

19 March 2026

Tax Technical
Inland Revenue
By email: public.consultation@ird.govt.nz

Tēnā koe,

Returns of capital: Off-market share cancellations – bright line tests and the Commissioner’s notice requirements and other matters

1. The New Zealand Law Society Te Kāhui Ture o Aotearoa (**Law Society**) welcomes the opportunity to comment on ED0267, a draft operational statement prepared by Inland Revenue (**IR**) regarding the notice requirements applying under the “bright line tests” for share cancellations (the **Draft OS**). Specifically, the Draft OS considers the requirement in section CD 22(3)(b) of the Income Tax Act 2007 (**ITA**) for the Commissioner to have given a notice under section CD 22(8) before the bright line test is satisfied for a capital reduction of 10% to 15%.
2. The Law Society considers that the Draft OS provides welcome guidance for taxpayers in this area, and will be of practical assistance for those undertaking a share capital repurchase. Our comments on the Draft OS, prepared with the Law Society’s Tax Law Committee, are set out below.

Paragraph 19 – the “three categories”

3. The Law Society suggests that paragraph 19 of the Draft OS be expanded slightly and restructured to make the “three categories” of pro rata share cancellations more explicit, those categories being:
 - a. Pro rata share cancellations of 15% or more – no notice required for bright line to be satisfied.
 - b. Pro rata share cancellations of 10% or more but less than 15% - notice required for the bright line to be satisfied.
 - c. Pro rata share cancellations of less than 10% - bright line test cannot be satisfied.

Paragraph 24 – notice of capital reduction

4. Paragraph 24 of the Draft OS refers to the timing requirement in the definitions of “*fifteen percent capital reduction*” and “*ten percent capital reduction*”, that market value be assessed “*at the time the company first gave notice to shareholders of the cancellation*”.
5. The Law Society recommends that paragraph 24 provide basic examples of what might qualify as notice to shareholders for these purposes. For example, the relevant time could

be when a company's board provides notice to shareholders of an offer to repurchase shares under the Companies Act 1993 (CA), when a section 107 entitled persons resolution is signed under the CA or simply when an email or other written correspondence is provided to shareholders by the board in relation to the proposed cancellation (depending on the circumstances, including the number of shareholders and any formal inter-relationships between the shareholders).

6. The time at which market value is assessed can be material depending on the particular factual circumstances.

Paragraph 32 – nature of indicative view

7. Paragraph 32 of the Draft OS refers to an "indicative view" being provided to significant enterprises customers. The Law Society considers it would be helpful to remind taxpayers of the legal status of an "indicative view", being a considered view of IR as to the legal requirements but ultimately being non-binding on IR, and which taxpayers should bear in mind before factoring that into their decision-making and proceeding on a basis consistent with that indicative view.

Paragraphs 34 to 37 – requirement for section CD 22(8) notice to be issued before payment

8. The following statements are made in paragraphs 34 to 37 of the Draft OS:
 - a. Paragraph 34: *"Notice must be sought before the shares are cancelled."*
 - b. Paragraph 35: *"The time to characterise a payment as being excluded from being a dividend under s CD 22 is the time of payment."*
 - c. Paragraph 37: *"Therefore, the Commissioner must have issued a notice before the payment reflecting the share cancellation is made."*
9. The Law Society generally agrees with the principle that the assessment as to whether a dividend arises, or an exclusion applies, is at the time of payment. Section CD 22(1) expressly states that it applies when a company "pays" an amount to a shareholder.
10. The Law Society disagrees, however, that notice under section CD 22(8) must necessarily be sought before the shares are cancelled. That is not provided for in the ITA.
11. The Law Society is concerned that IR is introducing an unnecessary, extrastatutory, timing restriction into section CD 22. The notice requirement is there to ensure that a share cancellation is not in lieu of the payment of a dividend, is a genuine return of capital and that the Commissioner is aware of the share cancellation. Best practice would of course be to seek the notice prior to the share cancellation taking effect, but a scenario where the notice is provided by IR after the fact would nevertheless provide an outcome that is consistent with the purpose of section CD 22.
12. The provision of notice after the fact is an interpretation that is open to IR on the statutory wording. The interpretation of section CD 22 in the manner suggested in the Draft OS creates the potential for an unnecessary "foot fault" in the legislation and could mean

legitimate scenarios where a section CD 22(8) notice could have been provided are excluded.

13. For example, a taxpayer might rely on a "fifteen percent capital reduction" under section CD 22(3)(a) but then subsequently determine that the 15% threshold was not quite satisfied in relation to a share cancellation. If the taxpayer falls into the 10% to 15% category in section CD 22(3)(b), there should be scope to seek a notice from IR under section CD 22(8) even though the cancellation of shares has already occurred. A dividend would otherwise necessarily arise under the interpretation in the Draft OS, which seems inconsistent with the policy intent of section CD 22.
14. A similar scenario might arise if a share repurchase and cancellation was required in short order for commercial reasons and prior to the expiry of the period of 28 days that is specified at paragraph 46 of the Draft OS as being the IR response period. In the Law Society's view, there seems no clear reason why the notice under section CD 22(8) could not similarly be sought from the Commissioner after the fact. There is again otherwise a risk that certain share cancellations that are genuine capital returns will be characterised as a dividend simply as consequence of this timing issue.

Paragraph 49 – practical implications of receiving notice

15. The Law Society considers that the analysis and commentary at paragraph 49 should be reconsidered. The key principle in paragraph 49 seems to be that any section CD 22(8) notice is not binding on IR and could at any point be subsequently withdrawn. That position undermines the statutory scheme, which is to give comfort to taxpayers that the Commissioner has the relevant information available to consider a particular share cancellation and to determine that it is a genuine capital return for the purposes of section CD 22.
16. Paragraph 49 of the Draft OS makes the statements that:
 - a. *"However, the notice does not legally require the Commissioner to maintain the position in the notice."*
 - b. *"Although the Commissioner may be satisfied when he issues the notice under subs (8), if he has cause to, he can later take issue with the dividend exclusion applying whether information has been withheld or not."*
17. While the Law Society acknowledges that a section CD 22(8) notice is not binding on the Commissioner, the Law Society considers that any decision by the Commissioner to revoke a section CD 22(8) notice will only be made in exceptional circumstances. The Law Society agrees with the following two scenarios noted in the Draft OS:
 - a. a taxpayer has withheld relevant information (or possibly misrepresented information) relating to the share cancellation that is the subject of the notice; or
 - b. the share cancellation that is the subject of the notice forms part of a wider arrangement giving rise to a "tax avoidance arrangement" under section BG 1.

18. However, outside those scenarios, the Law Society's view is that any revocation of a section CD 22(8) notice must be rare, and for good reason because of the potentially significant consequences for the taxpayer, and for its shareholders. A section CD 22(8) notice is not an "indicative view", and taxpayers (and shareholders) should have confidence that a notice can be relied upon for the purposes of determining the correct financial and income tax position. The Law Society considers that paragraph 49 should be revised accordingly to reiterate that it will only be an exceptional case that the Commissioner will revoke a notice.

Paragraphs 57 to 60 – breaching off-market share cancellation rules unintentionally or otherwise

19. The Law Society considers that it follows from the principles set out in the preceding comments that the analysis and commentary in paragraphs 57 to 60 should be reconsidered.
20. Paragraph 57 refers to a scenario where a cancellation of shares has been undertaken in accordance with section CD 22, but it is subsequently determined that part of the payment made to shareholders was *"in lieu of the payment of a dividend"*.
21. The following statements are made in paragraphs 58 and 59 of the Draft OS:
- a. *"However, it is unclear whether the Commissioner should be taken to have given the required notice if the pre-condition of that notice that the share cancellation was not in lieu of dividend has not been met."*
 - b. *"This means for any capital reduction, for an amount to be excluded from being a dividend, even if the Commissioner has given a notice that subs (6) does not apply, subs (6) must also not actually apply."*
22. The Law Society recommends that the analysis be revisited to provide confidence for taxpayers acting in reliance on a section CD 22(8) notice.
23. The position that subsection (6) must not actually apply, when the Commissioner has considered the share cancellation and given notice under subsection (8) that it does not apply, seems somewhat circular. The point of section CD 22(3)(b) is to enable taxpayers to make the case to the Commissioner that a *"ten percent capital reduction"* is a genuine return of capital and not a disguised dividend. As noted above, the Law Society considers that taxpayers should be able to rely on a section CD 22(8) notice absent a scenario of the type listed above (i.e. withholding information or section BG 1 applying). The risk, otherwise, is that the statutory scheme provided for in section CD 22(3)(b) is undermined.
24. Finally, there is also a reference at paragraph 58 of the Draft OS to *"the bright line test in section CD 22(8)"* which the Law Society does not consider is strictly correct. The bright line tests are contained in section CD 22(3). Section CD 22(8) is a separate requirement that must be satisfied to qualify for the dividend exclusion in section CD 22 (albeit that section CD 22(8) is relevant to section CD 22(3)(b)). The legislative position is more correctly expressed in the first sentence of paragraph 59.

Next steps

25. Should you wish to discuss any aspect of this feedback, please contact Aimee Bryant, Manager Law Reform and Advocacy (aimee.bryant@lawsociety.org.nz).

Nāku noa, nā



Mark Sherry
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