Arti Chand | Tax Law

actaxlaw.nz
+64 21 922 718
arti@actaxlaw.nz

AC Tax Desk

Issue No.7

Tax bits

Use of money interest

On 8 May 2017 the UOMI rates changed:

Underpayments - 8.22% (down from 8.27%)

Overpayments - 1.02% (down from 1.62%).

Taxation of trusts

IRD released an exposure draft on the taxation of trusts.

The deadline for submissions is 27th June 2017.

Here is a link to the draft:
Taxation of Trusts_Exposure Draft

Australian Budget

Foreign and temporary tax residents will no longer get the main home exemption for CGT.

CGT withholding rate for foreign tax residents will from 1 July 2017 increase to 12.5% (from 10%).

CGT withholding tax threshold re property sales will decrease from $2m to $750,000, from 1 July 2017.

Employee Share Schemes

Submissions on the Taxation (Annual Rates for 2017–18, Employment and Investment Income, and Remedial Matters) Bill ("the Bill") close on the 5th of July. The key item in the Bill is the introduction of new rules for the taxation of employee share schemes - summarised below.

What is an employee share scheme?

Any arrangement under which shares are issued or transferred in a company (Company A) to a person who will be, is, or was an employee/shareholder-employee (or an associate of the person) of Company A or any other company in the same group of companies as Company A.

However, where the person pays market value for the shares and the shares have no protection re a fall in value the arrangement is not an employee share scheme.

Share scheme taxing date

Unless the employee transfers the shares to a non-associate, or the company cancels the shares, the share scheme taxing date is when:

(a) there is no risk that the beneficial interest in the shares will change, or there is no requirement for the shares to be cancelled or transferred;

(b) the employee will not be compensated for any fall in value; and

(c) there is no real risk that the terms of the shares will change which will in turn affect the value of the shares.

Example A: Company A transfers 100 shares to a trust for the benefit of an employee. If the employee leaves within 3 years, the shares are forfeited. But, if the employee leaves because of sickness, the shares will be transferred to them.

The share scheme taxing date will be at the expiry of the 3 years, (or earlier if the employee leaves due to illness).

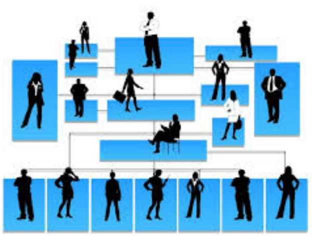
Example B: Same as above only while the shares transfer to the employee at the expiry of 3 years, the employee has to sell the shares to the trust if they leave employment and the trust has to purchase the shares at market value.

The share taxing date is at 3 years (or earlier if the employee leaves due to illness). This is because while the employee has to sell the shares to the trustee if they leave, the shares are sold at market value.

Example C: Company A gives the employee options to purchase 100 shares for $1 if the employee remains with the company for 3 years. At the end of 3 years, the employee exercises the options and purchases the shares. The market value of the shares when the options are exercised is $3/share. The employee will pay tax on $200 (market value of the shares ($300) minus the price paid ($100)).

Amount of employment income

The difference between the share value as at the share taxing date and the amount paid for the shares will be employment income for the person.



If the employee has paid more than what the shares are valued as at that date, the employee will get a deduction for the loss.

However, benefits that accrue while the employee is not a NZ resident nor deriving NZ sourced income is excluded from the taxable income.

Example D: Employee is employed by and works for a UK subsidiary of Company A. The employee, who lives in the UK, receives shares in Company A. Employee A is not taxed on the value of the shares as he/she is working in the UK and not a NZ resident.

Employer deduction

The employer claims a deduction of the same amount and at the same time as the employee returns the income. The employer can also claim deductions for costs incurred in the management and administration of the employee share scheme.

Loans to employees to fund the purchase of shares or reimbursements to a parent company for providing shares will not be deductible.

Start-ups and employee share schemes

On 30th May, an issues paper was released with proposals to defer the taxation re employee share purchase schemes for start-up companies. The submissions on these proposals is due by 12 July 2017.

The issues paper seeks submissions on the following "primary" option.

An employee gets shares in a start-up company. The employee will then be able to elect to defer the recognition of employment income from the share scheme until a "liquidity event" occurs - at which point the employee will be taxed on the value of the shares at that point in time and the employer will get a deduction at the same time. The liquidity event can be, for instance, when the shares in the start-up are listed, or when the assets of the start-up are sold.

The purpose of the proposal is that when the liquidity event occurs, the employee will be in a position to have cash to pay for the tax liability - which they would not have when the shares are issued (and at which point valuing the shares would also be difficult).

Other Tax News

Close companies and motor vehicles

Shareholder employees of close companies (5 or fewer natural person shareholders) can use the motor vehicle rules when purchasing a vehicle via their company. That is, the vehicle can be bought by the company and costs associated with the vehicle can be claimed based on a private/business apportionment. Previously, this scenario would have triggered an FBT issue if the vehicle was owned by the company but used by the shareholder-employee for private purposes.

Correction of errors

The self correction of minor errors threshold has increased to $1,000 for GST, income tax and FBT.

Look through companies

If the LTC owner is a trust, the counted owners will be the trust, and beneficiaries who have received distributions from the trust in the current or preceding three years. Previously, we only counted beneficiaries that had received a distribution of LTC income.

If the LTC owner is a trust, it cannot make a distribution to a corporate beneficiary.

An LTC that will no longer meet the eligibility criteria can transition and become an ordinary company under the transitional sections - so that no tax liability arises as a result of these changes for the company and its shareholders.

Tainted capital gains

Tainted capital gains rule will only apply to asset sales between companies that have 85% or more common ownership. This rule is effective from 30 March 2017.

By way of example, Company X and Company Y have an 85% common ownership. Company X sells an asset to Company Y and realises a gain. Company X liquidates - the gain will be taxable being a tainted capital gain if the common ownership of 85% still exists and Company Y (or another company which is also 85% or more commonly owned) still holds the asset.