



CHARTERED ACCOUNTANTS
AUSTRALIA + NEW ZEALAND

DavidCo Limited
CHARTERED ACCOUNTANTS

Level 2, Shortland Chambers
70 Shortland Street, Auckland
PO Box 2380, Shortland Street
Auckland 1140
T +64 9 921 6885
F +64 9 921 6889
M +64 21 639 710
E arun.david@davidco.co.nz
W www.davidco.co.nz

WEEKLY COMMENT: FRIDAY 1 APRIL 2016

1. This week and next week I review the property taxation amendments proposed in the version of the *Taxation (Residential Land Withholding Tax, GST on Online Services, and Student Loans) Bill* as reported from the Finance and Expenditure Committee on 21 March 2016 (“the RLWT Bill as Reported”).
2. I reviewed the Bill as introduced on 16 November 2015 in *Weekly Comment* 11 March 2016. There have been a number of changes so I have decided to re-review the RLWT rules in their entirety over this week and next week.
3. This week I review the imposition and obligation to pay RLWT and the 3 conditions for RLWT to be imposed. Next week I look at the operation of the RLWT rules, the calculation of RLWT, tax credits and refunds, information requirements and certificates of exemption.
4. The amendments relating to residential land withholding tax (“RLWT”) are contained in Part 2 (clauses 34 to 45 which contain the amendments to the *Income Tax Act 2007*) and Part 4 (clauses 72 and 74 containing the amendments to the *Tax Administration Act 1994*) and come into force on 1 July 2016.
5. Officials have commented in the *Officials’ Report to the Finance and Expenditure Committee on Submissions on the Bill* (“the Officials’ Report”) that the 1 July 2016 commencement date applies to a payment of a “residential land purchase amount” that is subject to RLWT (as explained in paragraph 29 onwards below). Therefore, where the vendor enters into an agreement to dispose of residential property before 1 July 2016 but settlement occurs after 1 July 2016, RLWT will apply even though the bright-line date was before 1 July 2016.

When land is acquired when an option is exercised

6. As I noted in *Weekly Comment* 18 March 2016, the acquisition date of land under s. CB 15B is relevant for determining whether land is acquired before or after 1 October 2015 for the purpose of applying the bright-line test.
7. As part of the amendments in the RLWT Bill as Reported, s. CB 15B(3) has been replaced with effect from 22 November 2013. Replaced s. CB 15B(3) states that a person that exercises an option to acquire land and acquires the land is treated as acquiring the land at the time when they exercise the option. Officials have commented in the Officials’ Report that this will clarify that the first interest in the land is acquired at the time the option is exercised, irrespective of whether the person previously held a different interest in the land such as a leasehold interest.

Imposition of the obligation to pay RLWT

8. RLWT is imposed under proposed subpart RL in cl. 44 of the RLWT Bill as Reported.

9. Under s. RL 1(2), subpart RL applies, and RLWT would be imposed, if income under the bright-line test in s. CB 6A would arise, regardless of whether or not income would arise under any of the other land tax provisions in ss. CB 6 to CB 12 (i.e. ignoring the rule in s. CB 6A(6) which states that s. CB 6A will not apply if any of ss. CB 6 to CB 12 apply) and ignoring the main home exclusion in s. CB 16A:
- (a) For a vendor who is an “offshore RLWT person”; and
 - (b) In relation to a “residential land purchase amount” (see paragraph 29 onwards below); and
 - (c) In relation to a disposal of “residential land” (as discussed in paragraph 13 onwards in *Weekly Comment* 19 February 2016) located in New Zealand.
10. Officials have commented in the Officials’ Report that RLWT will only apply if all of three conditions have been met: the land being disposed of is residential land, the land is being disposed of within two years of acquisition, and the vendor is an offshore person. If the vendor is outside the scope of RLWT on one of the conditions, RLWT will not apply. The legislation does not stipulate which condition should be checked first. In some cases, it will be easiest to first determine the residential land requirement, in some cases, the two-year disposal requirement, and in other cases, whether the vendor is an offshore person.
11. There is now a rule that divides disposals between co-owners for the purposes of RLWT. Section RL 1(2B) in the RLWT Bill as Reported states that vendors who are co-owners are treated as disposing of separate residential land based on an appropriate split of the residential land and the consideration for its disposal.
12. There is also a new rule that provides for an RLWT certificate of exemption to be issued by the Commissioner – see paragraph 55 onwards in next week’s *Weekly Comment* 8 April 2016.
13. The following points were made in the Explanatory Note to the RLWT Bill as introduced:
- (a) There will be an exemption for disposals of inherited property as well as relief for relationship property; and
 - (b) It is proposed to impose RLWT at the point in time when New Zealand land is sold by an offshore vendor.
14. It is stated in the *Commentary on the Bill* (“the Commentary”) that the obligation to retain/withhold and pay RLWT is intended to arise upon settlement when, in most cases, the bulk of the purchase price will be paid by the purchaser to the vendor via a conveyancing agent. At this point the RLWT paying or withholding agent should retain or withhold RLWT from the funds being paid.
15. It is also stated in the Commentary that RLWT must be paid before other disbursements made as part of the settlement process – for example, mortgages. This is so RLWT cannot be easily circumvented by gearing up before disposal of the residential property.

First condition: income under s. CB 6A ignoring sections CB 6A(6) and CB 16A

16. It is stated in the Commentary that:
- (a) The reference to “income” under the bright-line test means that there will not need to be a land title transfer for an RLWT obligation to arise; there will only need to be a residential

land purchase amount - off-the-plan sales, for example, will be subject to RLWT if other conditions are also met.

(b) There will be an exemption or rollover relief from RLWT for inherited property and for transfers of relationship property, as provided under the bright-line test, which is achieved under s. RL 1(2)(a), which refers to an amount that is, or would be “income” under s. CB 6A.

17. It is noted by a submitter in the Officials’ Report that while there is a specific exemption in s. CB 6A(5) for disposals by a deceased person’s personal representative or beneficiaries, there is no specific exemption for relationship property because the disposals and acquisitions occur at cost. Officials responded that they do not consider a specific provision relating to relationship property agreements is necessary for the purposes of RLWT as it may raise questions about the application of the income tax provisions regarding relationship property agreements in other areas. However, officials considered further guidance in this area would be useful for conveyancers and lawyers required to administer RLWT.

18. It is also stated in the Commentary that a disposal of New Zealand residential land that is income for the vendor under both s. CB 6A and another provision of the *Income Tax Act 2007* (for example, the intention test) will be subject to RLWT. This has now been clarified in the revised legislation: s. RL 1(2)(a) refers to income under s. CB 6A “ignoring s. CB 6A(6) and s. CB 16A”:

(a) Section CB 6A(6) is the “override” provision that states that s. CB 6A applies only if none of sections CB 6 to CB 12 apply – this is “switched off” for the purpose of determining whether there is an obligation to deduct RLWT; and

(b) Section CB 16A is the main home exclusion, which is also “switched off” – however, officials have noted in the Officials’ Report that people eligible for the main home exclusion could apply for a certificate of exemption from RLWT under the new certificate of exemption rules – discussed in **paragraph 55** onwards in next week’s *Weekly Comment* 8 April 2016.

Second condition: who is an offshore RLWT person

19. The RLWT Bill as Reported contains some significant changes to the definition of an offshore person for RLWT purposes, and introduces the new term “offshore RLWT person” to distinguish the definition from the definition of “offshore person” for information collection purposes (i.e. for the purposes of who should complete a tax statement) discussed in *Weekly Comment* 12 February 2016.

20. Under the new definition, in cl. 45 of the RLWT Bill as Reported, to be inserted into s. YA 1 of the *Income Tax Act 2007*, “offshore RLWT person” means:

(a) A natural person, if:

(i) The person is a New Zealand citizen who is outside New Zealand and they have not been in New Zealand within the last 3 years;

(ii) The person holds a residence class visa granted under the *Immigration Act 2009*, and they are outside New Zealand and have not been in New Zealand within the last 12 months;

- (iii) The person is not a New Zealand citizen and they do not hold a residence class visa granted under the *Immigration Act 2009*;
 - (iv) For the purpose of determining whether a New Zealand citizen or a person holding a residence class visa is outside New Zealand, officials have commented in the Officials' Report that presence in New Zealand for part of one day would satisfy the requirement not to be an offshore person.
- (b) A person that is a trustee of a trust (note: the fact that a settlor may be an offshore person or offshore RLWT person will not automatically result in the trustee being treated as an offshore RLWT person) if:
- (i) More than 25% of the trustees of the trust are offshore RLWT persons (this means that a trust will not automatically be an offshore RLWT person if any of the trustees is an offshore RLWT person);
 - (ii) More than 25% of the people that have the power to appoint or remove a trustee of the trust, or to amend the trust deed are offshore RLWT persons (this means that a trust will not automatically be an offshore RLWT person if any person with a power of appointment is an offshore RLWT person);
 - (iii) All natural person beneficiaries and all natural person discretionary beneficiaries of the trust are offshore RLWT persons – apparently to prevent a trust with all offshore natural person beneficiaries being set up with a New Zealand charity appointed as a discretionary beneficiary and thereby avoid the RLWT rules;
 - (iv) All beneficiaries and all discretionary beneficiaries of the trust are offshore RLWT persons;
 - (v) A beneficiary, including a discretionary beneficiary, that is an offshore RLWT person has received a distribution from the trust in 1 of the last 4 years before the relevant disposal of residential land and, if the beneficiary is a natural person, the total distributions to the beneficiary for the relevant year are more than \$5,000;
 - (vi) The trust has disposed of residential land within 4 years before the relevant disposal of residential land and the trust has a beneficiary, including a discretionary beneficiary, that is an offshore RLWT person – these last four rules relating to beneficiaries are meant to avoid the gain escaping tax by being shifted to an offshore beneficiary as beneficiary income.
- (c) A person, if:
- (i) The person is incorporated outside New Zealand;
 - (ii) The person is not a natural person and is registered outside New Zealand;
 - (iii) The person is constituted under foreign law;
 - (iv) The person is a company or a partner in a limited partnership and more than 25% of the company's directors or of the limited partnership's general partners are offshore RLWT persons (this means that a company will not automatically be an offshore RLWT person if a director or a partner is an offshore RLWT person);

- (v) The person is a company and more than 25% of the company's shareholder decision-making rights are held directly or indirectly by offshore RLWT persons;
- (vi) The person is a partner in a limited partnership or an owner of an effective look-through interest in a look-through company ("LTC") and more than 25% of the partnership's partnership shares or of the LTC's effective look-through interests are held directly or indirectly by offshore RLWT persons.

21. As noted in *Weekly Comment* 11 March, it is stated in the Commentary in relation to individuals that:

- (a) A New Zealand citizen or a holder of a residence class visa could meet with their New Zealand conveyancing agent and satisfy the requirement that they are not an offshore RLWT person.
- (b) An individual selling their property from outside New Zealand could provide, a certified statement or other suitable proof to their conveyancing agent that they are not an offshore person.
- (c) The withholding tax will apply when two or more individuals jointly own a property, and at least one of them is an offshore person, however, in this case the new rule in s. RL 1(2B) in the Reported Back Bill would apply so that vendors who are co-owners are treated as disposing of separate residential land based on an appropriate split of the residential land and the consideration for its disposal.

22. Officials consider that because the RLWT obligation will be triggered when there is a residential land purchase amount, it will need to be determined at the time of payment of the residential land purchase amount whether or not the vendor is an offshore person. This means that the three-year (for New Zealand citizens) or 12-month (for holders of residence-class visas) period immediately preceding the payment of the residential land purchase amount will be the relevant period.

23. In relation to Australian citizens, officials commented that an Australian citizen holding a resident visa endorsed with travel conditions, a permanent resident visa, or New Zealand citizenship can show that they are not an offshore person by looking back at the previous 12 months or three years depending on the circumstances. However, other Australian citizens (those whose resident visas expire upon departure) will need to be physically present in New Zealand on the day of the residential land purchase amount to satisfy the requirement.

24. In relation to companies, officials have confirmed in the Officials' Report in relation to the revised requirements relating to non-individuals that are offshore RLWT persons, that:

- (a) A company could satisfy the proof requirement by evidence such as:
 - (i) A copy of the company's New Zealand registration (although officials commented that incorporation or registration in New Zealand will not by itself exclude a company from being an offshore RLWT person); and
 - (ii) Certification by a New Zealand resident director that the percentage of directors offshore does not exceed 25%; and
 - (iii) A statement from a single New Zealand director that, to their knowledge, no more than 25 percent of the shareholder decision-making rights of the company are held by offshore persons.

- (b) A corporate trustee will be able to qualify for the non-offshore exemption if it meets both the company and the trust criteria listed in paragraph 20(b) and 20(c) above.
25. Officials have noted in the Officials' Report that it may be difficult to provide evidence of the offshore status of all shareholders in some situations, but a statement by a New Zealand director would provide integrity as this statement would be information provided in relation to a tax law, which means that the New Zealand director would be subject to criminal penalties, if they knowingly provide false information.
26. In relation to limited partnerships, officials have commented in the Officials' Report that:
- (a) Officials agree that the percentage test should apply to limited partners in the partnership in the same way as it is for shareholdings in companies.
 - (b) The requirements that apply to directors of companies should similarly apply to general partners of limited partnerships.
 - (c) In relation to partnerships, the independent specialist tax advisor to the Finance and Expenditure Committee has suggested that the test be amended so that a partnership will be an offshore person only if more than 25 percent of the partners are themselves offshore persons. Further, to address officials' concerns in relation to the misuse of partnerships, she recommended that a partnership should also be an "offshore person" if more than 25 percent of the voting interest, or income interest, is allocated to the offshore partner(s).
 - (d) In the case of a limited partnership, the general partner would be required to certify the partnership share percentage.
 - (e) In the case of a standard partnership, officials consider that one of the New Zealand partners would be required to make the certification.
 - (f) The independent specialist tax advisor to the Finance and Expenditure Committee has raised concerns in relation to the RLWT implications of changes in partners in the partnership and officials agree that Inland Revenue should develop guidance on this matter.
27. Officials note that it would be consistent for the same approach (a 25 percent threshold, a restriction on streaming interests in the property and certification by a New Zealand co-owner) to apply in the case of co-owners of a property – however this is not reflected in the revised legislation in the RLWT Bill as Reported.
28. In relation to trusts, officials have commented as follows in the Officials' Report:
- (a) In relation to settlors: Officials agree that the reference to settlors should be replaced by a person who has the power to appoint trustees or amend the trust deed. That way, a person who has no effective control over the trust would not affect its offshore status.
 - (b) In relation to percentage of trustees who are offshore: Officials agree with the independent specialist tax advisor to the Finance and Expenditure Committee that a trust will be an "offshore person" only if more than 25 percent of the trustees or persons with the power to appoint trustees or to amend the trust deed are offshore persons themselves. This is consistent with the *Overseas Investment Act 2005*.

(c) In relation to distributions to beneficiaries:

- (i) Officials agreed that a trust would be an offshore RLWT person only when an offshore beneficiary has received \$5,000 or more from the trust in any one year during the past four years.
- (ii) However, officials consider this \$5,000 per year threshold should be restricted to “natural person” beneficiaries. There should be no minimum threshold in the case of non-natural person beneficiaries. A trust would constitute an offshore person if a non-natural person beneficiary has received a distribution from the trust during the past four years.
- (iii) Officials commented that this distribution rule should apply to all beneficiaries including discretionary beneficiaries and recommended an amendment to cover this.

(d) In relation to the timing of determining whether a beneficiary is an offshore person:

- (i) Officials stated that it would not be necessary to determine whether the offshore beneficiary (discretionary or otherwise) was an offshore person at the time of each distribution.
- (ii) The test would look at whether a beneficiary or discretionary beneficiary who is currently an offshore person has received a distribution from the trust within the past four years.
- (iii) In the case natural persons, the test would look at whether a natural person beneficiary or natural person beneficiary who is currently an offshore person has received \$5,000 or more from the trust in any one year during the past four years.

(e) Officials considered that a trust should be an offshore person if a beneficiary (discretionary or otherwise) is an offshore person and the trust has disposed of residential land within the four years immediately before the relevant disposal of residential land for RLWT.

Third condition: what is a residential land purchase amount

29. The proposed definition in cl. 45 of the RLWT Bill as Reported is unchanged and states that a “residential land purchase amount” means, in relation to residential land located in New Zealand, an amount paid or payable for the disposal of the land, but excludes a deposit or part payment (the “part-amount”) if deposits and part payments, including the part-amount, total, in aggregate, less than 50% of the purchase price for the land.

30. Officials stated in the Commentary that “this rolling aggregate is to ensure that part-payments are not used to circumvent the application of the RLWT”.

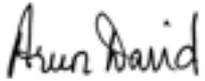
31. Officials commented in the Officials’ Report that:

“The intent for RLWT is that there should only be one RLWT liability per land disposal and this should arise when the 50 percent threshold is first exceeded.

However, there may be situations when there are a number of part-payments beyond the 50 percent threshold and none of these part payments individually would be sufficient to satisfy the RLWT liability for the entire transaction. In this case, the RLWT agent should retain or withhold RLWT from each part-payment beyond the 50 percent threshold to the extent that

they are able to until the RLWT liability has been fulfilled. Amendments to the legislation are required to ensure appropriate due dates and credits are provided in this situation.”

32. Section RL 4, which defines how much RLWT must be withheld, now contains a revised s. RL 4(1) requiring tax to be withheld from “residential land purchase amounts” (plural) and requiring that “RLWT is paid or withheld for each residential land purchase amount, up to the maximum of the relevant residential land purchase amount” – discussed in **paragraph 17** onwards in next week’s *Weekly Comment* 8 April 2016.



Arun David, Director,
DavidCo Limited