CHARTERED ACCOUNTANTS
AUSTRALIA • NEW ZEALAND

Tax Special Interest Group

Proposed Changes to LTC/QC's

Residential Land Withholding Tax (RLWT)

Prepared for: CAANZ

This document is prepared for general information purposes only and highlights some upcoming changes.

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MRA ROBERTS & ASSOCIATES LTD
Chartered Accountants ▲ Taxation Specialists

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QC Amendments
Shareholding Continuity

- Loss of Shareholding Continuity = Loss of QC status
- Period of Continuity
  - Date of Royal Assent to EOY
- Continuity – Commonality of Ownership 50%
- Measurement Criteria
  - Same as for Losses / ICA's
- Changes Effective: 2017/18 Income Year

LTC Amendments

LTC Entry Tax (1)

- Will apply to imputed & unimputed reserves

- **Current**

  (taxed on unimputed revenue reserves only)

  Income = [dividends + balances – assessable income – (balances ÷ tax rate) – exit exemption] x effective interest

- **Proposed**

- Not a QC in immediately preceding year and no unimputed revenue reserves:
  (taxed on imputed & unimputed revenue reserves with credit for ICA)

  Income = [dividends + ICA's – assessable income – exit exemption] x effective interest

- Previously a QC and dividend not fully imputed:
  (taxed on imputed revenue reserves only with credit for ICA's)

  Income = [(ICA balance + terminal tax) / tax rate] x effective interest

LTC Amendments

LTC Entry Tax (2)

Sample Calculation

		Taxable Dividend		
		2016/17	2017/18	2017/18
			Not a QC	QC
Capital Gains - non associated persons	200,000			
Retained Earnings	120,000		120,000	72,000
ICA Balance	28,000		28,000	28,000
Taxable Dividend		48,000	148,000	100,000
Tax @ 33%		15,840	48,840	33,000
ICA Credit			(28,000)	(28,000)
Additional Tax		**15,840**	**20,840**	**5,000**

LTC Amendments

Other Amendments (1)

- **Disposal of Interests – Market Value (MV) of Debt**
  - MV of Debt must take into account any credit impairment

- **Deduction Limitation Rule – Abolished**
  - Will be abolished
  - Except for partnership of LTC's / JV's with other LTC's
  - Effective 2017/18 Income Year

LTC Amendments

Other Amendments (2)

- **Definition of LTC excludes the following companies:**

  i) Companies with registered charities as a shareholder

  ii) Companies with a trustee shareholder that makes a distribution to a tax charity unless charity has no influence over company/trust

  iii) Companies where a trustee shareholder makes a distribution directly/indirectly to a company

  iv) Companies where a Maori Authority has a direct/ indirect ownership interest or receives a distribution

  v) Companies owned > 50% by non-resident individuals/ Foreign trusts with non-resident settlor/appointor if foreign source income > 20% gross income or $10k whichever is greater

- Effective 1/4/17

LTC Amendments

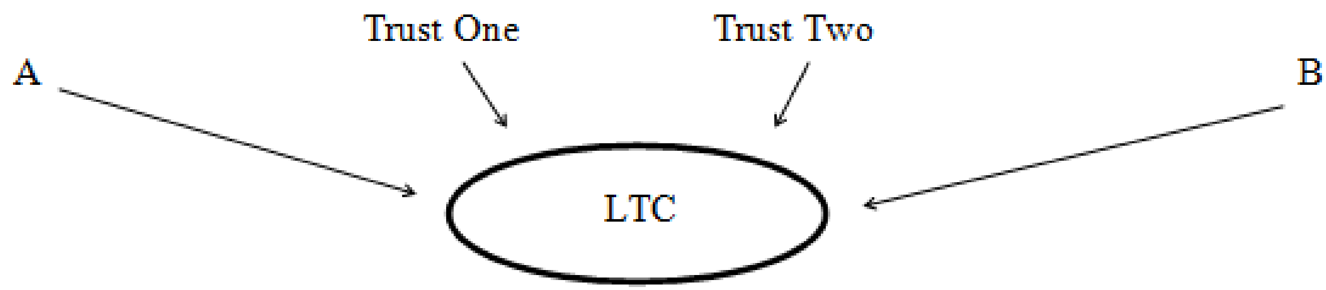
Other Amendments (3)

- **Definition Look Through Counted Owners (LTCO) Amended**
  - To include natural persons in receipt of any distribution (not simply LTC income)
  - Where trust has a direct/indirect beneficial interest for current or one of the three preceding years
  - Effective 2017/18 year in relation to income derived in 2017/18 and subsequent income years

- **More than 1 class of shares**
  - Must have identical rights apart from:
    - i) Voting on Constitutional changes
    - ii) Appointment of directors

Example

Effect of change to LTCO (1)



Assume:

- All shareholders unrelated
- Only beneficiaries in each trust are persons within 2 degrees of relationship
- Trust one distributed only 50% of its LTC income in 2016/17
- Trust two accumulates all 2016/17 income
- On 30/3/17 Trust two acquires Trust one’s interest
- 2017/18 Trust two retains all LTC income but distributed $10,000 non LTC income as beneficiary income

Example

Effect of change to LTCO (2)

Comment	LTCO 2016/17	LTCO 2017/18
Has a look through interest	A	A
Individual has a look through interest	B	B
No look through interest during 2017/18 year	Trust One	-
Received Beneficiary Income in current & previous 3 years	Beneficiary One	Beneficiary One
Look Through Interest & undistributed pre 2017/18 Accumulated earnings	Trust Two	Trust Two
Received distribution		Beneficiary Two
Total	**5**	**5**

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RLWT

When Does It Apply (1)

- **RLWT must be withheld from 01/07/2016 , where**
  - Residential land situated in NZ is sold within 2 years of acquisition (bright-line period), and
  - The vendor acquired the land on or after 01 Oct 15, and
  - The vendor is an "Offshore RLWT person"

    RLWT will apply even if the vendor is not subject to bright line test because other land taxing provisions apply.

  Land acquired prior to 01.10.2015 is not subject to RLWT.

- **Residential Land - defined term**
  - Land that has a dwelling on it;
  - Land with arrangement that relates to erecting a dwelling;
  - Bare land that is zoned residential;
  - Does not include farm land or land that is used predominantly as business premises.

Definitions

Offshore RLWT Person (1)

➢ **Offshore RLWT Person – new defined term**

- Non-NZ citizens and individuals who do not hold NZ residence class visa granted under the Immigration Act.
- Note: *student and work visas are not resident visas*.
- A holder of NZ residence class visa, that has not been in NZ within last 12 months.
- NZ citizens living overseas if they have not been present in NZ within the last 3 years.

- Extends to family trusts, companies and limited partnerships.

Definitions

Offshore RLWT Person (2)

- **Company is an Offshore RLWT Person**
  - If incorporated or registered outside of NZ
  - Is a company and more than 25% of its directors or holders of the shareholder decision making rights are held directly or indirectly by offshore RLWT persons.

- **Limited Partnership & LTC is an Offshore RLWT Person**
  - If 25% or more of the General Partners are offshore RLWT persons, or
  - 25% or more of voting or income interest in the partnership or of the LTC's effective look through interest is held directly or indirectly by Offshore RLWT persons.

- **Partnerships or joint ventures**
  - Status of each partner to be considered separately
  - There is no tainting , each party is considered separately
  - Apportionment may need to be made.

Definitions

Offshore RLWT Person (3)

- **A New Zealand Trust is an offshore RLWT person if**:
  - More than 25% of the trustees or persons with the power to appoint and remove trustees or vary the trust deed, are offshore RLWT persons.
    - The 25% threshold will not apply to beneficiaries.
  - Irrespective of the status of the Trustees, the Trust could be considered an Offshore RLWT person in any of the following circumstances:
    - All natural beneficiaries (incl. Discretionary) are offshore RLWT persons;
    - All beneficiaries (incl. Discretionary) whether natural or not are offshore RLWT persons;
    - A non-natural beneficiary (incl. discretionary), that is an offshore RLWT person, has received a distribution from the trust within the previous 4 years;
    - A natural person beneficiary (incl. Discretionary) that is an offshore RLWT person has received a distribution from the trust totalling $ 5,000 or more in any of the preceding 4 years of relevant disposal of land; and
    - A beneficiary (incl. discretionary) that is an offshore RLWT person and the trust has disposed of residential land within the previous 4 years of the current disposal.

Offshore RLWT Person

Trust Example

- Peter & Simon are only natural beneficiaries of ABC Trust
- Peter lives in Australia & Simon lives in UK
- Mom & Dad are Settlors & Trustees of ABC Trust and they are NZ citizens and live in NZ
- Peter visits Mom & Dad regularly, whilst Simon has not been back to NZ for 4 years because of his intensive study program
- Simon receives a distribution from ABC Trust of $ 4,000 each year to supplement his living & study expenses in UK.

- Mom & Dad as trustees are not "Offshore RLWT Persons", because they themselves are not Offshore RLWT Persons, only Simon is an Offshore RLWT Person, but he has not received more than $5,000 in distributions from the Trust in any of the previous 4 years.

Exemptions

When RLWT is not deducted

- **Sale/ disposal will be excluded from RLWT**
    - Transfers of inherited property to and from Executor
    - Transfers of relationship property
    - When valid certificate of exemption is in hand
        - Must be applied for prior to disposal of land Form IR1103
            - Main Home Exemption
            - Developers, subject to satisfying certain criteria

Exemptions

Developers

- **Using form IR1103 if:**

  - a person is in a business of developing land, dividing land into lots or erecting buildings, and
  - has met all tax obligations (income, PAYE, GST, child support, Kiwisaver, etc) for *the two years before* applying for the exemption certificate; or
  - the person is able to provide security to the IRD on account of income tax

- **Security amount that is greater of:**

  - 10% of the estimated turnover for the sale of the properties or $ 50,000.
  - The security can be provided by bank bond, mortgage over real property, or bond from finance or insurance provider, etc

Exemptions

Main Home Exemption

- **Using form IR1103 if**:
  - A person is disposing of main home
    - Which is used more than 50% of the time as the main home, and
    - 50% or more of the area of the property is used as main home.
  - Supporting evidence that property was used as the main home needs to be provided to IRD, such as water, power bills, etc.
  - No exemption available for the main home
    - Unless valid RLWT Exemption certificate is obtained from the IRD.
    - Must be obtained prior to the disposal of the property.
- As RLWT applies to “offshore RLWT persons” the main home exemption will apply in limited cases.

RLWT

Amount To Be Withheld

- **RLWT that needs to be withheld will be the lowest of**:
  - 33% (or 28% if the vendor is a company) x (current purchase price – vendor's acquisition cost);
  - 10% x the current purchase price;
  - Current purchase price – outstanding local authority rates – security discharge amount

  - Current purchase price is the price the land is being sold for
  - Vendor's acquisition price is the cost of the land to the vendor
  - RLWT must be paid before any disbursements are made at the time of settlement
  - RLWT can be reduced to the extent required to discharge vendor's mortgage obligation (held with NZ registered Bank or NZ licensed Finance Institution)

- **Generally triggered at the time of settlement**
  - Excludes deposits or part payments, where when aggregated
    - They are less than 50% of the purchase price
  - Once 50% is exceeded RLWT obligation will arise

RLWT

Calculation Examples

- **Sue & Bob UK residents invested in rental property in AKL**
  - Property acquired for $ 605,000 in Nov 2015
  - Property is being sold for $ 1,000,000 in Jul 2016
  - Outstanding mortgage with ANZ of $ 500,000
  - Outstanding rates of $ 1,700

- **RLWT will be lower of**
  - 33% x ($1,000,000- $605,000) = $130,350 , or
  - 10% x $1,000,000 = $100,000, or
  - $ 1,000,000 - $ 500,000 -$ 1,750 = $498,250

  - $ 100,000 needs to be withheld and paid over to the IRD by the 20th of the month following the month of settlement (unless triggered earlier)

RLWT

Not a Final Tax

- **RLWT is not a final withholding tax**
  - The vendor is able to claim a credit for the RLWT withheld against the final income tax liability in relation to the property disposal.
  - RLWT credit can be applied to satisfy the person's other income tax liabilities, provided that RLWT paid exceeds income tax liability in relation to the disposal of the residential property.

- **The vendor has a choice to claim the credit in the end of year tax return or will be able to file an interim return**
  - provided that the vendor has no outstanding tax obligations.

RLWT

Obligation to Pay

- **The obligation to pay RLWT**
  - Primarily lies with the vendor's conveyancer or solicitor
  - If the vendor does not have conveyancer or solicitor, the obligation to pay RLWT lies with purchaser's conveyancer or solicitor
  - If neither party has a conveyancer or solicitor, the obligation to pay RLWT rests with the purchaser.
  - Conveyancer not liable for RLWT- but may be liable for penalties
    - Shortfall penalties, late payment penalties, late filing penalties
  - If vendor and the purchaser are associated, the purchaser becomes liable for RLWT.

Contact Us

- We are an Auckland based chartered accountancy firm that specialises in taxation.
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