

Supplementary Departmental Disclosure Statement

Taxation (Annual Rates for 2020–21, Feasibility Expenditure, and Remedial Matters) Bill

A supplementary departmental disclosure statement for a Bill the government is proposing to amend seeks to bring together in one place a range of information to support and enhance the Parliamentary and public scrutiny of that Bill in amended form.

It highlights material changes to previous disclosures relating to:

- the general policy intent of the Bill and other background policy material;
- some of the key quality assurance products and processes used to develop and test the content of the Bill;
- the presence of certain significant powers or features in the Bill that might be of particular Parliamentary or public interest and warrant an explanation.

The original disclosure statement for the Taxation (Annual Rates for 2020–21, Feasibility Expenditure, and Remedial Matters) Bill dated 28 May 2020, can be found at <http://disclosure.legislation.govt.nz/bill/government/2020/273/>

This supplementary disclosure statement was prepared by the Inland Revenue Department.

The Inland Revenue Department certifies that, to the best of its knowledge and understanding, the information provided is complete and accurate at the date of finalisation below.

18 March 2021.

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The Main Areas of Change to the Original Disclosures

This is a supplementary disclosure statement for the Taxation (Annual Rates for 2020–21, Feasibility Expenditure, and Remedial Matters) Bill.

A supplementary disclosure statement supplements the original disclosure statement for the Bill by reporting the additions and changes that would need to be made to the original disclosure statement to accurately reflect the Bill with the proposed government amendments incorporated.

The main areas of change to the original disclosure statement include:

- the addition of a new proposal extending the residential property bright-line test;
- the addition of a new proposal loosening the loss continuity rules;
- the addition of a new proposal addressing the taxation of donated trading stock; and
- technical and remedial changes relating to the recent introduction of a 39% top personal tax rate.

The supplementary disclosure statement also covers changes to existing proposals in the Bill on unclaimed money and *Mycoplasma bovis* that have arisen after the Finance and Expenditure Committee's report back on the Bill.

Part One: General Policy Statement

This Supplementary Order Paper proposes amendments to the Taxation (Annual Rates for 2020–21, Feasibility Expenditure, and Remedial Matters) Bill and therefore amendments to the:

- Income Tax Act 2007;
- Tax Administration Act 1994;
- Taxation (Income Tax Rate and Other Amendments) Act 2020; and
- Unclaimed Money Act 1971.

Broadly, the proposals contained in the Supplementary Order Paper fall into four categories. The first is measures to reduce investor demand for residential property. The second is policies progressed as part of the Government's COVID-19 response. The third is changes to policies already included in the Bill. The last category is remedial and technical amendments.

Extending the bright-line test

The SOP proposes to extend the bright-line test, which taxes gains from residential property acquired and sold within a specified timeframe, from 5 years to 10 years.

The proposed changes apply to property acquired on or after 27 March 2021, but not to acquisitions where the offer was made by a purchaser on or before 23 March 2021 and was not able to be revoked before 27 March 2021.

Amendments are also proposed to the main home exclusion from the bright-line test. It would no longer apply on an all or nothing basis, but rather apply only for the period the property is actually used as the owner's main home. A 12-month change of use "buffer" is also proposed, within which the change of use to or from being the taxpayer's main home would not need to be accounted for.

Finally, the business premises exclusion in the definition of residential land would be amended to ensure that the provision of short-stay accommodation in a dwelling that is not the owner's home is subject to the bright-line test, applying to property acquired on or after 27 March 2021. The amendment also ensures that full-time Airbnb properties, or baches that are sometimes rented out, are subject to the residential deduction ring-fencing rules. For the purposes of the residential rental deduction ring-fencing rules, this proposed amendment would apply for the 2021–22 and later income years, regardless of when the property was acquired.

The extension of the bright-line test is part of the Government's response to the housing crisis. It is one part of a range of supply and demand-side measures that will be implemented over the coming months. Decreasing the tax advantage that property investors can receive will reduce the amount investors are prepared to pay for a given house and the number of houses they will buy. The measure will support first home buyers and help to lift New Zealand's home ownership rates.

Loosening the loss continuity rules

New Zealand's current loss continuity rules require at least 49% continuity of ownership of a company for losses to be carried forward to offset future taxable income. This test is intended to prevent loss trading. However, it can create an impediment for businesses obtaining capital in order to innovate and grow because doing so can breach the 49% threshold. While this is particularly an issue for start-ups, some

businesses recovering from the economic impacts of COVID-19 will look to recapitalise and innovate in order to survive.

The Supplementary Order Paper proposes to introduce into the Income Tax Act 2007 a business continuity test for loss carry forward. This test would permit a company to carry forward losses as long as there is no “major change” in the company’s business activities for five years after a change in ownership. The core test is supported by specific anti-avoidance measures to ensure that the loss continuity rules are not manipulated in order to gain a tax advantage through loss trading.

Donated trading stock

The Supplementary Order Paper proposes to turn off a rule in the Income Tax Act 2007 which imposes tax on the market value of donated trading stock effectively taxing a deemed profit (“deemed income rule”). This rule disincentives donations made in response to COVID-19 (and more generally). For example, the current rule is taxing goods donated for public benefit, such as food donated to food banks or masks donated to hospitals. The proposed changes amend the Income Tax Act 2007 to provide that trading stock donated between 17 March 2020 and 16 March 2022 (inclusive) to:

- public authorities and donee organisations will not be subject to the deemed income rule and will be eligible for a tax deduction;
- non-associated persons (who are not public authorities or donee organisations) will not be subject to the deemed income rule. However, the donor will only be able to claim a tax deduction where they can demonstrate the donation is made for business purposes.

Unclaimed money

The Supplementary Order Paper contains proposed changes to the unclaimed money proposals in the Bill which relate to work undertaken to modernise the Unclaimed Money Act 1971. The changes to these proposals are:

- reducing the proposed 60-year time bar on a claimant’s ability to claim unclaimed money to 25 years;
- making amounts of unclaimed money without any associated information unclaimable and vested in the Crown; and
- making amounts of unclaimed money which are \$100 or less unclaimable and vest this money in the Crown.

Overall, these changes are designed to allow Inland Revenue to focus on tracking down the rightful owners of unclaimed funds where there is the greatest likelihood of locating them.

Mycoplasma bovis

The Supplementary Order Paper contains changes to a proposal in the Bill which introduces a six-year income spreading option to mitigate the unexpected taxable income that can arise when a livestock owner’s breeding cattle are valued at cost and are culled due to the Mycoplasma bovis outbreak.

Some Mycoplasma bovis-affected farmers will by now have made deposits into the Income Equalisation Scheme (IES) or the Adverse Event Income Equalisation Scheme (AEIES) to mitigate the tax consequences created by the cull which commenced in

2017. Amendments are proposed to give farmers that made deposits into the IES or AEIES the option of retrospectively switching to the proposed six-year income spread provided the tax effects of the relevant deposits are reversed and the election is made by the date of filing their return of income for the 2020–21 year.

Other remedial and technical amendments

The Taxation (Income Tax Rate and Other Amendments) Act 2020 introduced a new top personal tax rate of 39% for income over \$180,000 into the Income Tax Act 2007. At the same time new disclosure requirements for certain trusts were introduced into the Tax Administration Act 1994 to assess compliance with the 39% rate and to understand and monitor the use of structures and entities by trustees. The Supplementary Order Paper contains the following in relation to these policies.

- Excluding trusts from the increased disclosure requirements where they are at low risk of being used to minimise income taxed at 39% and are unlikely to accumulate private wealth.
- Including a provision to allow the Commissioner of Inland Revenue to vary specific information requirements set out in the increased disclosure rules for certain trusts where it may be reasonable that they do not have to provide particular information.
- Clarifying that an exclusion from the increased disclosure requirements does not exclude trusts from current filing requirements.
- Retaining the default resident withholding tax rate at 33%.
- Consequential technical amendments to the provision clarifying the Commissioner of Inland Revenue's power to require information to support tax policy development.

The Supplementary Order Paper also contains minor remedial amendments to correct a typographical error in the Income Tax Act 2007 relating to the use of losses when companies amalgamate and to make a clarification relating to the application of the definition of "tax loss component".

Finally, the Supplementary Order Paper contains minor technical corrections to items in the Bill, in particular, to correct:

- an application date for the thin capitalisation interest apportionment formula; and
- an unintended overreach of the proposed purchase price allocation amendments in the Bill where these amendments repeal rather than override two provisions of the Income Tax Act 2007.

Part Two: Background Material and Policy Information

Published reviews or evaluations

2.1. Are there any publicly available inquiry, review or evaluation reports that have informed, or are relevant to, the policy to be given effect by this Bill?	YES
<p>A supplementary commentary on the Bill covering the additional policy proposals in the Supplementary Order Paper is available at https://taxpolicy.ird.govt.nz/publications/2021/2021-commentary-arferm-bill-supplementary. The supplementary commentary provides a more detailed explanation of the loss continuity rules in the Supplementary Order Paper.</p>	

Relevant international treaties

2.2. Does this Bill seek to give effect to New Zealand action in relation to an international treaty?	NO
2.2.1. If so, was a National Interest Analysis report prepared to inform a Parliamentary examination of the proposed New Zealand action in relation to the treaty?	N/A

Regulatory impact analysis

2.3. Were any regulatory impact statements provided to inform the policy decisions that led to this Bill?	YES
<p>A regulatory impact assessment (RIA) was prepared by The Treasury for the extension of the bright-line test <i>Tax measures to moderate house price growth – extension of the bright-line test</i> (5 March 2021).</p> <p>A RIA was also prepared by Inland Revenue for the donated trading stock proposal <i>COVID-19: Tax relief for donations of trading stock</i> (18 January 2021).</p> <p>The RIA prepared by Inland Revenue for the Unclaimed Money proposal in the Bill, <i>Review of Unclaimed Money Act</i> (24 April 2020), was amended on 15 January 2021 to reflect the changes proposed in the Supplementary Order Paper.</p> <p>A RIA was not required for the policy decisions on the loss continuity proposals, but a supplementary analysis report (SAR), <i>Loosening the loss continuity rules</i> (11 February 2021), was prepared by Inland Revenue to accompany the Supplementary Order Paper. The SAR provides a RIA-like analysis of the policy development to aid understanding of the proposals as they go through the legislative process.</p> <p>These documents are available at:</p> <ul style="list-style-type: none">• https://taxpolicy.ird.govt.nz/publications, and• https://www.treasury.govt.nz/publications/legislation/regulatory-impact-assessments <p>Other proposals in the Supplementary Order Paper are exempt from regulatory impact analysis requirements as they involve technical revisions that improve legislative clarity and understanding (including correcting errors), or have no, or only minor, impacts on businesses, individuals or non-for-profit entities.</p>	

2.3.1. If so, did the RIA Team in the Treasury provide an independent opinion on the quality of any of these regulatory impact statements?	YES
<p>Treasury's Regulatory Impact Analysis Team and Inland Revenue have reviewed the regulatory impact <i>Tax measures to moderate house price growth – extension of the bright-line test</i> prepared by the Treasury and dated 5 March 2021. The review panel considers that it partially meets the quality assurance criteria.</p> <p>The other regulatory impact statements for this Supplementary Order Paper did not meet the threshold for requiring an independent opinion on their quality from the Treasury's Regulatory Quality Team.</p>	

2.3.2. Are there aspects of the policy to be given effect by this Bill that were not addressed by, or that now vary materially from, the policy options analysed in these regulatory impact statements?	NO
<p>The RIA on the extension of the bright-line test did not consider policy settings relating to the bright-line test other than the number of years. Therefore, the RIA did not address the changes to the main home exclusion or definition of residential land.</p>	

Extent of impact analysis available

2.4. Has further impact analysis become available for any aspects of the policy to be given effect by this Bill?	NO
<p>No significant further impact analysis has become available for any aspects of the policy to be given effect by the Bill. Therefore, for the purposes of this statement, the answer is "No" as per the scope of this question explained in page 29 of the <i>Disclosure Statements for Government Legislation: Technical Guide for Departments</i> (June 2013).</p> <p>However, the supplementary commentary, available at https://taxpolicy.ird.govt.nz/publications/2021/2021-commentary-arferm-bill-supplementary, contains analysis of the bright-line test extension and loss continuity proposals included in the Supplementary Order Paper. This may supplement existing published analysis.</p>	

2.5. For the policy to be given effect by this Bill, is there analysis available on:	
(a) the size of the potential costs and benefits?	YES
(b) the potential for any group of persons to suffer a substantial unavoidable loss of income or wealth?	NO
<p>The regulatory impact assessments listed under 2.3 provide analysis on the size of the potential costs and benefits for the policy items included in the Supplementary Order Paper that are subject to the regulatory impact analysis requirements. It should be noted that, for the remaining policy items in the Supplementary Order Paper, there is little or no publicly available analysis on the size of potential costs and benefits, as these items have been assessed as having no or a very minor impact on businesses, individuals, or organisations.</p>	

2.6. For the policy to be given effect by this Bill, are the potential costs or benefits likely to be affected by:	
(a) the level of effective compliance or non-compliance with applicable obligations or standards?	YES

(b) the nature and level of regulator effort put into encouraging or securing compliance?	YES
<p>The effectiveness of taxation legislation is, by its nature, reliant on effective and voluntary compliance. The level of compliance or non-compliance with specific applicable obligations or standards, and the nature of regulator effort, may have an impact on the potential costs or benefits for some policy items to be given effect by the Supplementary Order Paper. For the appropriate policy items, this may be discussed in more detail in the regulatory impact assessments listed under 2.3.</p>	

Part Three: Testing of Legislative Content

Consistency with New Zealand's international obligations

3.1. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with New Zealand's international obligations?
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No formal steps to determine whether the policy to be given effect by this Supplementary Order Paper is consistent with New Zealand's international obligations.
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Consistency with the government's Treaty of Waitangi obligations

3.2. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with the principles of the Treaty of Waitangi?

No formal steps have been taken to determine whether the policy to be given effect by this Supplementary Order Paper is consistent with the principles of the Treaty of Waitangi.

Consistency with the New Zealand Bill of Rights Act 1990

3.3. Has advice been provided to the Attorney-General on whether any provisions of this Bill appear to limit any of the rights and freedoms affirmed in the New Zealand Bill of Rights Act 1990?	YES
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The Attorney-General has agreed to receive advice from the Ministry of Justice on whether the Supplementary Order Paper is consistent with the New Zealand Bill of Rights Act 1990.

Offences, penalties and court jurisdictions

3.4. Does this Bill create, amend, or remove:	
(a) offences or penalties (including infringement offences or penalties and civil pecuniary penalty regimes)?	NO
(b) the jurisdiction of a court or tribunal (including rights to judicial review or rights of appeal)?	NO

3.4.1. Was the Ministry of Justice consulted about these provisions?	N/A
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Privacy issues

3.5. Does this Bill create, amend or remove any provisions relating to the collection, storage, access to, correction of, use or disclosure of personal information?	YES
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The Supplementary Order Paper contains remedial amendments to information collection provisions enacted in the Taxation (Income Tax Rate and Other Amendments) Act 2020.
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The remedial amendments clarify the additional disclosure requirements for trusts and widen the categories of trusts that are excluded from providing this information to Inland Revenue.

The Supplementary Order Paper also includes consequential amendments to the Commissioner's information collection power for tax policy purposes – these amendments are technical in nature and insert relevant cross-references to other sections regarding information collection, demands and inquiries.
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3.5.1. Was the Privacy Commissioner consulted about these provisions?	NO
<p>These amendments are remedial in nature to ensure the policy intent of the recent amendments are achieved. The Privacy Commissioner was consulted on the substantive amendments included in the Taxation (Income Tax Rate and Other Amendments) Act 2020.</p>	

External consultation

3.6. Has there been any external consultation on the policy to be given effect by this Bill, or on a draft of this Bill?	YES
<p>Targeted external stakeholder consultation on the design of both the loss continuity and donated trading stock proposals has been undertaken. Among others, the Corporate Taxpayers Group, Chartered Accountants Australia and New Zealand, and members of the New Zealand Law Society Tax Law Committee have been involved in the policy development process.</p> <p>Officials sought information from these stakeholders on whether there were additional types of trusts which should be excluded from the increased disclosure requirements. The 39% rate technical amendment proposals take these submissions into consideration. The proposal on setting the default resident withholding tax rate was discussed with payers of interest.</p> <p>The particular issue with the Mycoplasma bovis proposal in the Bill was raised in submissions to the Finance and Expenditure Committee on the Bill. The Supplementary Order Paper amends the proposal in the Bill in response to the points raised in these submissions.</p> <p>The changes to the bright-line test and unclaimed money proposals have not been consulted on externally.</p>	

Other testing of proposals

3.7. Have the policy details to be given effect by this Bill been otherwise tested or assessed in any way to ensure the Bill's provisions are workable and complete?	NO
<p>All proposals in the Supplementary Order Paper have been reviewed by internal operational subject matter experts under Inland Revenue's standard process for assessing the administrative impacts of any new policy initiatives and ensuring they are workable and complete. This involves assessing whether systems need to be changed and, if so, whether formal testing needs to be carried out. None of the measures in the Supplementary Order Paper have required formal testing.</p> <p>The proposals in the Supplementary Order Paper have been subject to the Generic Tax Policy Process to the extent possible, the purpose of which is to promote and improve the workability of proposals. However, in most cases, the proposals have only been subject to more targeted consultation due to tight timeframes for developing the policy.</p>	

Part Four: Significant Legislative Features

Compulsory acquisition of private property

4.1. Does this Bill contain any provisions that could result in the compulsory acquisition of private property?	YES
<p>Clause 100K(3) of the Supplementary Order Paper makes three categories of unclaimed money unclaimable. These categories of unclaimed money are those that are:</p> <ul style="list-style-type: none">a. older than 25 years of ageb. \$100 or less, andc. without any identifying information associated with them. <p>This is required to ensure that Inland Revenue's publicly funded resources are used effectively. It focuses Inland Revenue's resources on amounts of money which are economic to administer and whose owners have the greatest likelihood of being located.</p> <p>The Supplementary Order Paper changes the limitation period of 60 years on the ability of a claimant to claim unclaimed money in the current Bill to 25 years. While this removes a property right, it also reflects the reality that the likelihood of unclaimed money being claimed decreases as time passes. Furthermore, it is impractical for the Crown to retain unclaimed money as a contingent liability on its accounts indefinitely.</p> <p>However, Inland Revenue's ability to use its existing tax information to match owners of unclaimed money with their money will result in a greater number of unclaimed money owners being reunited with their money, and fewer amounts of unclaimed money going unclaimed.</p>	

Charges in the nature of a tax

4.2. Does this Bill create or amend a power to impose a fee, levy or charge in the nature of a tax?	NO
<p>Given the Supplementary Order Paper is amending tax legislation, it does contain provisions that create or amend a power to impose a charge that is a tax. However, for the purposes of this statement, the answer is "No" as per the scope of this question explained in the guidance.</p>	

Retrospective effect

4.3. Does this Bill affect rights, freedoms, or impose obligations, retrospectively?	YES
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There are policy items in the Supplementary Order Paper that may have retrospective effect, and given the nature of tax, the retrospective application may have some impacts on the rights of taxpayers.

The proposal to extend the bright-line test has retrospective effect in order to limit the time between announcement and application date. This reduces the opportunity for people to rush in and purchase property subject to the five year bright-line before the extended bright-line test applies. However, the retrospectivity is limited as the extended bright-line test would only apply to residential land acquired on or after 27 March 2021 (but will exclude such an acquisition where an offer was made on or before 23 March 2021 by a buyer who could not withdraw their offer before 27 March 2021).

Both the loss continuity proposals and the donated trading stock proposals have retrospective effect in order to provide COVID-19 related support. In April 2020, it was signalled that the loss continuity rules would apply from the 2020–21 income year onwards in order to provide some comfort to taxpayers undertaking capital raising in response to economic conditions. The donated trading stock proposals are retrospective to 17 March 2020 in order to provide relief for donations made in response to COVID-19.

The Mycoplasma bovis proposal has retrospective effect in order to provide relief to farmers that may have had to cull livestock as far back as the 2017–18 income year.

Some of the 39% rate technical amendment proposals apply retrospectively to the date of enactment of the Taxation (Income Tax Rate and Other Amendments) Act 2020 (7 December 2020). This ensures the provisions operate as intended and avoids the confusion of having two different sets of rules for different time periods.

Strict liability or reversal of the burden of proof for offences

4.4. Does this Bill:	
(a) create or amend a strict or absolute liability offence?	NO
(b) reverse or modify the usual burden of proof for an offence or a civil pecuniary penalty proceeding?	NO

Civil or criminal immunity

4.5. Does this Bill create or amend a civil or criminal immunity for any person?	NO
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Significant decision-making powers

4.6. Does this Bill create or amend a decision-making power to make a determination about a person's rights, obligations, or interests protected or recognised by law, and that could have a significant impact on those rights, obligations, or interests?	NO
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Powers to make delegated legislation

4.7. Does this Bill create or amend a power to make delegated legislation that could amend an Act, define the meaning of a term in an Act, or grant an exemption from an Act or delegated legislation?	YES
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The amendments to the increased disclosure rules for trusts include the ability for the Commissioner to vary some of the requirements for certain trusts. This allows flexibility for the Commissioner to relax some of the requirements for certain types of trusts where appropriate due to compliance costs and value of the information that would be provided.

The Bill allows the exemption from the deemed income rule for donations of trading stock to be extended by Order in Council, or for another application period to be specified.

4.8. Does this Bill create or amend any other powers to make delegated legislation?

NO

Any other unusual provisions or features

4.9. Does this Bill contain any provisions (other than those noted above) that are unusual or call for special comment?

NO