

15 November 2021

Reporting requirements for domestic trusts  
C/- Deputy Commissioner, Policy and Regulatory Stewardship  
Inland Revenue Department  
**Wellington**

By email: [policy.webmaster@ird.govt.nz](mailto:policy.webmaster@ird.govt.nz)

**Re: Reporting requirements for domestic trusts – issues paper**

**1. Introduction**

1.1 The New Zealand Law Society | Te Kāhui Ture o Aotearoa (**Law Society**) welcomes the opportunity to comment on the issues paper: *Reporting requirements for domestic trusts (issues paper)*. The Law Society has prepared and filed a separate submission on the draft operational statement: *Reporting requirements for domestic trusts*. The Law Society's submissions in relation to the issues paper are set out below.

**2. Commencement date**

2.1 The commencement date of the financial reporting requirements for trusts in section 59BA of the Tax Administration Act 1994 was set by the Taxation (Income Tax Rate and Other Amendments) Act 2020, which was enacted under urgency and with no prior consultation with key stakeholders.

2.2 The Law Society recommends that the implementation date of the financial reporting rules is deferred until the 2022/23 income year, as taxpayers will not know what the financial reporting standards are, and what costs will be involved in complying with those standards, until the Order in Council is finalised. If the disclosure requirements apply from the 2021/22 income year, then affected taxpayers will not be able to restructure their trust arrangements to minimise compliance costs before disclosure is required.

2.3 The Law Society acknowledges that a legislative amendment will be required to defer the commencement date of the financial reporting requirements until the 2022/23 income year. That legislative amendment could be included in the Taxation (Annual Rates for 2021-22, GST, and Remedial Matters) Bill, which is currently before the Finance and Expenditure Select Committee.

**3. Valuation methodology**

3.1 The proposed criteria for applying the different valuation methodologies in the issues paper are more restrictive than the equivalent criteria that apply to foreign trusts with one or more

New Zealand resident trustees in the Tax Administration (Financial Statements – Foreign Trusts) Order 2017 (the Foreign Trusts Order).

- 3.2 Paragraph 2.5(ii) of the issues paper refers to using “historical cost, when tax values are not consistent with double entry or accrual accounting or when, in the preparer’s opinion, historical cost provides a better basis of valuation ...”. In contrast, the equivalent provision in the Foreign Trusts Order simply states in paragraph 4(c)(ii): “historical cost with impairment or depreciation as appropriate ...”.
- 3.3 The Law Society recommends that the wording in the Foreign Trusts Order should be used in the Order in Council that will apply to other trusts. This means that the preparers of financial statements for these trusts can also choose, without restriction, whether to use tax values, historical cost or market values.

#### **4. De minimis threshold for “small trusts”**

- 4.1 The Law Society supports a de minimis threshold for small trusts, but notes that the financial reporting concessions for small trusts are relatively minor, so the threshold for what amounts to a small trust should be relatively generous to save compliance costs.
- 4.2 The proposed de minimis threshold for income and expenditure appears to be based on actual income and expenditure, rather than taxable income and deductible expenditure. Many family trusts generate little taxable income, and such trusts do not constitute a threat to the tax base. These trusts may not, however, meet the income and expenditure thresholds for a small trust (as currently proposed), as these trusts may incur significant costs relating to those properties, such as rates and body corporate fees.
- 4.3 The Law Society recommends that the income and expenditure thresholds for small trusts is based on taxable income and deductible expenditure. This will mean that many more family trusts that own lifestyle assets will be treated as small trusts, which will make compliance with the new reporting requirements simpler.
- 4.4 Many family trusts hold lifestyle assets, such as the family home and, perhaps, a holiday home. The proposed de minimis threshold for the total value of trust assets may therefore prejudice against trusts which hold family homes in Auckland and other districts with higher than average house prices. For example, as at 27 September 2021, 23 of Auckland’s 208 suburbs had a median house price exceeding \$2 million.
- 4.5 The Law Society recommends further consideration of how this could be made more equitable. This could mean excluding the family home from the asset threshold for small trusts, or slightly decreasing the asset threshold for small trusts, with the family home excluded.
- 4.6 Excluding the family home from the asset threshold also means that trustees will not have to bear the cost of valuing the family home to determine whether the modified financial reporting rules for small trusts apply (or continue to apply) where the value of trust assets is close to the asset threshold. Requiring trusts which own a family home and, perhaps, a holiday home, to monitor and value those assets annually to determine whether a different set of financial reporting rules applies imposes unnecessary compliance costs.

#### **5. Transactions involving associated persons**

- 5.1 Section 59BA(2)(b) and (d) of the Tax Administration Act 1994 requires disclosure of full details of any settlements made on a trust including the “amount and nature” of each

settlement, and also information concerning any distributions by the trust. These obligations capture the provision of in-kind benefits to a beneficiary such as the use of trust property or a loan to a beneficiary for no interest or below market interest. They also capture in-substance settlements such as low-interest and interest-free loans to the trust.

- 5.2 As settlors and beneficiaries will be associated persons of the trust, any non-arm's length transactions between the trust on the one hand, and a settlor or beneficiary on the other, will be fully recorded and disclosed in compliance with section 59BA(2)(c) and (d). As such, there appears to be little benefit in identifying other associated persons (potentially a broad class) whose dealings with the trust are on arm's length terms, and therefore do not give rise to either a settlement or a distribution.
- 5.3 The Law Society considers that the requirement to identify transactions involving associated persons involves unnecessary compliance costs and should be removed, given that Inland Revenue is primarily interested in obtaining information about transactions between settlors, trustees and beneficiaries, all of which will be captured under the reporting requirements in section 59BA(2)(b) and (d).

**6. Next steps**

If you have any questions or would like to discuss these comments, please do not hesitate to contact the Tax Law Committee convenor Neil Russ, through the Law Society's Law Reform and Advocacy Advisor, Emily Sutton ([Emily.Sutton@lawsociety.org.nz](mailto:Emily.Sutton@lawsociety.org.nz)).

Yours faithfully



Herman Visagie  
**Vice President**