



NEW ZEALAND

RECENT TAX DEVELOPMENT

Individual tax rate changes

Legislation enacted in December 2008 introduces a three-year programme of personal tax cuts, with the first round starting on 1 April 2009, as follows (changes in bold):

Income (NZ\$)	Tax rates from 1 April 2009
0 – 14,000	12.5%
14,001 – 48,000	21%
48,001 – 70,000	33%
70,001 and over	38%
Income (NZ\$)	Tax rates from 1 April 2010
0 – 14,000	12.5%
14,001 – 50,000	21%
50,001 – 70,000	33%
70,001 and over	37%
Income (NZ\$)	Tax rates from 1 April 2011
0 – 14,000	12.5%
14,001 – 50,000	20%
50,001 – 70,000	33%
70,001 and over	37%

International tax rules review

Changes to the way in which income derived from investments in foreign subsidiaries is taxed are included in the Taxation (International Tax, Life Insurance and Remedial Matters) Bill (the Bill) that is expected to be enacted in mid-2009.

The key change is the exemption from New Zealand income tax for active income derived by New Zealand residents from interests in controlled foreign companies (CFCs). Passive income (such as dividends, interest, royalties and rents) will be taxed on an attribution basis.

For CFCs that pass an “active business” test, no income from the CFC will be attributable to taxpayers with an interest in that CFC. A CFC will pass the active business test if its passive income is less than 5% of gross income. The active business test will replace the current grey list exemption. A CFC that fails the active business test will attribute only passive income to taxpayers under the CFC rules. An exemption from attribution of income will be retained for CFCs in Australia that meet certain criteria.

Other changes include:

1. Extending the current thin capitalisation rules to New Zealand companies that are controlled by New Zealand residents and have interests in CFCs. However, the new rules will not apply where the New Zealand residents have 90% or more of their assets in New Zealand or less than NZ\$250,000 of interest deductions;
2. Amending the definitions of “debt” and “assets” for thin capitalisation purposes by treating fixed rate shares issued by a foreign company to New Zealand taxpayers as debt, excluding equity investments in CFCs from assets and aligning the definition of debt for the worldwide group with that for the New Zealand group;
3. Exempting most foreign dividends received by New Zealand companies from domestic tax, unless the dividends are received on fixed rate shares for which the CFC has received a tax deduction in its home jurisdiction or the dividends are from portfolio foreign investment funds (FIFs) (i.e. interests under 10%) that are exempt from the FIF rules (e.g. interests in Australian listed companies);
4. Repealing the foreign dividend payment and underlying foreign tax credit rules; and
5. Abolishing the conduit tax relief regime.

Once enacted, the new rules are expected to apply from the start of the 2009/10 income year, although the application date may be deferred.

United States – New Zealand double tax agreement

The Governments of New Zealand and the US signed a Protocol in December 2008 updating the double tax agreement (DTA) between the two countries. The Protocol amends the withholding tax rates on dividends, interest and royalties.

New Zealand

The table below compares the current withholding tax rates with the rates agreed to in the Protocol.

	Current DTA	Protocol
Dividends	15%	0 – 10% shareholding: 15% 10 to 80% shareholding: 5% > 80% shareholding: 0%
Interest	10%	0% – payable to eligible institutions 10% – other
Royalties	10%	5%

A number of criteria must be met within the amended Dividend and Limitation on Benefits articles in the DTA before a taxpayer is able to obtain the lower withholding tax rates.

The Protocol will come into force once it is ratified by both countries.

Philippines — New Zealand double tax agreement

The DTA between New Zealand and the Philippines has been updated with effect from 1 December 2008. The key changes to the DTA are:

1. The withholding tax rates on dividends and royalties have been lowered from a split rate of 15% and 25% to a flat rate of 15%; and
2. The withholding tax rate on interest has been reduced from 15% to 10%.

Research and development tax credit

Legislation enacted in December 2008 repeals the research and development (R&D) tax credit with effect from the 2009/10 income year. The credit will remain available for qualifying expenditure on R&D activities carried out in the 2008/09 income year.

Life insurance tax reform

The Bill makes comprehensive changes to the taxation of life insurance businesses.

Income from a life insurer's life business will be separated into shareholder income (income earned by the equity owners of the company) and policyholder income (income earned for policyholders from life insurance savings products).

Under the new rules, shareholder income will be taxed at the corporate rate in a similar manner to the way other businesses are taxed. The current portfolio investment entity rules will apply to policyholder income, allowing savers in life products to be taxed on their investment income at a maximum rate of 30%.

The new rules are currently set to apply for income years starting on or after 1 April 2009, although the application date may be deferred. However, a number of transitional rules will apply for life insurance products entered into prior to the new rules taking effect.

Petroleum mining

On 4 March 2008 the Government announced legislative changes to ensure that expenditure on petroleum mining operations undertaken through a foreign branch cannot be offset against petroleum mining income from New Zealand.

The changes are included in the Bill and, once enacted, will be effective from 4 March 2008, the date of the announcement. Expenditure incurred before 4 March 2008 will not be affected by the changes.

Emissions Trading Scheme

Legislation enacted in September 2008 establishes the New Zealand Emissions Trading Scheme.

The scheme operates alongside other measures to reduce greenhouse gas emissions. Participants in the scheme will be able to trade emissions units, within New Zealand and internationally, to cover their expected future emissions obligations.

The income tax legislation has been amended to provide for the tax consequences of transactions in emissions units related to forestry businesses. Legislation in relation to the income tax treatment of emissions units outside the forestry sector is included in the Bill.

The Government has established an Emissions Trading Scheme Review Committee to review the Emissions Trading Scheme and related matters. The Committee will examine the relative merits of an emissions trading scheme and a tax on carbon or energy as a New Zealand response to climate change.

Stapled securities

The Government has announced changes to the tax treatment of certain types of stapled securities. Under the new rules, stapled securities will be treated as equity for tax purposes, meaning that no deduction for interest payments will be available. Once enacted, the changes will be effective from 25 February 2008, the date of the announcement.

Relocation costs

The Bill, introduced in July 2008, provides that most relocation costs and overtime meal allowances paid by employers to employees are exempt from income tax and fringe benefit tax (FBT). Once enacted, the changes will apply retrospectively from the 2002/03 income year.

A draft Determination released in December 2008 sets out a list of relocation expenses likely to be eligible for treatment as non-taxable income in the hands of employees.

Provisional tax

The Government is reducing the provisional tax uplift rates for the 2008/20 and 2009/20 income years from:

1. 105% to 100% for taxpayers calculating their provisional tax obligations on the basis of their previous year's income;
2. 110% to 105% for taxpayers calculating their provisional tax obligations on the basis of their income from the year before last; and
3. 100% to 95% and 95% to 90% for "transitional provisional taxpayers" (companies and other entities subject to the 30% tax rate).

These changes are included in the recently enacted Taxation (Business Tax Measures) Act and applied from 1 April 2009.

Imputation

A 2008 Government Discussion Document considers two issues relating to the imputation credit rules: (1) whether the Government should change the rules to allow the streaming of imputation credits in some circumstances and (2) whether imputation credits should be refunded to charities and other tax exempt entities. The Government indicated that this is the first step in a process of consultation on ways of improving the imputation system. It also said that the outcome of the review would be influenced by the possibility of New Zealand entering negotiations with Australia to establish a system of mutual recognition of New Zealand imputation and Australian franking credits for trans-Tasman investment.

Associated persons

The Bill introduces significant changes to the definitions of associated person in the income tax legislation. The key changes are:

1. A standardised definition of associated person (subject to modifications for the purposes of the land taxing provisions).

2. New tests associating a trustee and a settlor and the trustees of two trusts that have the same settlor;
3. Tighter rules for aggregating the interests of associates;
4. A tripartite test associating two persons if they are each associated with the same third person (limited in certain circumstances); and
5. A new approach for dividends and FBT.

Once enacted, the new rules are likely to apply from the 2009/10 income year. In the land context, the new rules are likely to apply to land acquired on or after 1 April 2009 regardless of the taxpayer's balance date, although the application date may be deferred.

