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WEEKLY COMMENT: FRIDAY 11 OCTOBER 2013

1. The *Taxation (Livestock Valuation, Assets Expenditure, and Remedial Matters) Act 2013* ("the Assets Expenditure Tax Act") enacted on 17 July 2013 contains new GST rules to allow certain non-resident businesses to register for GST and claim input tax deductions for GST incurred on approximately the same basis as a resident registered person. The rules apply from 1 April 2014.

2. I previously discussed these rules as first introduced in the corresponding Tax Bill in *Weekly Comment* 28 September 2012. The rules as enacted, following the review by the Finance and Expenditure Committee, are substantially different in some respects from the rules that were initially proposed. Therefore, this week, I take another look at:

   (a) The new GST grouping rules;

   (b) The new timing rules for entry and exit;

   (c) The new GST registration requirements for non-residents;

   (d) The new rules for cancellation of GST registration;

   (e) The new rules for non-residents claiming deductions;

   (f) The GST accounting basis for non-residents; and

   (g) The zero-rating of certain goods supplied to an unregistered non-resident.

The new GST grouping rules

3. The most significant alteration from the rules as initially proposed is that cross-border groups will be allowed. In the rules as originally proposed, non-residents registered under proposed section 54B would only be able to group-register with other companies registered under that section (in other words, form wholly non-resident groups).

4. Officials' concern, as stated in pages 103-104 of the *Officials' Report to the Finance and Expenditure Committee on Submissions on the Bill* ("the Officials' Report") was that:

   "If cross-border groups were allowed, when a representative member filed a GST return on behalf of the group, it would be possible for what are effectively GST refunds to non-residents to be masked by the activities of a broader group that included New Zealand residents. Grouping with a New Zealand resident could also be used by non-residents as a method of accounting for GST on an invoice basis – a basis that is more susceptible to fraud because GST refunds are provided on invoices issued, rather than cash paid."

5. Officials accepted that there are sometimes legitimate reasons for forming cross-border groups and recommended that:

   (a) Only non-residents that make *no* taxable supplies in New Zealand can register for GST under new s. 54B – the requirement now contained in s. 54B(1)(d)(i) is that the non-resident person is not carrying on a taxable activity in New Zealand, or intending to carry on a taxable activity in New Zealand; and

   (b) Non-residents that make taxable supplies in New Zealand under the compulsory registration threshold would not be able to use s. 54B but would be able to voluntarily register under the existing registration provisions. This voluntary registration option would also apply to a non-resident that either did or did not make taxable supplies and wished to form a group with companies that made taxable supplies: new s. 54B(1)(d)(ii) provides that the non-resident person is not, and does not intend to become, a member of a group of companies that is carrying on a taxable activity in New Zealand; and

   (c) If a non-resident registered under section 54B starts making taxable supplies, they will be treated as being registered under the existing domestic rules: new s. 54B(2) provides that if a non-resident person who is registered under s. 54B starts making taxable supplies, or becomes a member of a group of companies that is making taxable supplies, they are treated as:

      (i) Registered on the date specified by the Commissioner under s. 54B(1); and

      (ii) Not being registered under s. 54B from the date on which they start making taxable supplies, or the date on which they join the group, as applicable.

6. It is stated in the Officials' Report that:

   "This would give a non-resident the option of either registering under section 54B or joining a group with a New Zealand resident and that group would be subject to the standard rules. The advantage of this solution is that non-residents that chose to group-register with a New Zealand company would have to show that any input deductions claimed were linked to taxable supplies made in New Zealand (rather than their worldwide business) in order to access refunds. This is consistent with the current situation and officials do not consider there is a significant revenue risk attached to it. On the flip side, the solution still allows non-residents in a pure refund position to register under the proposed rules and claim input deductions based on their worldwide supplies."

The new timing rules for entry and exit

7. Consistent with the new distinction between non-residents who can register under the new rules and those who cannot (due to making taxable supplies in New Zealand or are part of a New Zealand group of companies), s. 54B(3) states that for timing purposes, the following days are treated as the end of a taxable period:

   (a) The day on which a non-resident person ceases to be eligible to be registered under s. 54B; and

   (b) The day on which a non-resident person who is otherwise registered becomes registered under s. 54B.

The new GST registration requirements for non-residents

8. The complete new rules for GST registration of non-residents in s. 54B are that the Commissioner may register a non-resident who has not become liable to be registered under s. 51(1) if the Commissioner is satisfied that then person meets the following requirements:

   (a) The non-resident is registered for a consumption tax in their country of residence, or if that country does not have a consumption tax, *or has a consumption tax that does not apply to the non-resident person's activities, the non-resident has a level of activity in a country or territory* that would render them liable to be registered in New Zealand under s. 51(1) if they were carrying out the taxable activity in New Zealand (because the value of their supplies would exceed the registration threshold); and

   (b) The amount of the non-resident's input tax for the first taxable period after the date of registration in New Zealand is likely to be more than $500; and

   (c) The non-resident's taxable activity does not involve a *performance* of services in relation to which it is reasonably foreseeable that the *performance* of the services will be received in New Zealand by a person who is not GST-registered; and

   (d) The non-resident:

      (i) Is not carrying on a taxable activity in New Zealand, or intending to carry on a taxable activity in New Zealand; and

      (ii) Is not, and does not intend to become, a member of a group of companies that is carrying on a taxable activity in New Zealand.

9. In relation to the requirement referred to in paragraph 8(a) above, officials agreed with a submission that the person may live in a jurisdiction that has a consumption tax, but not be required to register for that tax because their activities are outside the tax base. Therefore, officials considered the wording should be amended so that a non-resident can register in New Zealand if their country of residence has a consumption tax that does not apply to their activities, but they have a level of activity that would render them liable to be registered in New Zealand.

The new rules for cancellation of GST registration

10. The new rules for cancellation of a non-resident's registration are contained in s. 54C, which provides that the existing cancellation rules in s. 52 apply to the cancellation of a non-resident's registration under s. 54B, as modified by s. 54C. Under s. 52(5) and s. 52(5A), the Commissioner may, even if not notified, cancel the person's registration:

    (a) From the last day of the taxable period in which he is satisfied that all taxable activities have ceased [s. 52(5)]; or

    (b) From the date of the person's registration if he is satisfied that no taxable activities were in fact carried on [s. 52(5A)].

11. The existing rule in s. 52(7) that the 'taxable activities' referred to in s. 52(5) and 52(5A) are taxable activities carried on in New Zealand is to apply only to non-resident persons who are not registered under the new s. 54B. Therefore, non-residents who are registered under s. 54B will not be required to de-register if taxable activities are not carried on in New Zealand.

12. Section 54C expands on the Commissioner's powers to cancel registration under s. 52(5) and 52(5A). The Commissioner may cancel a non-resident's registration if:

    (a) The Commissioner is satisfied that the non-resident no longer meets the requirement in s. 54B(1)(a) - that the non-resident is registered for a consumption tax in their country of residence, or if that country does not have a consumption tax, *or has a consumption tax that does not apply to the non-resident person's activities, the non-resident has a level of activity in a country or territory* that would render them liable to be registered in New Zealand under s. 51(1) if they were carrying out the taxable activity in New Zealand (because the value of their supplies would exceed the registration threshold); or

    (b) The non-resident has not filed a return or has filed late returns for 3 consecutive taxable periods, in which case:

        (i) The cancellation date is the first day of the third taxable period; and

        (ii) The non-resident and associated persons will be barred from becoming GST-registered again for at least 5 years from the date of cancellation.

13. The requirement in the rules as originally introduced that a New Zealand registered person who becomes non-resident be deregistered if the requirements of s. 54B(1) are not met after becoming non-resident has been removed.

14. When a non-resident ceases to be a registered person, new s. 5(3B) states that:

    (a) Goods that are part of the assets of the non-resident's taxable activity, that are present in New Zealand at the time the non-resident ceases to be registered, are treated as supplied by the non-resident in the course of the taxable activity immediately before the cessation of registration; and

    (b) Services that would be *performed* in New Zealand as part of the non-resident's taxable activity, at the time the non-resident ceases to be registered, are treated as *performed* by the non-resident in the course of the taxable activity immediately before the cessation of registration. (The rules as originally introduced referred to a "supply" of services.)

15. It is stated in the Officials' Report that s. 5(3B) is intended to be concessionary. Without it, officials consider there is an argument that a non-resident that registered for GST and the deregistered would need to account for output tax on the value of its worldwide assets. Therefore, the purpose of s. 5(3B) is to limit New Zealand's taxing right to goods and services that logically form part of the non-resident's New Zealand activities (if there are any). However, officials considered that output tax on services that have already been supplied in accordance with the time of supply rules should be returned, even though the non-resident will only be registered on a payments basis. The services caught by this provision should be the services performed in New Zealand prior to deregistration.

16. The market value rule in s. 10(7A) – that the consideration for the supply is treated as being the open market value of the supply - applies to supplies treated as made under s. 5(3B).

The new rules for non-residents claiming deductions

17. Under new s. 20(3L), *a non-resident person who is registered under s. 54B* may deduct input tax to the extent to which the goods or services are used for, or are available for use in, making taxable supplies, *treating all supplies made by the person as if they were made and received in New Zealand*.

18. This rule means that if a non-resident makes supplies that would be exempt supplies if made in New Zealand, input tax cannot be deducted to the extent that such supplies are made.

19. However, a concession has been introduced for suppliers of financial services. Under new s. 20(3M), a non-resident person who is registered under s. 54B and who principally makes supplies of financial services may, for the purposes of calculating the amount of input tax, choose to use a fair and reasonable method of apportionment agreed with the Commissioner as set out in existing s. 20(3E) – in other words, the same rule that applies to New Zealand resident suppliers of financial services.

The GST accounting basis for non-residents

20. New s. 19(1B) states that a non-resident person who is registered under s. 54B must account for tax payable on a payments basis. New s. 19A(1)(iv) requires the Commissioner to direct a non-resident person to account for tax payable on a payments basis.

21. It is stated on page 45 of the *Commentary* on the Bill at the time it was introduced that this rule "is designed to limit the possibility of a non-resident claiming a refund on the basis of invoices provided by registered residents on which no payment is made and, therefore, no GST is paid". Note, however, that this will only apply to non-residents registered under s. 54B, and not to non-residents making taxable supplies in New Zealand or who are registered as part of a group of companies.

22. New s. 46(1B) extends the period from 15 days to 90 days after a non-resident's GST return was received by the Commissioner for the purposes of:

    (a) Refunds to be paid by the Commissioner;

    (b) The period within which the Commissioner must give a request for information concerning a return; and

    (c) The period within which the Commissioner must give notice of an intention to investigate the return or withhold payment.

23. It is stated in the Officials' Report that:

    "Officials consider the 90-day period to be appropriate. There is an increased fraud risk associated with providing refunds to non-residents. This risk exists because, unlike residents, Inland Revenue has limited ability to accurately track down and recover money from non-residents when a refund is released in error.

    Having a longer timeframe for releasing refunds is considered preferable to having a shorter timeframe that the Commissioner may be more inclined to extend if doubts exist over the legitimacy of a claim. Officials consider that 90 days is a more realistic timeframe to allow the Commissioner to adopt a considered opinion on whether a refund will be released."

24. A related change to s. 120C of the *Tax Administration Act 1994* will mean that use of money interest on GST refunds to a non-resident will not start from 15 days after a non-resident provides a GST return.

25. There are no special rules for taxable periods for non-residents, so the usual rules will apply.

Zero-rating of certain goods supplied to an unregistered non-resident

26. New s. 11(1)(p) provides for goods supplied to an unregistered non-resident recipient to be zero-rated if those goods are: jigs, patterns, templates, dies, punches, and similar machine

tools to be used in New Zealand solely to manufacture goods that will be for export from New Zealand.

27. Officials declined a submission that the start date of this rule be brought forward from 1 April 2014 on the basis that:

"Officials consider these changes form a package of cross-border initiatives with the proposed registration system for non-residents mentioned above. For that reason, it is considered desirable for both rules to be effective from the same date."

Arun David, Director,

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