Inland Revenue
Te Tari Taake

POLICY AND STRATEGY

Tax policy report: COVID-19 Response (Taxation and other Regulatory Urgent Measures) Bill: Final design approval

Date:	24 April 2020	**Priority:**	High
Security level:	In Confidence	**Report number:**	IR2020/222

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to the recommendations in this report	28 April 2020
Minister of Revenue	**Agree** to the recommendations in this report **Refer** a copy of this report to relevant Ministers.	28 April 2020

Contact for telephone discussion (if required)

Name	Position	Telephone
s9(2)(a)	Principal Policy Advisor	s9(2)(a)
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24 April 2020

Minister of Finance
Minister of Revenue

COVID-19 Response (Taxation and other Regulatory Urgent Measures) Bill: Final design approval

1. This report seeks your approval to the final design of legislative measures aimed at assisting the Government's response to the impacts of COVID-19. These include measures aimed at providing economic relief and measures to address regulatory compliance issues. These measures will be included in an omnibus bill to be introduced by the Minister of Revenue on 29 April 2020, subject to Cabinet approval.

2. The draft Bill and accompanying disclosure statement are attached to this report. These documents are complete but subject to minor technical and editorial changes.

3. The Bill contains the proposals listed below.

Items in the Bill

Tax and social policy items

4. The following items have received Cabinet approval *(CAB-20-MIN-0165 refers)* for inclusion in the Bill:

   4.1 temporary loss carry-back regime; and

   4.2 increased administrative flexibility for Inland Revenue.

5. On 16 April 2020 the group of Ministers with Power to Act on COVID-19 matters *(CAB-20-MIN-0130 refers)* approved a proposal on the tax and social policy treatment of pension and benefit equivalent payments for inclusion in a bill.[1]

Other regulatory items

6. The Cabinet Business Committee (CBC) has given authority to responsible Ministers to defer commencement dates of new regulatory requirements where appropriate in response to COVID-19 (*CBC-20-Min-0038*). Under this delegation:

   6.1 the Minister of Agriculture has agreed to defer the commencement date of new animal surgical procedures regime introduced in the Animal Welfare Amendment (No 2) Act 2015; and

   6.2 the Minister of Commerce and Consumer Affairs has agreed to defer the commencement dates for broad system changes in the Credits Contracts Legislation Amendment Act 2019.

7. The CBC has also given authority to responsible Ministers to approve exemptions from statutory requirements, subject to certain criteria being met. The Minister of Finance and the Minister for State-Owned Enterprises agreed that proposals to amend the statutory timeframes for planning documents in those statutes could be included in the Bill.

[1] Paper titled *Implementing the Agreed Approach to Paying Benefits and Pensions to Those Stranded Overseas.*

8. On 16 April 2020 the group of Ministers with Power to Act on COVID-19 matters (CAB-20-MIN-0130 refers) agreed to bring forward the commencement dates of certain protections relating to high-cost consumer credit contracts in the Credit Contracts Legislation Amendment Act 2019.[2]

9. These items are covered in further detail in the attached Bill summary.

Tax policy items and final recommendations

Temporary loss carry-back regime

10. Cabinet has agreed to a temporary loss carry-back regime. This will have the effect of allowing businesses that anticipate being in loss in either the 2019-20 or 2020-21 tax year to carry some or all of that loss to the preceding year where profits were earned. Cabinet delegated authority to the Minister of Finance and Minister of Revenue to make decisions on the final design of the policy *(CAB-20-MIN-0165 refers)*.

11. Officials have carried out targeted consultation on the design of the temporary loss carry-back scheme (representatives from CAANZ, Corporate Taxpayer Group, Deloitte, KPMG, PwC, EY, Russell McVeagh). Stakeholders are generally very supportive of the measure, however, on design there are some issues we were unable to resolve. Some of these will be revisited as part of the longer-term project on the permanent loss carry-back regime.

12. The key design issues arising from these discussions and our recommended responses are set out below.

Two-year carryback

13. Some stakeholders raised the concern that large losses arising in the 2020-21 year would only be able to be offset against profit from the 2019-20 year which may also be significantly impacted by COVID-19. If there is not sufficient income in the profit year the taxpayer will be constrained in how much of a refund it is able to get. Stakeholders want to be able to claim the loss over the two years prior to the loss year (i.e., allowing the 2020-21 loss to be carried back to the 2018-19 and 2019-20 years).

14. Making this change would significantly increase the fiscal cost as well as administrative and compliance costs due to the additional number of returns that would need to be reopened if this was permitted. We do not recommend addressing this issue.

Use-of-money interest

15. Stakeholders considered that use-of-money interest (UOMI) should apply only from the date of the carry-back refund. However, Inland Revenue system constraints prevent any changes being made to the existing UOMI rules within such a short timeframe.

16. Some stakeholders thought that the Commissioner should be able to use the new discretionary powers to remit UOMI where interest arises as a result of COVID-19. Applying UOMI to underpayments of tax resulting from a loss carry-back refund is an important integrity measure to ensure inappropriate refunds are not claimed. We do not recommend any remittance powers be available in this situation.

[2] Paper titled: *COVID-19 Omnibus Bill 2020: Commerce and Consumer Affairs Portfolio.*

Shareholder salaries

17. Some small-medium companies will not benefit from the regime because the distribution of profits as shareholder salaries has resulted in zero income to claim a loss carry-back refund against. We have discussed this with the Minister of Revenue and provided briefings on the issue (BN2020/26 and BN2020/213 refer). We recognise this as an issue, but only a company with a loss in the 2019-20 tax year which it wishes to carry back to the 2018-19 tax year will be impacted. For losses in 2020-21, taxpayers will be able to manage their situation so that they will have capacity to benefit from a loss carry-back.

18. Resolving the issue would result in increased compliance and administrative costs which outweigh any benefit. Therefore, we do not recommend any change be made.

Imputation credit limitation

19. Loss carry-back refunds, like other tax refunds, are limited to a company's available imputation credit account (ICA) balance. This means that if a company has distributed all of its profits by paying imputed dividends, it will have no ability to use a loss carry-back until it has a new tax obligation.

20. Some stakeholders questioned whether the ICA balance limitation is required at all. We consider it to be an important safeguard to ensure that a company cannot get a refund of tax after it has transferred the credit for the tax payment to its shareholders. For this reason, this requirement should not be removed.

Shareholder continuity

21. Stakeholders considered the requirement to maintain 49% shareholder continuity was unnecessary and will impact access to the scheme for businesses seeking to raise capital in 2020 and 2021.

22. We do not recommend removing the continuity requirement. It is an important integrity measure that ensures tax refunds are not received by a company whose shareholders did not bear the burden of the tax when it was paid. However, consistent with the loss carry-forward rules, the part-year continuity test should apply to ensure that where there is a breach of continuity part way through a loss year the company can still carry back the amount of the loss arising up until the point of the breach. Part-year rules should also be applied to the continuity and commonality of ownership requirements that enable a loss company to carry back and use a loss against the profits of other entities in the same group. This should address some of the concerns raised.

Additional integrity measures

23. We recommend that a specific anti-avoidance rule be included directed at preventing arrangements entered into by taxpayers to defeat the intended purpose of the carry-back rules.

24. We are also concerned that companies in a group might carry a loss back in order to claim a refund of group income (66% commonality of ownership required), rather than first offsetting income of other wholly-owned companies in the year the loss arose. This ability to pick and choose how to use the loss could result in inappropriate outcomes. We recommend, as an integrity measure, requiring a loss company to maximise the use of its loss to offset income of wholly-owned companies in its group in the current year before its loss can be carried back and used against income of the company's group in the prior year.

Application of refunds to existing tax debt

25. We provided a briefing to the Minister of Revenue on 17 April 2020 (BN2020/213 refers) explaining that, unless switched off, the Inland Revenue system would apply any loss carry-back refund to existing tax debts before paying the balance in cash to a taxpayer. Consistent with subsequent discussion with the Minister of Revenue on this issue we recommend the Bill include a provision which will switch this off for the purposes of carry-back refunds.

Increased administrative flexibility for Inland Revenue

26. Cabinet agreed to an amendment to the Tax Administration Act 1994 to provide flexibility to Inland Revenue to modify timeframes or procedural requirements for taxpayers who are impact by COVID-19. This would provide the Commissioner of Inland Revenue with discretion to temporarily vary dates and timeframes and modify procedural requirements that are specified under the Revenue Acts, or provisions of the Unclaimed Money Act 1971. This would also allow for more flexibility when a time period is specified in a provision, for such time-related requirements to be modified where COVID-19 impacts or measures make the current requirement impracticable for certain taxpayers.

27. The proposed discretion will be time-limited in application starting from 17 March 2020. The initial recommendation was that this should be limited for an 18-month period from this date. Following feedback from consultation, officials recommend that this period end on 30 September 2021, so this would limit the application for approximately 18.5 months. This change will allow the Commissioner to potentially modify dates or requirements to align with any 30 September returns as appropriate. This period can be extended by the making of an Order in Council, allowing assessment of whether on-going effects from COVID-19 warrant keeping this discretion for a longer timeframe, once this information is available.

Tax treatment of pension and benefit equivalent payments

28. On 17 April 2020, the Minister for Social Development made a Ministerial welfare programme in relation to beneficiaries and superannuitants stranded overseas as a result of COVID-19 ("New Zealanders Stranded Overseas" or "NZSOS" programme). The NZSOS programme allows MSD to make payments to individuals who cannot otherwise receive their standard payment because they are stranded overseas as a consequence of COVID-19. Payments under the NZSOS programme began on 20 April 2020.

29. The Bill proposes that amendments be made to ensure that where NZSOS payments are paid in lieu of a main benefit, New Zealand superannuation, and veteran's pension, they are taxable and subject to PAYE. Other payments made under the Social Security Act 2018, which are normally exempt from tax, will remain exempt from tax when paid as an NZSOS payment. Other minor amendments are proposed to ensure that eligibility for working for families tax credits, and student loan and child support obligations are not impacted when an individual receives an NZSOS payment rather than their normal payment.

30. At its meeting of 16 April 2020, The COVID-19 Ministerial Group gave authority to the Minister of Revenue to resolve minor and technical details to the pension and benefit equivalent payments proposal.[3]

31. The Minister of Revenue has agreed that when a person receives an NZSOS payment and they are the receiving carer for child support, the usual Crown entitlement rules will apply, and further, that recipients of NZSOS payments

[3] Paper titled *Implementing the Agreed Approach to Paying Benefits and Pensions to Those Stranded Overseas.*

equivalent to a Supported Living Payment (SLP) will be eligible for the higher rate of living allowance available to SLP recipients (IR2020/214 refers).

New Zealand Bill of Rights Act 1990

32. The Bill has been reviewed by the Ministry of Justice to check it is consistent with the rights and freedoms affirmed by the New Zealand Bill of Rights Act 1990 (BORA). They will be advising the Attorney-General on BORA implications and recommending that this advice be referred to the Minister of Revenue.

Treasury consultation

33. Treasury have been consulted in the preparation of this report.

Next steps

34. A paper seeking agreement to delegate authority to the Minister of Revenue to introduce the attached Bill, in consultation with the Minister of Finance and the Leader of the House, will be considered by Cabinet at its meeting of Tuesday 28 April 2020.

35. Subject to approval by Cabinet, the Bill is scheduled to be introduced by the Minister of Revenue on Wednesday 29 April 2020 and will go through all stages under urgency.

Recommended action

We recommend that you:

36. **Agree** to apply the part-year ownership continuity rules and part-year commonality rules to the tax loss carry-back provisions.

Agreed/Not agreed Agreed/Not agreed

37. **Agree** to include a specific anti-avoidance measure to prevent arrangements being entered into by taxpayers in order to defeat the intended purpose of the carry-back rules.

Agreed/Not agreed Agreed/Not agreed

38. **Agree** to require a loss company to maximise the use of its loss to offset current year income of wholly-owned companies in its group before the loss can be used against income of the group in the prior year.

Agree/Not agreed Agreed/Not agreed

39. **Agree** to an amendment to switch-off the ability for Inland Revenue to apply loss carry-back refunds claimed as part of the temporary scheme to existing tax debts.

Agreed/Not agreed Agreed/Not agreed

40. **Agree** that the time period for increased administrative flexibility for Inland Revenue will end on 30 September 2021 unless extended by Order in Council.

Agreed/Not agreed Agreed/Not agreed

41. **Note** approval for the Minister of Revenue to introduce the attached Bill is being sought from Cabinet at its meeting of 28 April 2020.

    Noted | Noted

42. **Refer** a copy of this report to the Minister of Agriculture, Minister of State-Owned Enterprises, and the Minister of Commerce and Consumer Affairs for their information.

    Referred/Not referred

s9(2)(a)

[redacted]

Policy Lead
Policy and Strategy

Hon Grant Robertson
Minister of Finance
/ /2020

Hon Stuart Nash
Minister of Revenue
/ /2020