Elective attributing CFC or FIF

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Act introduced the election for a CFC to be classified as an elective attributing CFC. It also introduced an election for an FIF to be an elective attributing FIF so as to be subject to the CFC rules or the FIF rules, as appropriate, despite exclusion being available under the active business test (in the FIF rules, available under the attributable FIF income method). See ¶26-062.

Non-resident film renter

The income of a non-resident film renter is subject to non-resident withholding tax (NRWT) instead of tax on income deemed to comprise 10% of gross rents. See ¶26-450.

Irreparable damage or damage rendering building useless

Section EE 45(8) has been amended so that proceeds such as the scrap value, from the disposal of an item of depreciable property that is irreparably damaged or is a building rendered useless, are included in the amount derived by the owner of the item. The amendment is effective on 4 September 2010 and applies for the 2011/12 and later income years. An exception is provided for the 2010/11 income year for a person who has an extension of time for filing a return for that year, under the Canterbury Earthquake (Inland Revenue Acts) Order. See ¶5-049.

Capital contribution — depreciable property

In s YA 1, the definition of "capital contribution", as it relates to depreciable property, has been amended, effective 1 October 2010. The amendments to the definition provide that an insurance payment for interruption or impairment of business that is used to purchase replacement property in the 2011/12 or later income year is included in the capital contribution for the replacement property. An exception is provided for a person who uses a different treatment in a tax return filed before 28 August 2012 (the date on which the Taxation (Annual Rates, Returns Filing, and Remedial Matters) Act was first considered by a committee of the whole House). See ¶5-356 and ¶13-164.

Emissions trading scheme

The definition of "pre-1990 forest land emissions unit" in s YA 1 has been amended to ensure that transactions in emissions units which are transferred through certain entities as part of Treaty of Waitangi settlements still give rise to exempt income. The amendment is effective on 9 June 2009 which is just prior to the date any pre-1990 forest land emissions units were allocated to any relevant entities.

Section ED 1B has been amended so that the accrual income rules apply when a party to a negotiated greenhouse agreement receives emissions units in relation to the impact of the emissions trading scheme on the price of inputs. Amendments to s ED 1B amend the accrual accounting rules that apply to industrial allocations of emissions units by extending them to cover the allocation of emissions units for "removal activities". These are activities which result in greenhouse gases being removed from New Zealand's Kyoto Protocol liabilities by means including incorporating them into products for export. The amendments come into effect on 1 July 2010.

The definition of "forestry business" in s YA 1 has been replaced to include forestry activities undertaken solely for the purpose of receiving emissions units, rather than for the production of timber. The amendment comes into effect on 1 April 2008. See ¶5-234.

Employment income

The definition of "employment income" in s YA 1 has been amended to ensure that the income of a shareholder-employee who has elected that employment income is not subject to the PAYE rules remains treated as employment income for the purpose of non-PAYE provisions. Examples of employment income provisions that apply to shareholder-employees are ss CE 1, EA 4 and EI 9. The amendment is effective on 1 April 2008. See ¶5-053.

Insurance pay-outs used to purchase depreciable assets

The Act includes insurance proceeds in relation to an interruption or impairment of business activities which are used to purchase depreciable property in the definition of "capital contribution". See ¶10-200.

Unsuccessful software development

Expenditure incurred in relation to unsuccessful software developments will be deductible where the criteria in s DB 40B are satisfied. See ¶10-220.

Interruption expenditure

Section DZ 20 will permit ongoing expenditure incurred by taxpayers affected by the Canterbury earthquakes to be deductible where the taxpayer's income earning activity has been interrupted, and the taxpayer resumes the income earning activity prior to the 2016/17 income year. See ¶10-655.

In-work tax credit

New amendments provide that:

- a major shareholder in a close company can meet the full-time earner requirement even if the shareholder does not derive gross income for the income year
- a person will still meet the full-time earner requirement if that person is receiving weekly ACC compensation as a surviving spouse, civil union partner or de facto partner.

See ¶12-140.

Depreciation

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Act makes a number of earthquake related amendments to the depreciation rules. Many of these are temporary in nature, designed to provide relief to taxpayers affected by the Canterbury earthquakes. The changes include:

- An item of depreciable property is treated as being available for use despite access to it being denied as a result of a restriction imposed in the aftermath of the Canterbury earthquakes. See ¶13-044.
- The definition of "capital contribution" has been amended to include insurance proceeds received in relation to an interruption or impairment of business activities where the proceeds are used to purchase replacement depreciable property. See ¶13-164 and ¶5-356.
- A deemed sale and purchase where damaged assets are assessed as uneconomic to repair. See ¶13-300.
- A cap on depreciation recovery income where insurance is received for assets which are repairable. See ¶13-300.

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- An optional timing rule for income and deductions when assets are uneconomic to repair or irreparably damaged. See ¶13-300.
- An optional timing rule for income and deductions for assets which are damaged but repairable. See ¶13-300.

Trustee income

Section HC 25(1) was amended with effect from the 2008/09 and later income years to clarify that s HC 25 only applies to income derived by a trustee in an income year that is not also beneficiary income. See ¶25-035.

Livestock valuations

With effect from 1 April 2008, s EC 1(1) was replaced to amend an inadvertent error to restore the business nexus to subpart EC. See ¶27-235.

Investment savings, KiwiSaver and superannuation

Various remedial amendments have been made to the provision governing portfolio investment entities (PIEs) in order to clarify policy intent and drafting errors. The definition of foreign PIE equivalent now includes an Australian managed investment trust (MIT). See ¶29-110.

In addition, changes were made to the application of the foreign investor tax credit rules to foreign investment PIEs. The new rules apply from the 2013/14 income year. Further amendments provide that transitional residents that have elected a zero tax rate cannot benefit from certain tax credits. See ss HM 51(1)(b) and HM 53(1)(b)(ii) and ¶29-140.

The Taxation (Annual Rates, Returns Filing, and Remedial Matters) Act also introduced a provision to clarify the position of employee contributions to KiwiSaver after their end-payment date. If a member wants to cease contributing to their KiwiSaver scheme they must give their employer a ''non-deduction notice''. See ¶29-245.

Amendments to the Goods and Services Tax Act 1985

A brief summary of the main amendments made to the Goods and Services Tax Act 1985 by the Taxation (Annual Rates, Returns Filing, and Remedial Matters) Act is set out below.

Accounting basis — liquidators and receivers

New s 19(3B) removes the ability for a liquidator or receiver of a registered person to apply to change the person's accounting basis from a payments basis to an invoice basis. The amendment applies in relation to an application for a change to a registered person's accounting basis received on or after 2 November 2012. Refer to ¶32-078.

Adjustments on disposals before end of adjustment period

Section 21G(7B) has been inserted to clarify that a person must make a final apportionment of input tax when goods or services are disposed of during an adjustment period. The amendment is effective on 2 November 2012. Refer to ¶32-088.

Adjustments for goods and services acquired before 1 April 2011

Section 21H is a transitional provision that specifies which rules — the former change-in-use adjustment rules or the new apportionment rules — should be used for goods and services acquired before the date of introduction of the new apportionment rules on 1 April 2011.

Section 21H(2B) sets out the treatment for assets that have not been adjusted. If input tax was deducted or supplies were zero-rated at the time of purchase, the old apportionment rules apply to the supplies. If a person has not deducted any input tax for the goods or services, they should apply the new apportionment rules.

The amendments are effective on 1 April 2011. A savings provision allows taxpayers who have already applied either the old change-in-use adjustment rules or the new apportionment rules before the amendment was introduced on 14 September 2011 to continue with their chosen treatment.

Refer to ¶32-088.

Imported and secondhand goods acquired before registration

Section 21B(1)(a) has been amended to allow a registered person to claim an input tax deduction in respect of imported and secondhand goods acquired before registration.

Section 21B(4) has been repealed to remove the $5,000 minimum requirement for apportioning goods and services acquired before registration.

Section 3A(3C) has been consequentially amended. The amendments are effective on 1 April 2011.

Refer to ¶32-088.

Tax fraction for secondhand goods

Section 21B(5) has been inserted to provide that when a secondhand good is brought into a taxable activity, the input deduction available is similarly limited to the tax fraction in place when the goods were acquired. The amendment is effective on 1 April 2011. Refer to ¶32-056 and ¶32-088.

Calculation of tax payable — delivery of imported goods

Section 20(3C) has been replaced to prevent a registered person from claiming input tax deductions for goods entered for home consumption (imported goods) when they deliver or arrange the delivery of the goods to a person in New Zealand. Section 3A(4) has been consequentially repealed. The amendments apply from 1 April 2011. Refer to ¶32-022.

Calculation of tax payable — non-taxable use of zero-rated acquisition

Section 20(3J)(a)(iii) has been amended to clarify that the purchaser of goods or services zero-rated under s 11(1)(mb) must account for output tax on any non-taxable use of the goods or services acquired as part of the wider supply. The amendment applies from 1 April 2011. Refer to ¶32-022.

Concurrent use of land

Section 21E(1) has been amended to clarify the application of the ''concurrent use of land'' rules. The change provides that ''concurrent'' means the same part of the land is simultaneously used during an adjustment period for making concurrent taxable and non-taxable supplies. The amendment is effective on 2 November 2012. Refer to ¶32-088.

Information requirements in land transactions

Section 78F requires the recipient of a supply that involves land to provide information to the supplier about their registration status and intentions in relations to the land. This information may then be used by the supplier to determine whether the supply is zero-rated or standard-rated.

Section 78F(5) has been amended to clarify that when a contractual purchaser in a land transaction nominates another person to receive the supply, the information requirements in s 78F(2) are met if the contractual purchaser provides the required information in relation to the nominated person or the nominated person provides the required information.

Section 78F(3) has been amended to clarify that a contractual purchaser may provide the required information and the supplier may rely on it.

The amendments are effective on 1 April 2011. Refer to ¶32-088.

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Chapter 2 TAX RETURNS

	Para
Background	2-010
Assessment and Collection of Income Tax	2-015
Calculation of Tax	2-105
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¶2-010 Background [TAA ss 33, 33A, 35, 36, 37, 40, 138E(1)(a)]

Except for certain multi-rate PIEs and those persons not required to file returns under s 33A of the Tax Administration Act 1994 or those whose income statement is deemed to be a signed return (see ¶2-032), every person must furnish a return in the prescribed form for the previous tax year. A tax year runs from 1 April to the following 31 March. See ¶1-080.

The Commissioner is required to give public notice of the dates when returns should be filed, though failure to give notice does not affect a person's liability to file a return by the due date. Notice is given by publication in the *Gazette*, and by newspaper and television advertising. Due dates are also shown on the return forms and information literature posted to most people. The Commissioner may extend the time within which a return must be furnished. However, any unfavourable exercise of that discretion is not open to challenge.

Certain individuals outlined in s 33A(2) must furnish a return, such as provisional taxpayers, non-residents and those who have made a tax loss or have a tax loss carried forward. Companies and persons carrying on business for any part of an income year must also furnish returns, regardless of whether they have incurred a profit or a loss. Equally important is the capacity in which an individual has received income. For example, an individual might derive income personally, as the agent for a non-resident, in the capacity of trustee or as a member of a partnership. Different tax returns are required in each case. See ¶2-015.

The obligation is discharged only when the return is received by an Inland Revenue (IR) office. It is sufficient if the person can prove that a correctly addressed return was posted to the appropriate IR office. See *Martin Holdings Ltd v C of IR* (1973) 1 NZTC 61,081 (SC). See also *Case* T23 (1997) 18 NZTC 8,148, in which the Taxation Review Authority ruled that a tax return is furnished when it is received at IR's post office box.

ASSESSMENT AND COLLECTION OF INCOME TAX

¶2-015 Form and content of return [TAA ss 33(2), 34, 40, 42]

General content

A return must contain the information and must be accompanied by all the documents required under any of the Inland Revenue Acts. This includes a notice of self-assessment (see s 33(2) of the Tax Administration Act 1994). In practice, Inland Revenue tax return forms contain a notice of self-assessment and declaration at the end of the form. Returns required to be furnished in writing must be signed. Returns furnished by electronic means must be transmitted in an electronic format prescribed by the Commissioner under s 35, 36, 36A, 36AB, 36B, 36BB, 36BC or 36E of the Tax Administration Act; see ¶2-019 and ¶3-022.

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Persons need not personally fill out and sign their own returns. A return made by or on behalf of any person is deemed to have been made by the person or on his or her authority, unless the contrary is proved. See ¶2-036.

Return types

The main returns are as follows.

Individuals

- Form IR 3 is for self-employed individuals and others who pay provisional tax on investment or business income (including partners). Some private domestic workers (eg nannies or gardeners) who pay tax as IR 56 payers may have to file an IR 3 return.
- Form IR 3B (supplementary to form IR 3) is for business or professional taxpayers trading on their own account with business income, who are required to analyse their income and deductions.
- Form IR 3F (supplementary to form IR 3) is for taxpayers carrying on a farming business on their own account.
- Form IR 3NR is for non-residents.

Companies

- Form IR 4 is for companies, incorporated societies, public authorities, unit trusts, certain group investment funds and state enterprises liable for tax. (Note that only one return is required for companies within a consolidated group.)
- Form IR 4F is used if the company keeps an FDP account.
- Form IR 4J is used if the company is required to keep an imputation credit account.
- Form IR 4S is for company shareholders' details.

Trusts and estates

- Form IR 6 is for trustees in relation to trust and estate income. (When an estate has income from a farming business, form IR 3B or IR 3F can also be used.)
- Form IR 6B is required if income is distributed to beneficiaries.
- Form IR 307 is used if distributions of beneficiary income or taxable distributions are made to beneficiaries from a foreign or non-complying trust.

Partnerships

- Forms IR 7 and IR 7P are for partnerships (see ¶2-050). In addition, partnerships receiving income from business or rental activities must also file one of the following:
  - ☐ a fully completed accounts information form IR 10
  - ☐ a set of the partnership's financial statements
  - ☐ a completed form IR 3F (farmers), IR 3B (other business) or IR 3R (rents).

Each partner must file a personal tax return (form IR 3) with all income including a share from the partnership. The partnership is not assessed for tax, but each partner is liable to pay tax on his or her share of income.

Other

- Form IR 8 is for Maori authorities.
- Form IR 9 is for clubs and societies.
- Form IR 44 is for registered superannuation funds.
- Form IR 44E is for group investment funds.

An individual may be required to file several different returns according to the particular capacities in which he or she acts.

Example:

Mr TP is a partner of a four-member law firm. He owns several properties in his own name which he rents out. He also acts as a trustee for several trusts established on behalf of his clients. Mr TP would need to ensure that he filed the following returns of income:

- form IR 3, which would include his share of partnership income and the rents received from his properties
- form IR 6, of which a separate form would need to be filed for each of the trusts for which Mr TP acts as trustee
- form IR 6B, if any income is distributed to beneficiaries, and
- form IR 7, which would include the income earned by the law firm of which Mr TP is a partner.

As a variation on these facts, if some of the rental properties were owned by a family company and some jointly with his wife in partnership, Mr TP would need to ensure that the following returns were also filed:

- form IR 4, which would include the rental income earned by the family company
- form IR 4J, and
- form IR 7, which would include the rental income earned by Mr TP and his wife in partnership.

¶2-016 Individual tax return — a worked example

The practical example below demonstrates how the tax payable by or refundable to an individual taxpayer for the tax year ended 31 March 2013 might be calculated.

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Example:

Jenny is a full-time employee of a local company. For the tax year ended 31 March 2013 she had a gross salary of $35,000 and pay as you earn (PAYE) of $5,250 (excluding Accident Compensation Corporation (ACC) earner levy). She is married to Bruce, a real estate agent, who earns approximately $65,000 pa in commission and salary. They have two children at primary school.

Jenny has the following additional sources of income during the tax year:

- Interest was credited to her account by the bank. The gross amount of interest was $125. Resident withholding tax was deducted by the bank from this amount. The bank held her Inland Revenue (IR) number.
- The sum of $5,200 was received as a court-ordered maintenance payment from her former husband.
- Jenny received payments of $900 from the ACC during a period she was unable to work. This was because of an accident incurred while she was on a recreational hike.
- While at work Jenny took her wedding ring off during cleaning and lost it. Her insurance policy covered this loss and has paid out $300 on her claim.
- She also received a travel allowance of $150 from the company to reimburse her for the additional cost of getting to work on Sundays when there was no bus service available. This was not included in her summary of earnings.

Jenny incurred the following expenditure during the tax year, and this expenditure was not reimbursed by the company she worked for:

- travelling to work, $550
- dry-cleaning of work clothes, $70
- the fee for determining her income tax liability, $120 (see Note 1)
- child care during the school holidays, $910.

Jenny has receipts for the following donations made during the tax year:

- $20 to the Red Cross
- $25 to the Foundation for the Blind
- $12 to the National Party
- $15 to the Hamilton East Soccer Club
- $10 to Amnesty International
- $100 to the Hamilton East Primary School ($60 for school fees and $40 as a general donation).

	$	$	$
Annual gross income (ss BC 2, BD 1, BD 3)			
Salary (employment income, s YA 1) (s CE 1(1)(a))			35,000
Interest received (s CC 4)			125
Earnings-related compensation (ACC) (s CF 1(1)(a))			900
			36,025
Excluding personal income:			
insurance recovery			
Excluding exempt income (subpart CW):			
reimbursing travel allowance (s CW 18)			
payment for court-ordered maintenance (s CW 32)			
Less annual total deduction (s BC 3):			
determining tax liability, see Note 1 (s DB 3(1))			120
Equals net income (loss) (s BC 4)			35,905
Less available tax losses (s BC 5)			0
Equals taxable income (s BC 5)			35,905
multiplied by basic tax rate (sch 1, pt A), 10.5% up to $14,000, 17.5% from $14,001 up to $48,000			
Equals income tax liability before use of tax credits (ss BC 8, LA 2)			5,304
Less:			
Non-refundable credits (s LA 4)		0	
Refundable credits (s LA 4)		0	
PAYE (ss LA 6, LB 1)		5,250	
Resident withholding tax (s LA 6)		22	
			5,272
Equals:			
Terminal tax (ss BC 8(3), LA 1–LA 4)			0
Remaining credits (s LA 5)			
Amount owing by the person			32

▶ *Notes:* (1) Even though Jenny is not required to file a return for the 2013 tax year, the fee charged by her tax advisor for determining her tax liability and tax credit entitlement would be deductible under s DB 3.

(2) The housekeeper (now repealed) and charitable donations tax credits are excluded from the determination of a person's income tax liability. To claim these tax credits, a separate claim form must be completed and filed with IR. See ¶11-060.

¶2-017 Dates for furnishing returns [TAA ss 37(1), 40(3)]

The due dates for the filing of annual returns of income are:

- 7th day of the 4th month after the end of the person's corresponding income year for any person with a late balance date (ie 1 April to 30 September), and
- 7 July for all other persons.

Note that these dates do not apply to persons who have their returns prepared and filed by tax agents. See ¶2-018.

When received in time

A return is treated as being filed only when it has been received at an Inland Revenue Department office. See s 40(3) of the Tax Administration Act 1994.

Example:

This section was considered by the Taxation Review Authority where it was held that a tax return was delivered to the Commissioner when it was received at his private bag at the Post Office. See *Case* T23 (1997) 18 NZTC 8,148.

Canterbury earthquake relief measures

As part of the tax relief measures following the Canterbury earthquakes, the Commissioner may extend the time limits under the Inland Revenue Acts, including the due date for filing tax returns. Taxpayers affected by the earthquake and its aftershocks can apply for an extension of the due date: Canterbury Earthquakes (Inland Revenue Acts) Order 2011.

¶2-018 Extension of time to file returns [TAA ss 34B, 37]

Any person can apply to the Commissioner for an extension of time to furnish an annual income return. See s 37(3) of the Tax Administration Act 1994. This provision is likely to be used where the person does not have an extension of time arrangement through a tax agent (see below). Provided the application (which can be made verbally or in writing) is made before the due date for filing the return, the Commissioner may grant the extension if he thinks it "proper in the circumstances". Standard practice statement SPS 09/03, "Extension of time applications from taxpayers without tax agents", published in *Tax Information Bulletin* Vol 21, No 9, December 2009 at 27, gives the following examples of reasons Inland Revenue (IR) considers appropriate for extending the filing date:

- the person is unable to obtain the necessary information to file the return (eg is waiting to receive a summary of earnings from IR)
- the person has been overseas and needs extra time to prepare a return (depending on departure and returning dates)
- ill health, hospitalisation or injury of the person or the person's family member (eg partner or dependant)
- the person is awaiting the finalisation of financial statements for a related person with a different balance date.

IR will also take into account the person's history of filing returns.

The Commissioner may extend the due date for filing returns for those taxpayers affected by the Canterbury earthquake: see ¶2-017.

Tax agents

The Commissioner can also grant extensions to tax agents. See s 37(4) of the Tax Administration Act. A tax agent is a person who is eligible to be a tax agent and who is listed as a tax agent by the Commissioner. To be eligible to be a tax agent, the person must prepare the returns for 10 or more taxpayers and be a person who is:

- a practitioner in a professional public practice
- carrying on a business or occupation in which returns of income are prepared, or
- the Maori Trustee.

To be listed as a tax agent the Commissioner must be satisfied that the person is entitled to be a tax agent and that the listing will not adversely affect the integrity of the tax system.

The Commissioner may extend the time for filing for tax agents to not later than one of the following days:

- where the return is for the year ending 31 March, the day is the following 31 March, or
- where the return is for any year ending on an annual balance date between 31 March and 1 October, the day is the following 31 March.

The Commissioner may cancel an extension of time arrangement if a tax agent has not filed the required number of tax returns by the dates that the Commissioner has specified. For example, IR's April 2005 extension of time arrangement with tax agents for the *filing period* 1 April 2011 to 31 March 2012 sets four sets of targets for tax agents: standard, e-file, late balance date targets and negotiated personal dates (see IR's publication IR 9XA, "Extension of time (EOT) arrangements, Tax agents' extension of time agreement"). The targets set four interim dates throughout the year by which tax agents have to file a certain percentage of their clients' tax returns. The effect of s 37(4A) of the Tax Administration Act is that if these targets are not met, the Commissioner can cancel the extension of time arrangement with regard to those non-complying tax agents.

Extension of time for group companies

The extension of time arrangements also apply to group companies. Group companies can nominate a company officer to act as tax agent for the group. Statements and returns for all companies in a group are to be sent together. See *Tax Information Bulletin* Vol 3, No 2, September 1992 at 4.

¶2-019 Electronic filing [TAA ss 23, 36, 36A, 36AB, 36C, 36CA, 40]

The Commissioner may give approval to any person or GST-registered person and/or the person's agent to file information electronically. The return must be filed in the prescribed format and approval may be subject to any conditions specified by the Commissioner.

Prior to 2 November 2012, information contained in a person's return that was electronically filed was required to be retained in a signed, hard-copy form for at least seven years (with the exception of employer monthly schedules (see ¶3-131) and annual reconciliation statements of multi-rate PIEs). However, an amendment contained in the Taxation (Annual Rates, Returns Filing, and Remedial Matters) Act 2012 removes the requirement for a signed, hard-copy to be retained where the return has been filed electronically and the information is retained in an electronic form meeting the requirements of s 25 of the Electronic Transactions Act 2002.

A further amendment by the Taxation (Annual Rates, Returns Filing, and Remedial Matters) Act 2012 means that an agent may sign any hard-copy form of a return where the return is filed electronically. This amendment also applies from 2 November 2012. Prior to the amendment, the legislative requirement was that the taxpayer (or GST-registered person in the case of GST returns) was required to sign the hard-copy form of the return.

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Chapter 12 CHILD SUPPORT AND FAMILY SCHEME

Para

Child Support 12-010
Family Scheme 12-110

CHILD SUPPORT

¶12-010 Background [CHS ss 1–20, 58]

The child support scheme operates under the Child Support Act 1991. The aim of the legislation is to ensure that:

- parents take financial responsibility for their children
- custodians receive financial support from liable parents, the level of which conforms with legislatively fixed standards
- the costs to the Government of providing benefits to custodians are offset by a fair contribution from liable parents, and
- a system exists for the collection and payment of child support.

The Child Support Act is one of the Inland Revenue Acts. It is administered by Inland Revenue (IR). IR accepts applications for child support from custodians, calculates how much support a liable parent is required to pay and collects the amount due.

If the custodian is a beneficiary, any child support payments collected by IR are first applied to paying the custodian's benefit, subject to any offset arrangements. See ¶12-025 and ¶12-030. Any surplus, after the Government's costs of the benefit are met, is then paid directly to the custodian. If the custodian is not a beneficiary, any child support payments collected by IR are paid directly by IR to the custodian without deduction.

IR also collects and pays domestic maintenance (ie maintenance paid to a spouse or partner where there are no children), court-ordered child maintenance and any maintenance payable under a voluntary agreement (ie an agreement to pay child support where both parties agree on the amount to be paid).

Participation in the child support scheme is compulsory for those people who:

- receive a social security benefit (eg a domestic purposes benefit, an unsupported child benefit or a sole parent benefit)
- are required to make financial contributions under the Child Support Act, or
- are required to make maintenance payments under a court order.

Custodians who do not receive a benefit can choose whether they want to have child support collected by IR under the child support scheme.

Voluntary agreements

Often a liable parent and custodian will choose to enter into a voluntary agreement for child support, rather than adopt the level of support prescribed in the Child Support Act. However, if the custodian is a beneficiary, the amount of any child support voluntarily agreed between the parties must be more than the amount that the liable parent would have been required to pay under the formula set out in the Child Support Act. Voluntary agreements do not need to be registered in the Family Court.

IR will administer voluntary agreements where an application is made by both parties and the application is accompanied by a signed written agreement for regular payments of at least $520 per annum to be paid by the liable parent to the custodian. The custodian, children and liable parent must be New Zealand citizens or residents.

Once IR accepts an application to administer a voluntary agreement, only IR can collect the payments. Notification of changes to a voluntary agreement should be made to IR on form IR 108.

Voluntary agreements do not need to be administered by IR unless the custodian or the liable parent is required to comply with the Child Support Act.

Terminology

Child	A child qualifies for child support if he or she is a New Zealand citizen (or ordinarily resident in New Zealand) who is under 19 years of age, is not married (or living in a de facto relationship) and is not financially independent.
Eligible custodian	An eligible custodian is the sole or principal provider of ongoing daily care of the child (or someone who shares daily care equally with another) and lives apart from the liable parent.
Liable parent	A parent who is liable to pay child support. Liability arises if IR accepts a custodian's application for assessment of child support.

Education and information

IR provides booklet IR 100, "Helping you to understand child support", August 2012, to assist paying persons and custodians at the beginning of their child support obligations. Alternatively, further information on child support can be found on IR's website at www.ird.govt.nz/childsupport.

▶ ***Note:** Child support reforms*

On 5 October 2011 the Child Support Amendment Bill was introduced. This Bill proposes a range of changes to the child support regime following a substantive review period that invited public comment regarding the best operation of the child support system. The Bill was reported back from the Social Services Committee on 31 October 2012.

The changes proposed in the Bill fall into three broad categories:

- a new child support calculation formula
- secondary changes to update the child support scheme, and
- amendments to the payment, penalty and debt rules for child support.

Child support formula

The Bill introduces a new child support formula that is intended to provide a more equitable system of financial support in a variety of circumstances.

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The new formula bases child support payments on:

- a wider recognition of shared care for formula assessment calculations, that is based on 28% of nights in a year
- the income of both parents, and
- the estimated average expenditures for raising children in New Zealand.

Secondary changes to update the child support scheme

The Bill also includes amendments that will:

- allow IR to rely on parenting orders and agreements when establishing care levels
- give the Commissioner greater discretion in respect of how care is measured
- more closely align the definition of "income" for child support purposes with the broader definition of "family scheme income" for Working for Families purposes. See ¶12-110
- recognise re-establishment costs, following a separation, as an administrative review ground in certain circumstances, and
- reduce the qualifying age of children subject to the child support scheme from under 19 to under 18, unless they are 18 and attending school.

Changes to payment, penalties and write-off rules

New rules will be introduced to encourage parents to make timely payments of child support including:

- a new two-stage initial penalty, with the current full 10% only being charged if the debt remains unpaid after seven days
- a reduction in the incremental monthly penalty from 2% to 1% after a year of non-compliance
- a broader ground for writing penalties off.

Application dates

The amendments in the Bill apply in two phases. If passed in its reported back form, the new child support formula will apply for assessment periods from 1 April 2014. The majority of the other changes to the child support scheme will apply from 1 April 2015.

Calculation and payment

¶12-015 Calculation of child support [CHS ss 29–31, 40, 44, 44A, 45, 72]

Under the Child Support Act 1991 the person caring for the child (ie the custodian) generally applies to Inland Revenue (IR) for a child support assessment to be made. If the custodian is not a beneficiary, the custodian can choose whether or not to apply for child support. A liable parent is also able to apply for a child support formula assessment. Applications for child support formula assessments should be made using form IR 101.

To determine how much child support a liable parent is required to pay IR applies a standard formula. The standard formula uses a process that works out the liable parent's taxable income, less a living allowance, and multiplies the result by a percentage based on the number of children the liable parent pays child support for.

Once the calculation has been performed an assessment notice is sent to the liable parent detailing the amount of child support to be paid and when the payments are to be made. The custodian also receives a notice showing the amount of the liable parent's assessment.

Child support formula

The standard formula used to determine a liable parent's annual child support payments is:

$$(a - b) \times c$$

where:

a	is the taxable income of the liable parent, up to a maximum amount
b	is a living allowance, and
c	is a percentage rate between 18% and 30%, depending on the number of children the liable parent pays child support for.

▶ *Note:* The Child Support Amendment Bill provides for new child support formula for assessment periods from 1 April 2014. See ¶12-010.

Taxable income

IR uses three methods to assess the taxable income of a liable parent. They are as follows:

- If the liable parent's income is only from the following sources:
  - ☐ salary and wages with PAYE deducted
  - ☐ a benefit, or
  - ☐ interest or dividends subject to resident withholding tax,

  the assessment is based on the parent's taxable income for the preceding year. For example, a child support assessment for the year 1 April 2012 to 31 March 2013 is based on the liable parent's salary and wages earned in the year 1 April 2011 to 31 March 2012. To determine the salary and wages earned the Commissioner uses the employer's wage records for the preceding year. Liable parents in this category are assessed for child support annually in March. The full income earned over the year is not known at that stage and so the assessment is based on the 10 months of income from 1 April to 31 January and two months of estimated earnings. A comparison to the actual figures is made in July and a revised assessment is issued if the income has changed by more than $500. See *Tax Information Bulletin* Vol 11, No 7, August 1999 at 3.
- If the liable parent has income other than salary and wages, a benefit, or dividends and interest (eg self-employed income or rental income), the assessment is based on the parent's taxable income from two years earlier, adjusted for inflation. For example, the child support assessment for a self-employed person for the year from 1 April 2012 to 31 March 2013 is based on the tax return he or she filed for the 2010/11 tax year, increased by the Consumers Price Index for the 12-month period before the start of the child support year to account for inflation. The inflation factor is set each year. Assessments for this category of liable parents are made in February.
- If the liable parent is based overseas, the child support assessment is based on the parent's overseas income and any New Zealand income, for a period equivalent to the New Zealand tax year. Assessments are made in February each year.

If a liable parent's taxable income for a tax year has not been assessed, IR can determine that person's income on the basis of "income and any other particulars known to the Commissioner".

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Living allowance

An amount is deducted from the taxable income of the liable parent as a living allowance for that parent. The amount deducted depends on the personal circumstances and living arrangements of the liable parent, and takes into account their other family obligations. The amount of the living allowance is based mainly on gross benefits from Work and Income New Zealand.

From 1 April 2012 to 31 March 2013, the living allowance rates are as follows:

Living arrangement	Allowance
Single with no children living with the liable parent	$14,679.00
Married/de facto/in a civil union with no children living with the liable parent	$19,969.00
Single or married/de facto/in a civil union with:	
■ one child living with the liable parent	$28,240.00
■ two children living with the liable parent	$31,222.00
■ three children living with the liable parent	$34,205.00
■ four or more children living with the liable parent	$37,187.00

Percentage rate

The percentage rate used in the standard formula depends on the number of children for whom the liable parent must pay child support.

Where the liable parent is not in a shared care arrangement with the custodian, the percentage rates are:

Number of children	Rate (%)
one	18
two	24
three	27
four or more	30

Different rates apply where a shared care arrangement exists. See ¶12-030.

Minimum and maximum child support liability

There is a minimum amount of child support to pay, even if the liable parent has little or no income. The minimum amount is revised each year. It is calculated as the minimum liability for the immediately previous tax year adjusted by the movement in the Consumers Price Index for the year ending with the December quarter prior to the tax year to which the increase will apply.

The minimum child support liability is $848.00 pa (or $16.30 a week).

There is a maximum amount of taxable income for the purposes of the standard formula. It is determined each year and is calculated as 2.5 times the ordinary time average wage as published by the Department of Statistics.

The maximum taxable income threshold for the 2012/13 tax year is $126,577.00.

There is an online calculator available on IR's website at www.ird.govt.nz/childsupport.

Example 1:

Mr Jones and Mrs Jones are separated. Mrs Jones has custody of the two children from the marriage. Mr Jones is now living by himself. Mr Jones only derives income from salary and interest, and his taxable income in the 2011/12 tax year was $45,000. Mr Jones' child support liability for the year commencing on 1 April 2012 is as follows:

Income	$45,000
less living allowance	$14,679
Balance	$30,321
Multiplied by the two-child percentage	24%
Child support liability	$7,277.04 pa ($139.94 per week)

Example 2:

Mr Smith and Mrs Smith are separated. Mr Smith has custody of the three children from the marriage. Mrs Smith is now living by herself. Mrs Smith's taxable income for the 2011/12 tax year from her business amounted to $50,900. Mrs Smith's child support liability for the year commencing on 1 April 2012 will be:

Income (after inflation adjustment of 3.4%)	$50,900
less living allowance	$14,679
Balance	$36,221
Multiplied by the three-child percentage	27%
Child support liability	$9,779.67 pa ($188.07 per week)

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Election to estimate income

A liable parent whose child support liability is assessed by the application of the standard formula can apply to have that liability recalculated if he or she estimates that his or her current year taxable income will be 85% or less of the taxable income used in the assessment. This option to estimate income is not available to child support liabilities determined by court orders or under voluntary agreements.

Example:

Bob earned $40,000 employment income in the previous tax year but will earn only $20,000 this year. Bob can apply to IR to have his child support assessed on $20,000, because it is at least 15% less than his taxable income from the previous tax year.

The Commissioner can give effect to an election for estimation only after receiving notice in writing from the liable parent, so it is advisable for the liable parent to make the election as soon as it is known that his or her income is going to drop. An application for an estimate can be made to IR using form IR 104 or by letter. The application must be accompanied by information and evidence that, in the Commissioner's opinion, is sufficient to support the liable parent's estimate of income. Examples of suitable evidence would be new pay slips showing the reduced income or a letter from the liable parent's employer or accountant advising the reduced income details.

Liable parents who are required to file a tax return, but have not done so, will have their child support liability assessed as if they had not made an election to estimate their income.

The amount that liable parents have to pay is capped at what they would have had to pay had they not estimated their income. Liable parents who revoke their estimation or no longer meet the 85% threshold will have their child support liability assessed on what they would have had to pay had they not estimated their income.

Income may be estimated more than once a year. Each estimate must always be 85% or less of the income used to calculate child support. If an estimate is made within three months of the last estimate, the income must also change by more than $500.

Liable parents can estimate their income part-way through the child support year if they suffer a reduction in income. In such a situation, liable parents who have already extinguished their liability for the full year do not have to pay the minimum payment of $16.30 per week.

Example:

A single liable parent pays child support for three months based on an income of $36,000 a year. He becomes unemployed and estimates his income for the year at $15,000. His child support liability is reduced to the minimum payable and, because he has already paid more than that, he is not required to pay any more child support for the rest of the child support year.

Example adapted from *Tax Information Bulletin* Vol 11, No 7, August 1999 at 5.

Underestimation

Liable parents who underestimate their child support liability are liable for an underestimation penalty if the sum of the amounts of child support paid is less then 80% of the sum of the amounts that are payable. The penalty is 10% of the difference between the total amount of child support and that which was paid for the relevant year. No interest is charged on underestimated child support.

Further information on estimation

For further information on estimating income for child support purposes, see IR leaflet IR 151, ''Estimating your income'' and IR booklet IR 100, ''Helping you to understand child support'' (August 2012) at 23–27.

¶12-020 Departure from the child support formula assessment

[CHS Pts 6A, 6B, 7, ss 104–106]

In certain circumstances, the Commissioner may make a determination allowing a departure from the formula assessment for calculating child support (see ¶12-015). The determination process can be commenced at the request of:

- a qualifying custodian
- a liable parent, or
- the Commissioner of Inland Revenue.

The procedure is known as an ''administrative review'' and involves a hearing with an independent review officer. The procedures are similar to the process for a Family Court departure order.

Applications by custodians or liable parents

Qualifying custodians or liable parents may make applications for an administrative review of child support where they consider special circumstances exist to depart from the standard formula calculation. All applications for administrative review must be in writing, stating the grounds on which the application is made. The other party to the child support assessment is advised of the application and has the right to reply, confirm or contest any details given by the applicant and the right to attend the hearing.

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The Commissioner can make a determination varying the amount of child support payable when:

- at least one of the special circumstances set out in s 105(2) of the Child Support Act 1991 is satisfied
- it is ''just and equitable'' for the child, the qualifying custodian and the liable parent that an order be made: see *L v W* (1994) 16 NZTC 11,279 (CA), and
- it is ''otherwise proper'' that an order be made: see *C of IR v Cutbush* (1994) 16 NZTC 11,307.

Section 105(2) is an exhaustive list of the special circumstances which are able to be considered as grounds for a determination by the Commissioner or a Family Court departure order. The special circumstances all focus on economic considerations. Some examples of the special circumstances covered by s 105(2) are as follows:

- Where either parent's ability to provide financial support is significantly affected by that parent's duty to maintain another special needs child.
- Where the liable parent's travel costs to enable access to the child are more than 5% of the assessed child support amount.
- Where the liable parent still has a financial interest in a property that the custodian is entitled to live in.

On the other hand, some examples of circumstances which the courts do not consider meet the requirements of s 105(2) are as follows:

- A liable parent having insufficient income to meet outgoings, unless there is something more to take the case out of the ordinary. See *B v C of IR* (1993) 15 NZTC 10,015.
- Factors such as responsibility for the pregnancy, lack of contact between the parents, and lack of contact between the child and the liable parent have no relevance in deciding the amount of child support. In addition, the income and financial position of a child's step-parent do not amount to the requisite special circumstances and are not relevant considerations. See *L v W* (1994) 16 NZTC 11,279 (CA).
- The provision of an interest-free loan to the custodial parent by a liable parent does not create a situation in which it is unjust or inequitable for the liable parent to contribute, or in which special circumstances exist. See *Hudson v C of IR* (1996) 17 NZTC 12,594.
- The special circumstances have to be abnormal or unusual. It is not enough for the applicant to point to some degree of hardship. In a marriage break-up, the existence of hardship is commonplace. See *C of IR v Short* (1995) 17 NZTC 12,029.

A departure order can be made where the court is satisfied that a trading structure or trust is being utilised to reduce a liable parent's assessable income. See *F v S* HC Christchurch CIV-2010-409-20979, 29 September 2011 and *B v X* (2011) 25 NZTC ¶20-034.

There is also provision for an applicant to apply for a suspension of his or her assessed child support liability while an application is in the process of being determined. See *Tax Information Bulletin* Vol 6, No 2, August 1994 at 10.

The Commissioner's jurisdiction to consider an application for a determination is limited to circumstances in which:

- a formula assessment is in force
- the child support payable relates to the child support year starting on 1 April 1994 or any later year, and
- no previous determination of the application has been made by the Commissioner or heard by a court in relation to the same matter or on the same grounds.

¶27-490 Valuation of potatoes not harvested

Inland Revenue (IR) accepts that some farmers and growers value potatoes in the ground and treat them as stock on hand. The practice is based on the view that a credit for the crop should be brought in for the same year in which the expenses are debited. IR accepts the practice, subject to the person consistently following it.

¶27-500 Valuation of nursery plants

Generally, nursery plants that are trading stock must be valued at either market selling value or cost (ie the normal trading stock rules apply). See ¶9-010 et seq. As to whether plants are covered by the current definition of trading stock, see ¶9-120.

In November 2001 Inland Revenue released an interpretation statement on the valuation of nursery plants under the discounted selling price method. See *Tax Information Bulletin* Vol 13, No 11, November 2001 at 68.

See also CCH, *Tax Guide to Farming, Forestry and Fishing*, para 8.9–8.9.2.

¶27-510 Valuation of hives

Ordinary commercial beekeeper hives are a capital asset and are not trading stock for the following reasons:

- The hives as housing have a semi-permanent nature in the same manner as farm buildings, even though the bees themselves have a life of only six to eight weeks.
- There is no ready market for bees as such, and it would not be economic for the beekeeper to raise additional colonies of bees for sale.
- It is a matter of fact that the ordinary commercial beekeeper does not engage in trading in bees or in hives.
- ''Supers'' and ''bottom boards'' which comprise the hive buildings are now generally purchased fully manufactured and are not constructed by the beekeeper.

See CCH, *New Zealand IRD Technical Rulings*, para 48.8 (historical reference only — see ¶1-525).

Chapter 28 FORESTRY AND MINING

Para

Forestry 28-010
Mining 28-053
Petroleum Mining 28-120

FORESTRY

¶28-010 Forestry — background [IT07 s YA 1]

The tax issues associated with any forestry investment or activity can be divided into several identifiable stages:

- the deductibility of pre-investment expenditure, eg consultant's fees: see ¶28-025
- whether the costs of land and timber acquisition can be claimed as a deduction
- the deductibility of the costs of land preparation: see ¶28-027
- the deductibility of costs associated with tree planting and maintenance (eg pruning and thinning): see ¶28-040
- how to return profits arising on the sale of timber and rights in timber: see ¶28-013 and ¶28-015, and
- the deductibility of post-harvest expenditure, eg cleaning up and de-stumping.

The basic rule relating to the taxation of a forestry activity is that any amount derived from disposing of timber or disposing of a right to take timber is income of a person. A person is also allowed a deduction for the cost of timber, provided certain conditions are met. See ss CB 24 and DP 11 and ¶28-014. Income derived from the subdivision or development of forestry land might come within the exemption from income under s CB 21. See ¶28-015. Planting, maintenance and associated costs are allowed as a deduction in the income year incurred. See ¶28-040.

History of the development of the forestry regime

There have been a number of different regimes applied to the taxation of forestry since 1962. Briefly, these are:

- from 1962 to 1978 — capital forestry encouragement loan scheme
- from 1970 to 1985 — forestry encouragement grant scheme
- from 1985 to 1986 — full deductibility of forestry expenditure
- from 1986 to 1991 — capitalisation of certain expenditure to a ''cost of bush account'', and
- from 1992 to date — full deductibility of forestry planting and maintenance expenditure.

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For more detail on these regimes see CCH, *Tax Guide to Farming, Forestry, and Fishing* at paras 9.0 and 9.3.10, CCH, *2002 New Zealand Master Tax Guide* at ¶28-010, and *Tax Education Office Newsletter* No 148, 18 June 1998.

Emissions trading

By ratifying the 2002 Kyoto Protocol New Zealand joined many other nations in making a commitment to reducing the amount of global greenhouse gases. The emissions trading scheme (ETS) was the method New Zealand selected to achieve this objective for the initial period between 2008 and the end of 2012 (the first Kyoto Protocol commitment period). Broadly, the scheme involves pricing of emissions from industry, transport and other sectors. A business must hold sufficient emissions units to reflect the emission levels relating to it. Units are surrendered annually to the Government, although the obligation may also be satisfied by payment at the rate of $25 per New Zealand unit.

The ETS is being phased in, with different commencement dates for different participants. Forestry was the first ETS entrant, joining on 1 January 2008.

The ETS places forest owners in two categories. Pre-1990 forest owners received a once-only allocation of free emissions credits, although these taxpayers were not eligible for credits for the carbon sequestered by their trees. If deforestation occurs, a liability arises under the ETS.

Post-1989 forest owners can elect into the ETS and accrue New Zealand emissions units as the forests mature.

On 7 November 2008, Inland Revenue released two public binding rulings relating to the ETS. The rulings deal with the Crown's ''Projects to Reduce Emissions'' programme which was established by the New Zealand Government in 2003. A total of 41 agreements were entered into. These are the agreements to which the binding rulings apply.

Public binding ruling BR Pub 08/03, ''Projects to Reduce Emissions programme — income tax treatment'', sets out the following:

- Emissions units derived by a participant under a project agreement are treated as income from the participant's business under s CB 1. They are not a capital receipt.
- Emissions units will be derived in each year of the term of a project agreement when the Crown accepts the annual report, or in the case where there is a dispute, on resolution of the dispute.
- If in a subsequent year the participant becomes entitled to receive additional emissions units in respect of emissions reductions achieved in a prior year, the additional emissions units will be derived in the year in which it is determined that the participant is entitled to the additional units.
- If in a subsequent year it is determined that the participant is required to refund emissions units to the Crown (or to pay a cash equivalent), as long as the participant continues to carry on business involving generation of energy for sale or for use in supply of goods or services for sale, a deduction is allowed for the emissions units refunded or the cash repaid in the year the refund is made.
- Amounts derived from the sale of emissions units are income to the participant under s CB 1.
- If the participant continues to carry on business involving generation of energy for sale or for use in supply of goods or services for sale, a deduction is allowable under s DA 1 in the year in which the emissions units are sold for an amount equal to the value of the emissions units at the time of their transfer to the participant.

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- A project agreement is a financial arrangement. However, a participant will not derive income or expenditure under the financial arrangement rules because the consideration for services provided by a participant under a project agreement is an amount equal to the value of the emissions units transferred by the Crown.
- The consideration provided by and payable under the agreement is an amount equal to the value of emissions units transferred to the participant.

Public binding ruling BR Pub 08/04, ''Projects to Reduce Emissions programme — GST treatment'', sets out the following:

- For the purposes of s 8 of the Goods and Services Tax Act 1985, a participant's obligations to the Crown under the project agreement will constitute a supply of emission reduction services to the Crown.
- The value of the supply of the services will be determined at open market value (the ruling sets out general rules that apply to the valuation of the services).
- The time of supply is the earlier of the transfer date set out in the agreement and the date on which the emissions units are actually transferred.

The rulings were published in *Tax Information Bulletin* Vol 20, No 10, December 2008 at 4 and 21.

Further amendments to the tax treatment of emissions units transactions were made by the Taxation (International Taxation, Life Insurance, and Remedial Matters) Act 2009. These amendments deal mainly with transactions outside the forestry sector. See further at ¶5-234, ¶5-062 and ¶10-286, and for a detailed analysis see *Tax Information Bulletin* Vol 21, No 8, October/November 2009, Pt II at 94–99.

Amendments to the ETS enacted in 2012 allow pre-1990 forest land to be deforested, subject to a comparable forest being planted in another location.

New Zealand's approach to climate change is regularly reviewed in response to policies adopted by the international community. In November 2012 the Government announced that instead of joining the second commitment period under the Kyoto Protocol (2013–2020) New Zealand would make its climate change commitment under the alternative option, the Convention Framework. That approach effectively aligns New Zealand with other developed nations such as the United States, China, Japan, Russia and Canada, but not Australia. The Minister for Climate Change Issues confirmed that New Zealand remains committed to the Kyoto Protocol's basic objectives.

Permanent Forest Sink Initiatives

The Permanent Forest Sink Initiatives (PFSI) is a government climate change initiative. Under the scheme, a person who owns land which has been reforested since 31 December 1989, or who owns land which they intend to reforest, can enter into a binding covenant with the Government. This covenant limits the landowner's rights to fell the trees, but in exchange they receive emissions units reflecting carbon capture in the trees.

The existing income tax rules for forestry (primarily in subpart DP) apply to people who carry on a ''forestry business''.

The definition of ''forestry business'' includes forestry activities which are carried on for the purpose of deriving income in relation to an emissions unit. The objective is to cover forest owners who grow a forest purely with the intention of receiving emissions units and who will not harvest the trees. Expenditure by these taxpayers will receive the same treatment as that of ordinary forestry businesses. They can also use income equalisation accounts.

The former definition of forestry business went only so far as to clarify that PFSI foresters were carrying on a "forestry business". See *Tax Information Bulletin* Vol 22, No 1, February 2010 at 24. See *Tax Information Bulletin* Vol 22, No 10, November 2010 at 77.

¶28-013 Disposals of forests and forestry rights

[IT07 ss CB 25(2), DP 10(2), EB 24, GC 1, GC 2]

Any disposals of timber or timber rights by methods other than selling them are treated as having been made at market price for tax purposes. Buyers are able to claim the cost of buying the timber when they harvest it, or the cost of the rights when they sell them.

Land owners who create a forestry right for themselves do not incur a tax liability when they do so. Small forestry owners can, therefore, sell their land but retain ownership of their trees without creating adverse tax consequences. See also ¶28-014 regarding the tax treatment of transfers of property following a taxpayer's death, "in-kind" distributions of property by companies and trusts (including estates) and gifts of property.

¶28-014 Disposals of timber

[IT07 ss CB 24, DP 11, EA 2, FC 1, FC 2, FC 6]

An amount derived from disposing of timber or a right to take timber is income of a person, whether or not the person owns the land on which the timber is situated. Also, if a person disposes of land with standing timber on it, the amount derived from the standing timber is income of the person. However, see exceptions for disposing of land with standing timber at ¶28-018.

The income derived from disposing of timber, the right to take timber or the standing timber is offset by a deduction for the cost of the timber. This includes expenditure not allowed as a deduction in previous years that forms part of the cost of that timber extracted or removed. The income year in which that deduction may be allocated is dependent on whether or not the timber extracted is trading stock, as defined, or revenue account property. If the property is trading stock, the deduction is allocated to the first income year the property becomes trading stock (eg the first year in which it is bought for resale). If the property is not trading stock, it is revenue account property and the deduction will be allocated to the earlier of the income year in which the property is disposed of and the income year in which the property ceases to exist.

Income and deduction spreading provisions are discussed at ¶28-016.

Distributions

Generic rules were enacted in 2005 for the tax treatment of the transfer of property in certain situations. From the 2005/06 income year, if timber, the right to take timber or standing timber is:

- distributed by a trustee of a trust to a beneficiary
- distributed by a company to a shareholder of the company (including an associated person of the shareholder)
- gifted by one person to another person
- transferred from an estate of a deceased person to an administrator or executor of the estate
- distributed by an administrator, executor or trustee of an estate to a person beneficially entitled to receive the property under a will or an intestacy, or
- resettled by one trust on another trust,

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the distribution, gift or resettlement is treated as having taken place at market value on the date the transaction occurs. However, in the case of a transfer from an estate of a deceased person to an administrator or executor of the estate, the transaction is treated as if the transfer at market value occurred on the day immediately before the date of death. See below for an exception for transfers in relation to a deceased estate.

Death of a person

If the disposal and acquisition of timber, standing timber or the right to take timber is transferred on a person's death or on final distribution of the estate, the disposal is treated as a transfer under a relationship agreement, provided the recipient of the property is within the second degree of relationship to the deceased person (for example, the spouse, civil union partner or de facto partner, or the children, siblings or grandchildren of the deceased). Generally, this means that consideration for the transfer is equal to the total cost of timber to the transferor at the date of transfer. See ss FB 6, FB 7, FC 6 and ¶28-023.

¶28-015 Subdivision or development of forestry land

[IT07 ss CB 12, CB 13, CB 21]

An interpretation statement addresses the question of whether amounts derived from the subdivision or development of forestry land were assessable income under s CD 1(2)(f) and (g) of the Income Tax Act 1994 (s CB 12 and CB 13 of the Income Tax Act 2007). The Commissioner has concluded that the exemption under s CD 1(7) of the Income Tax Act 1994 (s CB 21 of the Income Tax Act 2007) could apply to forestry land because forestry could be considered to be a "farming or agricultural business". Any amount derived would not constitute assessable income so long as the following requirements were fulfilled:

- the land sold is the result of the subdivision of a block of land which the vendor, immediately before the subdivision, occupied or used primarily or principally for the purpose of a farming or agricultural business that the vendor carried on
- the land sold is of an area and nature that is currently capable of being worked as an economic unit in a farming or agricultural business, and
- the land is disposed of primarily and principally for the purpose of being used in a farming or agricultural business.

The policy is a departure from Inland Revenue's previous policy which specifically excluded the growing of trees for the production of timber from the meaning of a "farming or agricultural business". The interpretation statement is published in *Tax Information Bulletin* Vol 10, No 4, April 1988 at 43.

¶28-016 Spreading of income and deductions

[IT07 ss EI 1, EJ 1; TAA ss 120P, 142A]

Income derived from disposing of timber or of the right to take timber or of standing timber need not all be returned as assessable income for the income year the timber is disposed of. The vendor can elect to have the income allocated between the income year of derivation and any one or more of the previous three income years. If the income is spread over two or more income years, the deduction for the cost of timber must also be spread to the same income years and in the same proportions. To take advantage of this concession, the person must apply in writing to the Commissioner within one year after the end of the income year in which the income is derived, see s EI 1(3).

Section 120P of the Tax Administration Act 1994 provides a safeguard (until the terminal tax date for the current tax year) from adverse use of money interest implications in respect of the prior years to which the income is allocated. In terms of late payment penalty implications, the Commissioner is required to set a new due date for payment of the increased tax. See s 142A

of the Tax Administration Act. Late payment penalties would only apply where the taxpayer did not pay the increased tax by the new due date. Since 1995 the Commissioner's policy has been to set a new due date two months from the date of assessment. A factor to be considered when making an application under s EI 1 is that the earlier in the one-year application period the application is made, the earlier payment of the increased tax will be required.

¶28-017 Disposal of timber to associated person [IT07 s DP 10(3)–(5)]

Where timber or the right to take timber or standing timber is disposed of to an associated person, the deduction for the cost of timber is limited to the proceeds of sale which are included in income. Where the proceeds of a sale to an associated person are exceeded by the deductible cost of the timber, the excess is transferred to the purchaser. The cost of the timber to the associate is the total of the cost of timber to that person and any amount which the seller of the timber has not been able to deduct (because it exceeded the amount of the sale proceeds). See CCH, *Tax Guide to Farming, Forestry and Fishing*, para 9.2.3.

¶28-018 Disposal of land with standing timber [IT07 ss CB 25, DP 10(1), DP 11, YA 1; TAA s 44C(1), (2)]

A disposal of land with standing timber is treated as a disposal of timber, with the result that the vendor is required to return as income any amounts derived from the disposal. For this purpose standing timber includes immature trees as well as mature trees. This principle of assessability applies irrespective of whether the sale includes other land or other assets or whether the land and timber are the assets of a business. Under s CB 25(2) amounts derived from the disposal of standing timber are not required to be returned as income if the timber is of the following kinds:

- trees that are ornamental or incidental as evidenced by a certificate given under s 44C of the Tax Administration Act 1994, or
- trees that are subject to a forestry right (as defined in s 2 of the Forestry Rights Registration Act 1983) registered under the Land Transfer Act 1952, or
- trees subject to a removal right (profit à prendre) granted before 1 January 1984.

A certificate evidencing the ornamental or incidental nature of trees is obtained from the Ministry of Forestry or some other suitably qualified person. Such certificate is conclusive evidence.

The cost of timber is not expressly limited to the purchase price on disposal plus subsequent deductible expenditure not previously deducted. The cost of timber is to be calculated taking into account other matters.

Example:

Standing timber had been distributed to the taxpayer in specie upon the merger of two companies. The taxpayer sought to include an amount which corresponded to the fair market value of the timber at the time of the in specie distributions as the cost of timber for deduction against income received from the subsequent sale of felled timber. The "cost" of the timber acquired by distribution in specie was held to be the initial cost of acquiring shares in the target company. See *Tasman Forestry Ltd v C of IR* (1999) 19 NZTC 15,147 (CA).

A person is allowed a deduction for the cost of the standing timber so disposed of. The timing of the deduction is governed by s DP 11(3). See ¶28-014.

For further discussion see CCH, *Tax Guide to Farming, Forestry and Fishing*, paras 9.1.3–9.1.7, 9.2–9.2.2.

If the disposal of land with standing timber is income to a person under s CB 25, the cost of acquiring the timber is equal to the amount of the income that arose to the vendor under that section.

¶28-019 Compensation for ceasing logging indigenous timber

In a 1996 Taxation Review Authority decision, a timber logging and farming partnership argued that compensation payments received for the cessation of logging indigenous timber constituted assessable income. However, a bid to have the payment assessed under s 74(2)(b) of the Income Tax Act 1976 (the equivalent of s CB 24 of the Income Tax Act 2007) and to claim a deduction for the cost of the timber under the proviso to that section (now s DP 11) was unsuccessful. The Authority found that the partnership could not take a deduction for the cost of the standing timber as there had been no sale or disposition of the timber. The facts of the case did not come within the criteria under s 74(2)(b). The compensation payment filled the "hole" in the taxpayers' profits caused by the Government decision to stop the logging and exporting of native timber. The Authority confirmed the Commissioner's view that the adjustment assistance payments received by the partnership from the Ministry of Forestry constituted assessable income under the business income and royalty provisions, but not the s CB 24 equivalent as argued. See *Case* S104 (1996) 17 NZTC 7,662. See also *Case* T47 (1998) 18 NZTC 8,319.

¶28-020 Forestry right defined

The Forestry Rights Registration Act 1983 defines a "forestry right" as a right granted in accordance with that Act. Briefly, an owner or lessee of land can create a forestry right by creating, granting or reserving the right to establish, maintain and harvest or to maintain and harvest a crop of trees on the land. The forestry right may also grant or reserve rights of access and rights of construction and use of tracks, culverts, bridges, buildings and other works and facilities if those rights are ancillary to and necessary for the purposes of the rights created. In addition, the forestry rights may provide for charges, payments, royalties or division of the crop or the proceeds of the crop. Although a forestry right falls short of a right of exclusive possession, it can be registered against the title to the land pursuant to the Land Transfer Act 1952. Where a registered right contains a covenant, this becomes binding upon the successors in title, unless the parties agree otherwise.

Persons can grant rights to themselves. See ¶28-013 and s 2A(3) of the Forestry Rights Registration Act.

¶28-021 Treaty of Waitangi claim settlements: rights to take timber [IT07 ss CW 1B, DP 9B, DP 11]

Exempt income arises when a forestry right is extinguished and re-granted in whole or in part solely for the purpose of facilitating a Treaty of Waitangi claim settlement process.

The new rights are treated as having been acquired for a cost equal to the expenditure incurred in relation to the old right. This will apply only to the extent that the expenditure relates to the land covered by the new right and to the extent that it has not been deducted previously.

When a person is entitled to the exempt income treatment, detailed above, the deemed cost of the new right does not give rise to a deduction under the cost of timber rules in s DP 11.

¶28-022 GST on sale of forestry rights [GST s 20(3)]

The Commissioner issued a binding public ruling, BR Pub 07/01, on the subject of when the recipient of a forestry right will be able to claim a secondhand goods GST input tax credit. Essentially, the ruling confirms that the grant of a forestry right is a supply of secondhand goods if at least one prior owner has exercised his or her right of removing trees from the land. The original grant of a forestry right cannot be a supply of secondhand goods.

The ruling applies for an indefinite period from 1 October 2006.

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