committing 69 offences of personal income tax and GST evasion and failures to account for PAYE for their company.

The Judge found the overall evasion of income tax and GST amounted to about $750,000, with a further $80,000 in unaccounted-for PAYE. After some PAYE payments were made, the total loss was about $800,000. The Judge described it as deliberate offending in which business income was underreported through filing false returns. The offending happened between 2010 and 2015.

Determination: Amount of tax for a payment of a main benefit

On 10 July 2024, Inland Revenue issued DET 24/03: Determination under section RD 11(3) of the Income Tax Act 2007 of the amount of tax for a payment of a main benefit.

- For any payments made up to and including 1 August 2024, the amount of tax for a payment follows the M tax code rate set out in the Commissioner's PAYE tables that apply from 1 April 2024 to 30 July 2024.
- For any payments made on or after 2 August 2024, the amount of tax for a payment follows the M tax code rate set out in the Commissioner's weekly PAYE tables that apply from 31 July 2024.

Updated factsheets for GST on listed services

On 16 July 2024, Inland Revenue updated its factsheets on:

- GST on listed services - drivers, deliverers and accommodation owners - AD277
- GST on listed services - online marketplaces - AD278.

These include information on the new rules that took effect on 1 April 2024.

Inland Revenue have also developed a new GST on listed services factsheet for property managers and agents - AD282.

PAYE threshold changes 31 July 2024

On 18 July 2024, Inland Revenue announced an updated income tax threshold changes page, including information on the composite rates.

Updated PAYE tax tables, calculator, and a new IR330 declaration are also available.

On 26 July 2024 the Ministers of Finance and Revenue announced that most payroll software providers and employers were ready to implement the tax reductions.

Guidance for small value loans (transfer pricing)

On 18 July 2024, Inland Revenue published guidance for small-value loans (cross-border associated party loans by groups of companies for up to $10 million principal in total). Inland Revenue considers that 175 basis points (1.75%) over the relevant base indicator is broadly indicative of an arm's length rate in the absence of a readily available market rate for a debt instrument with similar terms and risk characteristics.

Deloitte Global Perspectives

Global Tax Policy Survey Report: The future in focus

The Deloitte Global Tax Policy Survey examined over 1,000 business leaders responses to current tax trends. Ranked from most to least impactful, the trends were transparency and reporting, digitalisation of tax, international tax reform, future of work, and climate and sustainability.

Stock-based compensation for an increasingly diverse workforce

Deloitte's survey of 1,750 early-career employees who receive company stock highlights how stock-based compensation can be used as a tool to meet talent objectives, attract and retain a diverse workforce, and enhance the employee value proposition.

OECD updates

Corporate Tax Statistics 2024

On 11 July 2024, the OECD released Corporate Tax Statistics 2024. The statistics include information on corporate taxation, multinational enterprise activity, and base erosion and profit-shifting practices.

The headline statistic is that average statutory corporate income tax rates have remained steady at 21.1% over the past three years. This follows a two-decade period that saw average statutory corporate income tax rates decline from 28% in 2000 to 21.1% in 2021.

OECD releases Secretary-General Tax Report to G20 leaders

On 25 July 2024, the OECD published the OECD Secretary-General Tax Report to the G20 leaders, covering key developments in international tax reform. The report highlights progress made on the Two Pillar Solution, tax transparency and administration, and BEPS.

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

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