

# C O R P O R A T E S   C O N T A C T

## N U M B E R   T W E N T Y   S I X   ~   J U N E   2 0 0 5

### Taking a risk-focused approach

Speaking at the International Fiscal Association Conference in Christchurch at the end of April, I highlighted a number of changes that we have made over the past year within Corporates that see us taking a risk-focused approach and moving towards real time presence.

We are endeavouring to streamline our processes and become more risk-focused so that we are able to complete reviews in a timelier manner and work on current periods. We believe this will benefit taxpayers as reviews will be in real time and will consequently be less costly.

Through our Risk and Intelligence Unit, established in April 2004, we are able to identify taxpayer risk and rank that across our taxpayer base, enabling us to allocate resources to high risks and address these in a timelier manner.

We are working on modifying our risk methodologies to include other criteria to enable greater in-depth analysis. This will result in a more comprehensive ranking of risk. We are also focusing on using our intelligence more effectively. One example of this in action is the way we use reports showing which companies are generating and utilising losses. We are comparing these companies to industry and economic trends. Where the analysis is not consistent with our expectations (for example, why should companies in buoyant sectors still be generating losses?) we are feeding these risks to the relevant teams to follow up.

To create and maintain an environment where taxpayers, of their own accord, voluntarily comply with the tax laws, we strive to be timely in everything we do, be consistent and create certainty. I also believe that if we expect taxpayers to voluntarily comply it is only right that we share with them the risks we have identified or perceive to exist.

Some of the risks we have identified and will be monitoring and developing appropriate risk responses for, include:

- **Related party financing into New Zealand**  
We have identified a number of instances where related party financing is occurring based around the accrual determination to create what we consider to be inappropriate deductions.
- **Intangible property**  
We are looking at a number of issues surrounding intangible property (including the cross-jurisdiction sale and leaseback of intangible property and transactions between associated parties with major transfer pricing implications).
- **Asset valuations and allocations for depreciation**  
We are reviewing a number of depreciation issues relating to the valuation and asset allocations for significant asset purchases.
- **Dividend withholding payments**  
We are reviewing a number of structures that either utilise dividend withholding payments (DWP) in inappropriate ways or that defer or avoid DWP liability altogether.

It is fair to say that the communication of such risks to taxpayers has caused some tension between us in the past. This is another area we have made changes in over the past 12 months and believe that our communication about risk analysis will be clear, concise and widely understood.

Spyros Papageorgiou  
Group Manager  
Corporates

## Bribes are not deductible for income tax

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Bribes intended to influence a public official in order to act, or fail to act, to retain business, or obtain an improper advantage in the conduct of business, are explicitly not deductible for tax purposes.

As a member of OECD, New Zealand introduced legislation (Income Tax Act 2004 DB 36) to fulfil its obligations under the OECD Anti-Bribery Convention to stop paying bribes at home and abroad.

Our tax law uses the Crimes Act 1961 definition of a bribe as any money, valuable consideration, office, employment or any benefit whether direct or indirect.

The law relates to bribes to New Zealand and foreign public officials. The provision does not apply to a payment made (to a foreign public official) to expedite the performance of a routine government action when the value of the benefit is small.

In terms of risk, businesses trading on the international market must be conscious of the countries they are trading with to ensure compliance with the legislation. *Transparency International* lists the international corruption perception index. It identifies 106 of 146 countries which score less than 5 on the 10 point compliance scale. Sixty countries score less than 3 out of 10, indicating rampant corruption.

If you have treated bribes as tax deductible you may wish to consider using the *voluntary disclosure regime* to get your tax affairs into order. We will be testing for compliance with section DB 36 later this year.

## Corporate migration

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### Recent Ministerial announcement about outward migration—managing the transition

The Minister of Revenue Dr Michael Cullen recently announced that, for tax purposes, migrating companies are to be on a par with liquidating companies. This legislation has recently been introduced in the Taxation (Depreciation, Payment Dates Alignment, FBT and miscellaneous provisions) Bill and is effective from the date of announcement—21 March 2005.

As set out in the *Bill commentary*, the migrating company will be first deemed to have disposed of all assets and liabilities and realised them at market value immediately before it ceases to be a New Zealand resident. Certain proceeds (such as gains in the value of revenue account property) will then be subject to income tax. A deemed liquidation and distribution rule will also create withholding liabilities for the migrating company, such as resident withholding tax and non-resident withholding tax.

Our current practice is that a migration will not be approved if the Commissioner cannot guarantee that tax debts, that may arise once the company has migrated, will be met.

To mitigate this concern, taxpayers have in the past offered us a letter of guarantee from, for example, a related New Zealand company that has the means to satisfy the migrated company's tax liability, or a bank in other circumstances. With the letter of guarantee in place, we are then able to provide written notice to the Registrar of Companies that the Commissioner has no objection to the migration.

With the recent introduction of legislation we would look to extend our existing practice and include any potential withholding or additional income tax liabilities as a possible tax debt that would need to be met once the company has migrated.

Thus if a suitable guarantee were offered which meant we were comfortable that tax debts would be met when they fell due, the fact that the legislation had not passed should not prevent the migration.

### Inward migrations—our practice

With the recent introduction of legislation on outward migration, it seemed timely to set out our current view and practice with migrations of controlled foreign companies from a foreign jurisdiction to New Zealand.

At a minimum we will be reviewing dividends, paid by the newly resident company, to ensure that dividend withholding payment, where appropriate, is deducted. This will include situations where the newly migrated company then amalgamates with another New Zealand resident company, as the amalgamated company retains the obligations of the migrated company.

Where no dividends are paid but the value of the reserves is passed onto another New Zealand group company in another form, the transaction will be reviewed with a view to seeing whether the dividend withholding payment anti-avoidance rule—section GC 25—could apply. This could include, but is not limited to, situations where passing on the value of reserves would have been an attributed repatriation if the company were still resident offshore.

## Changes to the disputes resolution procedures

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Amendments have been made to the disputes resolution procedures. The changes will apply to disputes commenced under Part IVA of the Tax Administration Act 1994 on or after 1 April 2005.

The amendments give effect to proposals outlined in the government discussion document *Resolving tax disputes: a legislative review*, which was released in July 2003. More information about the legislative changes can be found in the *Tax Information Bulletin Vol 17, No 1 (February 2005)*.

The implementation of the amended disputes procedures will have an impact on the way we manage the audits of corporate taxpayers. Standard practice statements 05/03 *Disputes resolution process commenced by the Commissioner of Inland Revenue* and 05/04 *Disputes resolution process commenced by a taxpayer* set out the Commissioner's practice in respect of the disputes process generally commencing on or after 1 April 2005.

We have already moved to earlier and better identification of risk through our Risk and Intelligence Unit. We will now also need to be more efficient and timely when gathering information and enter into the formal disputes process earlier to ensure that the full disputes process can be completed before time bar.

### *What does this mean for you as a corporate taxpayer?*

You will notice some changes to our procedures, for example:

- we will initiate audits earlier
- we will work with you to set timeframes for all information requests
- there will need to be less flexibility afforded to delays in providing information
- “issues papers” will be used less as a way of raising and discussing Inland Revenue's position on potential discrepancy items
- we will enter into the formal disputes process earlier
- time bar waivers may need to be requested at an earlier stage in the process.

By working together we can ensure that any disputes identified during an audit are resolved in a timely manner through the formal disputes procedures.

### **Transitional issues—taxpayer NOPAs relating to GST periods commencing before 1 April 2005**

Generally, the new disputes rules apply for GST periods commencing on or after 1 April 2005. However, there are some transitional issues to be discussed.

The two month response period for a taxpayer's notice of proposed adjustment (NOPA) still applies to any dispute commenced from 1 April 2005 that relates to a GST period commencing before April 2005. In this case, taxpayers have two months to file their NOPA from the day immediately following the due date for the filing of that GST return. For example, if a taxpayer files a six-monthly GST return for the taxable period commencing on 1 January 2005 and wishes to issue a NOPA on that return, the NOPA must be issued to us no later than 29 September 2005 (being two months from the day immediately following the due date for filing that return).

In most other cases, a four month response period will apply for taxpayer NOPAs issued from 1 April 2005—that is relating to revenues other than GST regardless of the return period, as well as GST return periods commencing on or after 1 April 2005.

If you are issuing a NOPA in relation to a disputable decision (not being an assessment) the response period for this, under the new disputes rules, will remain at two months from the date of issue of that decision. Further legislative amendments have been proposed in the drafting of the next taxation bill to allow a taxpayer a four month response period to issue a NOPA in respect of a “disputable decision” that is not an assessment.

## Made a mistake? How to amend a return

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A taxpayer or their tax agent can request Inland Revenue amend an assessment to correct a genuine error—such as arithmetic or transposition errors.

### *Making a request*

Amendment requests must be made as a written application—do not send in a second return marked “amended”. When making a request it is important that you provide all the relevant information to support the claim at the time the request is made. This includes:

- tax type and period containing the error
- amount of tax in error
- nature of the error
- how the error occurred
- how and why the error was identified
- action required to ensure correctness.

### *Considering requests*

Each request is dealt with on a case-by-case basis taking into account all relevant factors. We will determine whether the request is clear and may ask for clarification or further information from you or your tax agent.

The assessment will be amended once we are satisfied that the request is clear, all information has been provided, the error has been verified by the Commissioner and the amendment is within the time limits.

In cases where we are not satisfied that a genuine error exists or consider one of more of the limitations applies, the assessment will not be amended. Where such a decision is made, we will advise you of the decision and the reasons for it.

More information can be found in the standard practice statement INV-510 *Requests to amend assessments*.

## File it online

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The Inland Revenue website allows taxpayers to “get it done online”—it’s where you go when you want to make a payment, look at your account information, register for some of our services and file your returns electronically.

So what returns can you file online?

- Employers who pay fringe benefit tax (FBT) can file their FBT returns.
- Businesses registered for goods and services tax (GST) can file GST returns—you can also register for GST online.
- *Individual tax returns (IR 3)* and *Income tax return – Companies (IR 4)* can both be filed.
- The ir-File service allows employers, tax agents, payroll bureaux and PAYE intermediaries a secure and convenient method of filing employer monthly schedules through Inland Revenue’s website.

For e-FBT, GST and income tax return online filing you will need the DLN number from the paper return. This is the 14 character computer printed number on the front of the return. All the characters are numbers except the second to last which is a capital letter. If you don’t have this number, call us on 0800 443 773.

More information about *filing these or other returns online* can be found on our website.

## Non-resident contractors’ withholding tax (NRCWT)

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The *Non-resident contractors’ withholding tax (NRCWT) certificate of exemption application (IR 197) form* is now available from our website.

## New Income Tax Act 2004 now in effect

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The rewritten Income Tax Act 2004 came into effect from 1 April 2005 for those taxpayers with a standard tax balance date of 31 March. The new Act applies to income derived from the 2005—06 year and onwards. The earliest non-standard balance date that the new Act applies to is 1 October 2005.

The new Act is the third stage of a programme to rewrite income tax legislation so that it is clear, uses plain language and is structurally consistent. It is anticipated that in the long term this will allow taxpayers and agents to save time and resources, making compliance easier. The remainder of the Income Tax Act 2004 is being rewritten progressively and should be completed during 2007.

Aside from a small number of intended policy changes listed in Schedule 22A of the Income Tax Act 2004, income tax law remains the same as it did previously.

For more information about the new Act please refer to the *Tax Information Bulletin Vol 16, No 5* (June 2004).

## Provisional tax pooling

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We are aware that some businesses struggle to estimate provisional tax because of factors like currency exchange movements, seasonal trends and uneven trading patterns. One option to mitigate risks is provisional tax pooling.

Legislation allows for the establishment of provisional tax pooling accounts. Provisional tax pooling was introduced to reduce compliance costs in response to taxpayer concerns over difficulties in calculating their provisional tax and the resulting exposure to use-of-money interest (UOMI).

Often, the amount of income tax a taxpayer will be liable for is uncertain, with the amount paid during the year as provisional tax reflecting the taxpayer's best judgement of the law on a large number of technical issues. If the taxpayer's judgement of their liability is incorrect, and they have actually overpaid or underpaid tax, they may be exposed to the imposition of UOMI.

### *How tax pooling works*

Provisional tax pooling allows taxpayers to pool provisional tax payments with those of other businesses, offsetting underpayments by overpayments within the same pool, thereby reducing their UOMI exposure. The pooling arrangement is made through a commercial intermediary who arranges for participating taxpayers to be charged or compensated for the offset.

Provisional tax payments made to an intermediary are passed on to Inland Revenue and held in a tax pooling account. When the taxpayer knows their income tax liability for the year, they can arrange for the intermediary to ask Inland Revenue to deal with their payment accordingly, for example, transfer the payment to their income tax account if they are liable for debit UOMI.

## Do you have feedback about *Corporates Contact*? We'd like to hear from you

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*Corporates Contact* is a quarterly e-newsletter for everyone in large corporate organisations who deal with tax matters.

We want to ensure that *Corporates Contact* is meeting your needs. Your feedback will help us tailor the articles to make sure you get the most use from this newsletter.

- Have the articles in this and previous issues been useful and informative?
- Do you have any suggestions on how we could improve the way we provide the information?

We'd also like to make sure we're sending *Corporates Contact* to the right person in your organisation. If not, let us know who it should be going to and we'll update the distribution list. Please provide the name of your company, the name and position of the contact person and their email address.

Let us know your thoughts by emailing the editor [corps.contact@ird.govt.nz](mailto:corps.contact@ird.govt.nz)