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PUB00261: Interpretation Statement: IS XX/XX Taxation of Trusts – Income Tax

Introduction

1. The New Zealand Law Society (Law Society) welcomes the opportunity to comment on *PUB00261: Interpretation Statement: IS XX/XX Taxation of Trusts – Income Tax* (Interpretation Statement) and thanks Inland Revenue for the extension of time allowed to make this submission.
2. The Interpretation Statement notes at its outset that there are a number of areas it does not cover. Despite that, the Law Society submits that there are some key omissions from the content of the Interpretation Statement, aside from those mentioned in further detail below, which should be included or addressed in a separate item:
 - a. The application of double tax agreements to trusts
 - b. Whether beneficiaries become settlors of a trust by having a credit current account balance
3. Overall, the Law Society's view is that, while we understand that this is an Interpretation Statement of the current law as Inland Revenue sees it, it would be beneficial to consider placing the widely acknowledged problems with the current legislation on the work programme to be reviewed and where required, amended.
4. In the meantime, the Law Society submits that a purposive interpretation of the current law is required, to ensure that the law does not overreach what Parliament has intended under the current provisions.

5. The comments below outline a number of areas where Inland Revenue has, in the Law Society's opinion, incorrectly interpreted the law; where the Interpretation Statement is unclear; or where the Law Society suggests that the wording of the legislation be referred for review. The references in the main headings below correspond to those in the Interpretation Statement.

Part 1: Introduction

Taxable distributions from non-complying trusts to non-resident beneficiaries

6. The Interpretation Statement at paragraph [1.18] reads "Foreign-sourced amounts distributed to non-resident beneficiaries are also not subject to tax in New Zealand **unless they are included in a taxable distribution made by a non-complying trust**". This is incorrect. The Interpretation Statement later refers to this at paragraphs [10.34] and [10.35], as well as at paragraph [11.11], with reference to relevant sections of the Income Tax Act 2007 as well as *Case Y25 (2008) 25 NZTC 23,070*.
7. Section BD 1(1) provides that "An amount is income of a person if it is their income under a provision in Part C (Income)". Subpart CX defines excluded income and includes a taxable distribution from a non-complying trust. This is a provision in Part C, and therefore is included as income of a person under section BD 1(1).
8. Further, sections BD 1(2) and BD 1(3) provide that exempt income and excluded income is a subset of the income referred to in section BD 1(1). For example, section BD 1(3) states "an amount **of income of a person** is excluded income if..." This means that it has to be "income of a person", which is the defined term in section BD 1(1), before it can be excluded income.
9. It follows then that such a taxable distribution can be a foreign-sourced amount and will not be taxable under section BF 1(b) where the beneficiary is a non-resident or a transitional resident.
10. Its status as excluded income under sections HC 19(1) and CX 59 is only so that they can be subjected to income tax at the 45% rate rather than at the beneficiary's marginal tax rate.
11. In *Case Y25* Judge Barber did not implicitly confirm that source is irrelevant to the tax treatment of taxable distributions from a non-complying trust with a non-resident trustee. *Case Y25* involved two proceedings which were heard together. The non-resident beneficiary was only a party to the original proceeding which involved whether the relevant trust was a qualifying trust. The second proceeding relating to the corpus of the trust was brought by the three resident beneficiaries and it was only these three beneficiaries who were issued assessments on 22 May 2006.

12. The confusion arises because Judge Barber did not define who “the disputants” were at each stage of his judgment. Because the non-resident beneficiary was not a disputant to the second proceeding, the references at paragraphs [15], [16] and [18] of the judgment are to the resident beneficiaries.
13. This means that an error has been made by Judge Barber in paragraph [1] where he refers to the 45% income tax that the four beneficiaries must pay. The non-resident beneficiary was never assessed by IRD. The Law Society recommends that Inland Revenue check its records on this case to confirm the above position and amend the Interpretation Statement to take it into account.
14. The Interpretation Statement contains a number of paragraphs that are consistent with the above interpretation and contrary to the position taken at paragraphs [1.18], [10.34], [10.35] and [11.11]. For example, see paragraphs [8.68], [11.4], [11.6], [13.64] and example 26 at [8.103].

Part 2: Settlers

Providing financial assistance to a trust

15. Paragraph [2.41] provides that where a person acts as a guarantor for an amount borrowed by a trust, or provides a trust with security for the purpose of borrowing, that person is treated as a settlor. In many cases, it will be the trustees themselves who will provide a guarantee or security for the borrowings of the trust, without consideration for doing so. In these circumstances, it is not the trust who borrows (as it is not a legal entity) but the trustees who are the borrowers.
16. While paragraph [2.45] states that generally services provided to a trust in the trustee’s capacity as trustee will not result in a transfer of value, the Law Society submits that this should be made clearer in situations involving the provision of financial assistance to a trust.
17. In addition, paragraph [2.45] does not give sufficient comfort that where a company is a trustee, the company would not be considered to be providing a transfer of value where the trustee is not paid for its services. It also does not cover other situations where a company may provide services to a trust for no consideration, for example where the trustee holds the power to appoint and remove trustees, and receives no consideration for the performance of that service.
18. Paragraphs [2.47] to [2.49] discuss a situation where the right to demand interest, as opposed to the right to demand payment of the debt, is not made. Section HC 27(2)(b) does not make a reference to interest, but rather to the situation where one party provides financial assistance to the other, and that party does not exercise, or defers the exercise, of their right to demand

repayment. The definition of financial assistance also includes a situation where financial assistance is made and the right to demand repayment is either not made or is deferred.

19. While it is clear that the provision of financial assistance would result in the person providing the financial assistance being treated as a settlor, it is not clear whether any interest which would have been demanded, but is not, is a settlement on the trust.
20. The Law Society submits that the commentary in the Interpretation Statement regarding financial assistance provided to a trust should be clarified.

Indirect transfers of value

21. The definition of settlor includes situations where a person makes a transfer of value to an entity owned by a trust. Paragraphs [2.53] and [2.54] suggest that a degree of intention is required for a transfer of value made through a series of transactions to result in a person being treated as a settlor. This is not evident from a reading of the wording of section HC 27(4).
22. The Law Society submits that whether or not intention is required should be clarified in the interpretation statement and, if it is required, section HC 27(4) should also be amended.

Control over a trustee or settlor

23. Paragraphs [2.82] to [2.88] address situations where a person is treated as a settlor of a trust if they acquire rights or powers in relation to a trustee or settlor of the trust which has the purpose or effect of enabling them to require the trustee to treat them as a beneficiary of the trust.
24. Often, trustees will have the power to appoint and remove beneficiaries, which may include themselves. It means that a person who holds the power to appoint and remove trustees is able to appoint a person as a trustee and then they can appoint themselves as a beneficiary.
25. The power to appoint and remove trustees may be vested in the trustees under the trust deed or transferred to them by the person who holds that power under the trust deed, either during that person's life or on their death. In some cases, the power to appoint and remove trustees will pass to the trustees by default. In both of these cases, when the power is transferred to the trustee, it has also been acquired by the trustee.
26. The Interpretation Statement's discussion of section HC 28(6) seems to imply therefore that where a person acquires a power to appoint and remove trustees and consequently also acquires (in their capacity as trustee) the power to appoint and remove beneficiaries, they will

be treated as a settlor. According to paragraph [2.85], it does not matter if they do not exercise the power, as they will still be considered to be a settlor.

27. The Law Society submits that a purposive interpretation of section HC 28(6) should be taken, such that a person will not be considered a settlor where that person is unrelated to the original settlor. If that is not Inland Revenue's view of the interpretation of the section, then the section should be amended to make this clear. It is not explicitly clear from the wording of the section whether an independent person, such as a solicitor, who is transferred the power to appoint and remove trustees by the original appointor, would be considered to be a settlor, if by virtue of holding the power to appoint and remove trustees, they could appoint themselves as a trustee, which could, in turn, also result in that person, in their capacity as trustee, appointing him or herself as a beneficiary. However that would be inconsistent with what the section is trying to achieve.
28. Generally, the decision to appoint a person as a beneficiary would have to be made by all trustees. The Law Society submits that the Interpretation Statement should be amended to make clear what the word "require" means. As an example, it could be limited to a situation where the person holds the sole power to exercise a particular power under the trust deed or terms of the trust to appoint the person as a beneficiary.
29. The Law Society also submits that "purpose or effect" in section HC 28(6) should be qualified so that it requires some form of positive act or intention to acquire the rights of a trustee which will result in that person being able to require the trustee to appoint that person or a nominee as a beneficiary.
30. The Law Society further submits that the concepts and meaning of "acquire", "acquisition", "require" and "purpose and effect" should be expanded so that it is clear in situations where a person acquires the right to appoint and remove beneficiaries, but has no relationship with the settlor or beneficiaries of the trust (for example, they are a professional trustee or a trustee company), that person is not inadvertently considered to be a settlor.
31. Finally, the Law Society submits that example 8 at paragraph [2.88] is hard to understand and should be amended or clarified to show why Steve may be considered a settlor. It is difficult to understand why Steve would pay \$1 million for the shares in Dragon Co, when Dragon Co in essence has no value, given it has no beneficial interest in the assets of the trust of which it is a trustee. For section HC 28(6) to apply, Dragon Co would have to hold the power to appoint Steve as a beneficiary – this is not clear from the example.

Anti-avoidance provision

32. Example 9 at paragraph [2.95] appears to indicate that a shareholder who votes, or refrains from voting, for shares in the company to be issued to a trust will be treated as a settlor of that trust irrespective of whether or not that person receives a benefit from the trust which has been issued the shares.
33. Paragraph [2.93] states that intention is not relevant, which means that by a consequence of action or inaction, without any proper comprehension of the outcome, a person can be treated as a settlor. The problem with the section and the examples given is that a person could be considered to be a settlor of a trust they have no relationship with simply due to the fact they voted or did not vote in a particular way. Again this would appear to be beyond the purpose of the section.
34. The Law Society submits that example 9 should be amended to reflect that the scenario given would not result in a shareholder, who has no relationship or interest in the trust in which shares in the company are being issued, being considered to be a settlor of that trust. Similarly, in example 10, if the shareholder was unrelated to the trust and failed to vote on the provision of income to that trust, the example should be amended to state that the unrelated shareholder would not be considered to be a settlor of the recipient trust.

Miscellaneous amendment

35. The example at paragraph [2.101] should be amended by removing the words “set up a trust on their behalf” and replacing them with “make a settlement on a trust on their behalf”.

Part 3: Trustees and beneficiaries

Miscellaneous amendments or comments

36. The Law Society submits that paragraphs (a) and (b) of paragraph [3.8] should be deleted and instead the Interpretation Statement should refer to Part 7. This paragraph may be misleading otherwise, as there are situations where foreign-sourced amounts derived by a trustee (whether resident or foreign) will not be taxed even where a settlor is resident (and is not a transitional resident).
37. Paragraph [3.10] states that “Where one of the trustees is resident, then all of the co-trustees as the notional single person under section HC 2 are resident in that capacity.” The Law Society submits that it should be explained why the notional single person is treated as resident in this situation.

Part 4: Income derived by trustees

Miscellaneous comment

38. Paragraph [4.4] notes that “income derived by a trustee” is not the same as the concept of “trustee income” in the trust rules. The Law Society, however, notes that the Income Tax Act 2007 is not consistent on this point, which should be referred to Inland Revenue’s Policy team for review. As an example, sections CW 54 and HC 26 treat as exempt income, a foreign-sourced amount that “a New Zealand resident trustee derives”, without using the concept of “trustee income”.

Part 5: Beneficiary income

Trustee resolution and beneficiary income

39. The wording of paragraphs [5.33] to [5.39] appear to suggest that the passing of the resolution in *CIR v Ward* [1970] NZLR 1 means that the income has been applied in a particular way, even though it is in contravention of the trust deed. For a resolution to be considered to be an effective application of income, the resolution must be made in accordance with the terms of the trust deed. The trust deed in *CIR v Ward* specifically allowed for income to be distributed in this way.
40. The Law Society therefore submits that the wording of paragraphs [5.33] to [5.39] should be amended so it is clear that any resolution to allocate income to a beneficiary can only be effective if it is made in accordance with the terms of the trust deed.

Miscellaneous amendments and comments

41. The Law Society submits that examples 12 and 13 at paragraph [5.21] should be amended so that they are both referring to distributions of income. Currently, example 12 refers to an allocation of income, while example 13 refers only to trust property. If Inland Revenue was referring to a distribution of income in example 13, the distribution could not be beneficiary income because the beneficiary was not entitled to it until they reached 18 years of age. Therefore it would have to be treated as trustee income and accumulated for the beneficiary until they turned 18.
42. The Law Society submits that paragraphs [5.30] to [5.32] need to make clear that if a payment was made to a parent or guardian on behalf of a beneficiary, the payment is made for the benefit of that beneficiary, and not the parent or guardian. This is particularly relevant where the parent or guardian is also a beneficiary.

Part 7: Trustee income

Miscellaneous amendments and comments

43. Paragraph [7.6] purports to state unequivocally that foreign-sourced amounts derived by a non-resident trustee are assessable as trustee income. This is misleading however, as exceptions are noted at paragraph [7.9]. The Law Society submits that paragraph [7.6] should make reference to the exceptions at paragraph [7.9], and paragraph [7.9] should begin “Even if a settlor of a trust is a New Zealand resident who is not a transitional resident...”
44. Paragraph [7.8] discusses section HC 25(2)(c). Since section HC 25 applies to non-resident trustees, it follows that the section has no application if the trustee is resident in New Zealand for all of the income year. It also follows that section HC 26 only applies if the trustee is resident in New Zealand for all of the income year in which a foreign-sourced amount is derived. The Law Society submits that the Interpretation Statement should include confirmation of this.
45. The Law Society submits that the exceptions at paragraph [7.9] should note that they apply even where a settlor is resident in the income year of derivation. The Law Society further submits that the statement at paragraph [7.10] that “a New Zealand resident settlor will still be liable as agent of the [non-resident] trustee for income tax payable by the trustee” is unequivocal and should include reference to the exceptions, and also that it is limited to New Zealand income tax payable on New Zealand sourced income.
46. The Law Society submits that paragraph [7.14a] is incorrect and should instead read “at all times in the income year no settlor of the trust is a New Zealand resident who is not a transitional resident.”
47. Paragraph [7.14] assumes that section HC 26 only applies to foreign trusts. This is incorrect however, as the requirements in paragraph 7.14(c), (d) and (e) only apply to foreign trusts. The Law Society submits that paragraph [7.14] should be redrafted to set out the requirements for foreign-sourced amounts derived by New Zealand resident trustees to be exempt income where (i) the trust is a foreign trust, and (ii) where the trust is not a foreign trust.

Part 8: Distributions from complying, foreign and non-complying trusts

Transactions that are not genuine and other ordering adjustments

48. Section HC 16(5) is described as acting as a type of anti-avoidance provision in paragraph [8.93]. The section is drafted so widely however that it also applies to transactions which are genuine and are not intended to avoid tax. It is not sufficient that the distribution “is a genuine

transaction entered into and carried out in good faith”, it also has to meet the other requirements in that section.

49. An example is where a trustee of a foreign trust without any knowledge of New Zealand tax law can make a genuine, good faith distribution such as one or more equal settlements on sub-trusts, so that each member of a family may have a sub-trust established for the benefit of themselves and their family. As sections HC 16(5) and HC 16(2) are drafted, if one of the sub-trusts is established for a person who is or becomes a New Zealand resident beneficiary, any income settlement on one of the other sub-trusts is disregarded and that income is treated as being settled on the New Zealand sub-trust.
50. Additionally, paragraph [8.100] is unclear in that the phrase “This requirement would be satisfied...” does not refer to which requirement and whether the example distribution would fall foul of section HC 16(5)(b) or not. If the test in section HC 16(5)(b) is met then the amount of the distribution is beyond the possession and control of the trustee, which would be to satisfy the requirement. However, if the distribution is credited to the beneficiary's current account with the trust, the amount is within the possession of the trustee (see paragraph [5.20]). Further, if the trustee can use the distribution retained as working capital, it is within the trustee's control (again, see paragraph [5.20]). Accordingly, it is considered that section HC 15(b) is not satisfied if a distribution is credited to a beneficiary's current account.
51. Finally, the test in section HC 15(b) is inconsistent with the concept of beneficiary income. As noted at paragraph [5.20], an amount does not need to be placed beyond the possession and control of the trustee before an amount of income derived by a trustee in an income year “vests absolutely in interest” in a beneficiary as beneficiary income. Accordingly, where there is a genuine transaction entered into and carried out in good faith, involving an income distribution where the amount is credited to a beneficiary's current account with a trust, it is unmerited to treat such a distribution as not genuine. *CIR v Ward* is clear authority that vesting of income is not affected by the income distributed remaining under the control of the distributing trustees. Therefore, there is no reason for section HC 16(5) to include the amount of that distribution as undistributed income in applying the ordering rules in section HC 16(2).
52. The Law Society submits that the section should be referred to Inland Revenue's Policy team for review, and recommends it is narrowed so that it does not apply to genuine transactions which are not designed to manipulate distributions for New Zealand tax purposes.

Miscellaneous amendments and comments

53. Paragraph [8.13b] provides that in order for a trust to be treated as a complying trust, “the **income tax obligations** of the trustees have been satisfied for every tax year”. The Law Society submits that this overstates the requirement in section HC 10(1)(a)(ii) which only requires that

“the tax obligations relating to the trustee’s **income tax liability** have been satisfied for every tax year”. The income tax obligations of trustees may extend beyond satisfying the trustee’s income tax liability. This misstatement also arises in paragraphs [8.22] and [8.35b].

54. Paragraph [8.19] should be amended to also state that a trustee of a complying trust that derives non-resident passive income can retain complying trust status where an election is made to pay New Zealand income tax on that income.
55. The Law Society submits that paragraph [8.32] is incorrect insofar that the type of trust mentioned in that paragraph could also technically be a foreign trust. This was confirmed in paragraph [4.64] of the 1989 *Explanation of Taxation of Trusts*. Inland Revenue should explain why its stance on this has changed or amend the Interpretation Statement to the previous position.
56. Paragraph [8.84] provides that after being made up of income derived by the trustees in the current year, a distribution is made up of income, **other than beneficiary income**, derived by the trustees in an earlier income year. Beneficiary income does not necessarily have to be distributed in the year that it is derived by the trustees however, as section HC 6(1B) permits a longer period of time. Such income would therefore not fall within section HC 16(2)(a) or section HC 16(2)(b). The Law Society submits that this inconsistency should be addressed by the Interpretation Statement.

Part 10: Entry to the trust regime

Whether a foreign trust can be a complying trust without making an election

57. Paragraph [10.13] states that a foreign trust that does not make an election under section HC 33 to become a complying trust will not be a complying trust as it would not have met the requirements set out in section HC 10 since inception. This is not necessarily the case; for example, a foreign trust that derives only New Zealand-sourced income and has not derived any non-resident withholding income will meet the requirements set out in section HC 10 to be a complying trust, provided the trustees have satisfied their tax obligations in respect of the trustees’ income tax liability in each income year. The Law Society submits that the Interpretation Statement should be amended to reflect this.
58. On a related point, the Interpretation Statement does not address whether a trust can be both a foreign trust and a complying trust on the basis that it meets the requirements of both sections HC 10 and HC 11. The Law Society considers that, based on the natural meaning of the wording of sections HC 10 and HC 11, there is nothing preventing a trust from being both a complying trust and a foreign trust. Further, the Law Society is not aware of any sound policy reason why distributions (other than distributions of beneficiary income) made by a complying trust that

also happens to be a foreign trust should be liable to New Zealand income tax. Given that trustee income of such a trust would have already been subjected to New Zealand income tax, taxing that income again on distribution would amount to economic double taxation.

59. The Law Society acknowledges that the application of subpart HC to trusts that are both complying trusts and foreign trusts raises a number of issues, such as whether the rules relating to distributions from complying trusts apply to such trusts (the Law Society considers they do) and whether the recently-enacted foreign trust disclosure rules in section 59B of the Tax Administration Act 1994 apply to such trusts (Law Society members have different views on this issue, although the prevalent view is that the foreign trust disclosure rules tax do apply in this instance). The Law Society submits that the Interpretation Statement needs to address these issues.

The application of the ordering rules to bifurcated trusts

60. Paragraph [10.16] includes three worked examples on the application of the ordering rules to bifurcated trusts (i.e. foreign trusts where a settlor becomes New Zealand tax resident, and either an election is made (in which case the trust becomes a foreign / complying trust) or no election is made (in which case the trust becomes a foreign / non-complying trust). Examples 28, 29 and 30 appear to treat such a trust as a single trust for the purpose of the ordering rules. This means that, in the case of a foreign / non-complying trust, distributions will generally be treated as having been made from amounts derived while the trust was a non-complying trust in preference to amounts derived while the trust was a foreign trust.
61. The Law Society does not agree with Inland Revenue's view of how the ordering rules apply to a bifurcated trust. Rather, the Law Society considers that the ordering rules should apply to each fund separately (consistent with the natural wording of the ordering rules), and that it will be a question of fact whether an amount has been distributed from amounts derived before or after the election (in the case of a foreign / complying trust) or the election expiry date (in the case of a foreign / non-complying trust).

Miscellaneous amendments and comments

62. Paragraph [10.5] states that the period of "transitional resident" extends "... for a period of 48 months (plus the days remaining in the month) **after becoming resident.**" The words "after becoming resident" are misleading, as the period of transitional residence extends from the time that the person is deemed to be New Zealand tax resident to 48 months after the end of the month in which the person is able to determine that they have become New Zealand tax resident. This is the latter of when the person obtains a permanent place of abode in New Zealand and the person's 184th day of presence within a 365 day period. The period of

“transitional residence” can therefore extend to just under 5 years in certain circumstances. The Law Society submits that paragraph [10.5] should be amended to address this.

63. The last two paragraphs of example 27 at paragraph [10.16] are incorrect. The tax treatment of distributions made by a trust that has made an election is determined by whether the amount distributed was sourced from amounts derived before or after the election date, not whether the distribution was made after the election date. In a similar vein, if no election has been made, then the tax treatment of distributions turns on whether distributions were made from amounts sourced before or after the election expiry date, not whether the distribution was made after the election expiry date. The Law Society submits that the example should be corrected.
64. Paragraph [10.37] states that the source rules in sections YD 4(13) and YD 4(18) apply to determine the source of a taxable distribution from a foreign trust that comprises income or capital gains. Section YD 4(13) provides that income derived by a beneficiary from a trust has a source in New Zealand to the extent to which the income of the trust fund has a source in New Zealand. As such, the source of a taxable distribution made by a foreign trust will turn on the source of the income of the trust, whether or not that taxable distribution comprises capital gains. The Law Society submits that the application of the source rules to trust distributions should be referred to Inland Revenue’s Policy team.
65. Paragraph [10.41] provides that one of the section HC 29(5) prerequisites for a natural person settlor to avoid liability as agent of the trustee is for the settlor to make no settlements on a foreign trust after they become resident. This is incorrect, as the prerequisite is instead that the natural person settlor is not resident in New Zealand at the time of **any** settlement on the trust. The Law Society submits that paragraph [10.41] should be amended to reflect this.

Part 11: Exit from the trust regime

Departing settlors of a complying trust

66. The first sentence of paragraph [11.3] implies that if all settlors of a complying trust leave NZ, the trust becomes a foreign trust. This implication is incorrect, since a trust cannot be a foreign trust if a settlor of the trust is resident in New Zealand at any time. Nevertheless, section HC 26 will result in the foreign-sourced amounts of a resident trustee being exempt income in the income year following the departure of the last of the settlors, as the exemption in section HC 26 is not limited to foreign trusts. In that case, the trust will become a non-complying trust, unless either an election is made under section HC 33 or the trustee distributes the foreign-sourced amount as beneficiary income.

67. If the trustee is non-resident and no settlor is resident in New Zealand at any time in an income year, section HC 25 will not apply and the trustee will derive an amount of non-residents' foreign-sourced income. The trust will become a non-complying trust, unless either an election is made under section HC 33 or the trustee distributes the foreign-sourced amount as beneficiary income.
68. The Law Society submits that paragraph [11.3] should be amended to address the above.

Miscellaneous amendments and comments

69. The last sentence of paragraph [11.2] states that the tax rate for New Zealand-sourced income derived by a trustee of a foreign or non-complying trust turns on the type of income and the application of any applicable double tax agreement. The tax rate applicable to New Zealand-sourced interest, dividends and royalties turns on the residence of the trustees and whether an election has been made, not whether the trust is a foreign or non-complying trust. That is, if none of the trustees are New Zealand tax resident and no election has been made to pay New Zealand income tax on the interest, dividends and royalties as if the trust had a New Zealand resident trustee, then NRWT will apply to that source of income, and the rate of NRWT may be reduced under any applicable double tax treaty. The Law Society submits that this sentence should be amended.
70. The Law Society submits that the words “and New Zealand-sourced taxable distributions” should be deleted from paragraph [11.9]. A beneficiary of a complying trust, wherever they are resident, is only subject to NZ tax on distributions of beneficiary income. A non-resident beneficiary of a complying trust does not receive taxable distributions.

Part 13: Compliance

Miscellaneous amendments and comments

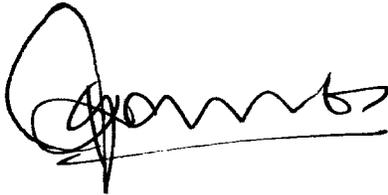
71. Paragraph [13.7] (and the subheading that precedes it) provides that disclosure is only required in respect of non-complying trusts. The disclosure obligations under sections 59(1) and 59(2) of the Tax Administration Act 1994 do not distinguish between the types of trusts (unlike the disclosure obligations under section 59B which are specifically directed at “foreign trusts”). The Law Society submits that the reference to non-complying trusts in paragraph [13.7] (and the subheading that precedes it) should be deleted and replaced with the requirements in sections 59(1) and 59(2) of the Tax Administration Act 1994.
72. Paragraph [13.37] provides that, prior to the enactment of section 43B of the Tax Administration Act 1994, non-active trusts were required to file nil tax returns. That is not the case where the trust did not have an IRD number and had not taken a “tax position” (and, therefore, was not a

“taxpayer”). The Law Society submitted on this point with regards to the Taxation (Bright-Line Test for Residential Land) Bill 2015. The Officials’ comment on this submission was that “the proposed amendment will provide that complying trusts that do not have any income or deductions (as defined in the provision) do not have to file returns. The provision will be explained in the Tax Information Bulletin for the Bill”. However, the Tax Information Bulletin did not refer to the position of trusts without IRD numbers and the comment in paragraph [13.37] appears to be contrary to the position set out in the Officials’ Report. The Law Society submits that paragraph [13.37] should be amended to take into account the previous submissions and response.

Conclusion

73. This submission was prepared with assistance from the Law Society’s Tax Law Committee. If you wish to discuss this further please contact the committee convenor Neil Russ, through the committee secretary Jo Holland (04 463 2967 / jo.holland@lawsociety.org.nz).

Yours faithfully

A handwritten signature in black ink, appearing to read 'Tim Jones', with a horizontal line underneath.

Tim Jones
Vice-President