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Investing in New Zealand

Tax Considerations

Current as at June 2020

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Taxation

Introduction

1. New Zealand's tax policy settings have been stable during the past decade or so and (with some exceptions) are simpler than is the case in some jurisdictions. The two principal taxes are the income tax (which includes tax on the income of corporations) and the goods and services tax. Excise duties apply to a limited category of goods: certain fuels, tobacco and alcoholic beverages. New Zealand has a unitary (rather than a federal) system of government and all taxes are levied by the central government (ie there are no separate state or provincial taxes (other than local authority rates levied on the value of real property)).

2. New Zealand has a double tax agreement ("**DTA**") network of some 40 DTAs, covering almost all of our major trading partners. DTAs are currently in force with Australia, Austria, Belgium, Canada, Chile, China, the Czech Republic, Denmark, Fiji, Finland, France, Germany, Hong Kong, India, Indonesia, Ireland, Italy, Japan, the Republic of Korea, Malaysia, Mexico, the Netherlands, Norway, Papua New Guinea, the Philippines, Poland, the Russian Federation, Samoa, Singapore, South Africa, Spain, Sweden, Switzerland, Taiwan (consistently with New Zealand's one China policy, the parties to this DTA are the New Zealand Commerce and Industry Office and the Taipei Economic and Cultural Office in New Zealand), Thailand, Turkey, the United Arab Emirates, the United Kingdom, the United States of America and Viet Nam.

3. New Zealand has no general capital gains tax, although the definition of income includes profits and gains from certain transactions (notably involving personal property, land and financial arrangements) that would otherwise be capital in nature. One of the important cases in which a capital gain is deemed to be income is the so-called bright-line test applicable to the proceeds of sale of residential property. A gain made in circumstances where a residential property (other than the person's principal residence) is bought and sold within 5 years is deemed to be income even if it would otherwise be a capital gain.

4. New Zealand has no inheritance tax, wealth tax, gift tax, stamp duty or payroll tax. There are no current proposals to introduce such taxes.

5. A Government appointed Tax Working Group undertook a review of the tax system, culminating in the release of its final report in early 2019. The report's most significant recommendation was the introduction of a comprehensive tax on capital gains. The Government, however, rejected that recommendation. It is now the policy of both of New Zealand's major political parties not to introduce a comprehensive capital gains tax.

6. The income tax rate for companies (resident and non-resident) is 28%. Individuals are subject to taxation at progressive marginal rates, with the top rate (for income in excess of $70,000) being 33%. Trustees (other than of unit trusts, which are taxed as companies) are taxed at 33% on trustee income.

7. New Zealand resident individuals are generally subject to New Zealand tax on their worldwide income, with a credit being allowed for foreign tax. Individuals who become New Zealand tax resident for the first time or (in certain cases) after a period of at least 10 years as a non-resident, may qualify for transitional resident status. Transitional resident status applies for (approximately) the first four years during which a person is New Zealand resident, and

provides an exemption from New Zealand tax for most non-New Zealand sourced income the person derives during that period.

Income tax - principal features of corporate taxation

8. Companies resident in New Zealand generally pay tax on their worldwide income, the main exception being that a participation exemption applies to dividends received from a foreign company in which the New Zealand resident company holds a voting interest of at least 10%. Non-resident companies are subject to tax on any income derived from New Zealand. Income tax is levied on annual gross income less annual total deductions and any losses brought forward from prior years or offset from companies in the same group. The resulting net amount is the taxable income.

9. A full imputation system enables New Zealand resident companies to attach to dividends credits for tax paid by them. Dividends received by a New Zealand resident company from another New Zealand resident company (other than where those companies are wholly-owned) are assessable for tax. Imputation credits received with dividends may be used to offset the recipient company's tax liability.

Income tax - taxation of foreign investment into New Zealand

Withholding tax on dividends, interest and royalties

10. Dividends, interest and royalties paid to non-residents are subject to New Zealand withholding tax. Exceptions apply to interest paid to a non-resident in connection with a business it carries on through a New Zealand branch and in certain other cases to interest paid to a non-resident carrying on business in New Zealand as a registered bank.

11. New Zealand does not have an exemption from interest withholding tax for widely held debt. There is, however, an option for borrowers to reduce the withholding tax rate to 0% by making certain registrations and paying a levy (known as the approved issuer levy (or AIL)) in respect of interest paid to a lender that is not associated with the borrower. The definition of association for this purpose is broad, and includes the circumstance in which the borrower is owned by a consortium or other group of lenders that act together in respect of their ownership interests.

12. AIL applies at the rate of 2% of the amount of interest paid. It is payable by the borrower and is a levy rather than a tax. Accordingly, it is unlikely to be creditable against foreign tax payable by the lender on its interest receipts.

13. For interest and royalties paid to non-residents, the rate of withholding tax under domestic law is generally 15%, although this is typically reduced to 10% under an applicable DTA. In the case of some more recently concluded DTAs, the rate in respect of royalties may be reduced to 5%.

14. Dividends paid to non-residents are generally subject to non-resident withholding tax at a rate of 15% (to the extent fully imputed) or 30%, subject to the availability of tax treaty relief (described below). However, the rate of non-resident withholding tax for such dividends may be reduced to 0% where the dividend is fully-imputed and where the recipient has a 10% or greater direct voting interest in the payer. In the case of a non-resident holding a less than 10% voting interest, the company paying the dividend may pay a "supplementary dividend"

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to the shareholder (in which case the company will receive a credit, equal to the amount of the supplementary dividend it pays, against income tax otherwise payable on its taxable income). In the case of a fully imputed dividend, the supplementary dividend paid to the non-resident is intended to have the effect that income tax on the earnings together with withholding tax (at the rate of 15%), do not in aggregate exceed 28% (being the corporate tax rate).

15. The withholding tax rates for dividends described above are generally capped at 15% in the case of persons resident in a country with which New Zealand has a DTA. Lower dividend withholding tax rates (typically 5%, or in some cases 0%) apply under certain of New Zealand's DTAs (including those with Australia, Canada, China, Hong Kong, Japan, Mexico, Samoa, Singapore, Turkey, the United States and Viet Nam) in the case of dividends paid to a shareholder that is a company that meets the relevant minimum ownership requirement and certain other criteria.

16. Withholding taxes may also apply to payments to non-residents in certain other situations, including payments to non-residents for services performed or for the use of personal property in New Zealand, or to the proceeds from a disposal of New Zealand residential land. In the case of payments for services performed or for the use of personal property in New Zealand, the rate of withholding tax is generally 15%. If the payer has not been notified of the non-resident contractor's name and tax file number, this rate may be increased to 20% (if the recipient is a company) or 45% (in other cases). In the case of the proceeds from a disposal of New Zealand residential land, the amount of withholding tax is the lowest of: i) 33% (for individuals) or 28% (for companies) of the profit on disposal; ii) 10% of the disposal price; and iii) if certain criteria are met, the disposal price less amounts required to discharge securities over the land and outstanding local authority rates.

17. DTA relief (if available) does not always apply at source in respect of these payments. Therefore, even if an amount may be fully relieved from New Zealand tax under an applicable DTA, the payer may be required to withhold tax nonetheless. A non-resident recipient of such payments may need to obtain an exemption from withholding if available (one ground for an exemption from withholding in respect of payments for services performed or for the use of personal property in New Zealand, is that the payments would be fully relieved from New Zealand tax under a DTA). Alternatively, the non-resident may need to file a New Zealand tax return and seek a refund of the tax withheld.

Limits on deductibility of related party financing costs

18. New Zealand entities controlled by non-residents are subject to comprehensive transfer pricing and thin capitalisation rules. During the past few years, Inland Revenue has identified related party interest expenditure as one of its most significant compliance priorities in respect of large businesses.

19. The thin capitalisation rules limit interest deductions based on a ratio of debt to assets. In the case of inbound investment, interest deductions will be denied to the extent the New Zealand group's ratio of total debt to total assets exceeds both an absolute 60% threshold and a threshold of 110% of the worldwide group ratio.

20. Although the transfer pricing rules may apply in respect of most cross-border related party supplies, the rules contain a set of highly prescriptive rules specifically directed at limiting the rate of interest payable on inbound related party debt. In certain circumstances, these rules may require debt to be priced on the assumption that the borrower has a deemed credit rating determined on the basis of the wider group's credit rating even if the deemed credit rating exceeds the borrower's actual credit rating. The rules may also require debt to be priced on a basis that ignores subordination or similar terms of the debt that would otherwise result in a higher arm's length interest rate.

Base erosion and profit shifting measures

21. New Zealand has enacted a range of reforms intended to implement the OECD's proposals targeting base erosion and profit shifting (BEPS), including strengthening the thin capitalisation, transfer pricing and permanent establishment rules, and measures targeted at hybrid mismatch arrangements. New Zealand has also signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (also known as the multilateral instrument, or MLI), which amends certain of its DTAs to reflect OECD recommendations relating to anti-abuse rules, hybrid mismatches, preventing the avoidance of permanent establishment status, and dispute resolution, to the extent the relevant treaty partner also elects to include the relevant provisions.

R&D tax credit

22. New Zealand recently implemented a 15% tax credit that will be available, in respect of eligible research and development ("**R&D**") expenditure, to businesses undertaking eligible R&D activities in New Zealand. The R&D tax credit can be applied against tax on the person's taxable income. However, to the extent a person has remaining R&D tax credits after reducing tax on taxable income to zero, the R&D tax credit can be applied to satisfy certain of the person's other tax liabilities (for example, the person's income tax liability for a later year) subject to satisfying continuity of ownership requirements, and if any R&D tax credit remains after this, cashed out (provided the person meets certain criteria and with certain limitations).

Income tax - taxation of employees

23. Income tax is assessed on the gross income of employees. Tax payable by employees (together with certain other amounts including KiwiSaver employee contributions and ACC levies) is collected at source by the employer (this system is known as "pay-as-you-earn" or PAYE).

Taxation of trusts

24. As a general rule, trust income is taxed either as beneficiary income (where distributed or applied for the benefit of beneficiaries within a certain period) or trustee income (to the extent not beneficiary income).

25. Where a trust has a New Zealand resident settlor, the trust is in effect treated as resident in New Zealand and its worldwide income is subject to tax in New Zealand. Where there is no New Zealand settlor of a trust (and even if there are New Zealand resident trustees), the

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income of the trust will generally (and provided the trust meets the disclosure requirements described below) be subject to tax in New Zealand only to the extent the income has a New Zealand source or is derived as beneficiary income by a New Zealand resident beneficiary.

26. A set of disclosure rules applicable to foreign trusts was introduced in early 2017. Non-compliance with these disclosure requirements may result in the trust being subject to New Zealand tax on its worldwide income. The main obligations fall on New Zealand resident trustees of foreign trusts (including providing information relating to the settlor, beneficiaries and the trust deed). One consequence of the reforms is that a register of foreign trusts is now administered by Inland Revenue.

Goods and services tax

27. New Zealand imposes a broad-based value added tax referred to as goods and services tax ("**GST**") at the rate of 15% on the supply of all goods and services in New Zealand (subject to rules applying a zero-rate for certain transactions (including exported goods and services and sales of land between GST registered persons), exemptions for financial services and the supply of residential accommodation, and certain other limited exceptions).

28. In the case of goods imported into New Zealand, GST is collected by Customs together with any Customs duty. As a result of recently enacted reforms, an exception applies in respect of low-value goods (generally defined as goods valued at NZ$1,000 or less). The new rules require non-resident suppliers to New Zealand consumers to register for and collect GST on low-value goods. The new rules also require, in some circumstances, electronic marketplaces and re-deliverers to register for and collect GST.

29. Services imported into New Zealand may be subject to a "reverse charge", which requires the New Zealand resident recipient of the imported services to self-assess GST in respect of those services. In addition, certain non-resident suppliers of remote services (for example, certain services provided online) are required to register for and pay GST on services supplied remotely to New Zealand residents from 1 October 2016.

This article is intended only to provide a summary of the subject covered. It does not purport to be comprehensive or to provide legal advice. No person should act in reliance on any statement contained in this publication without first obtaining specific professional advice. If you require any advice or further information on the subject matter of this newsletter, please contact the partner/solicitor in the firm who normally advises you, or alternatively contact one of the experts listed below.

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