# Cross-border workers-issues and options for reform

*An Officials' Issue Paper*

*2 December 2021*

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2 December 2021

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Dear David

## Cross-border workers – issues and options for reform

Thank you for the opportunity to comment on the Officials' Issues Paper.

The objective of the issues paper is to highlight the domestic technical tax and policy issues that arise for businesses bringing workers to New Zealand where those workers are either employees or non-resident contractors. The focus is on the payer's employment-related tax obligations.

The paper clarifies and simplifies the PAYE rules for employees on a shadow payroll and non-resident contractors.

CA ANZ welcomes the pragmatic solutions offered to address the problems faced by non-resident employers and cross-border workers. However, there are some subjects that the issues paper does not address, namely:

- Whether the presence of a remote worker in New Zealand creates a permanent establishment for their non-resident employer;

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- The home country claiming taxing rights over the employment income despite there being relief granted in a double tax agreement;
- Other employment obligations such as ACC levies and KiwiSaver;
- Issues affecting New Zealand tax residents working overseas; and
- The dynamic and changing regional ways firms do business e.g., global distributed workforce model

The key points we raise are:

- The 28-day period for catch-up payments should be increased;
- Flexible PAYE arrangements should not be limited to shadow payroll employees only;
- The merits of an end-of year square up via the PAYE system should be explored;
- The different application of the territorial principle for PAYE and NRCT warrants further consideration;
- Consideration be given to using the threshold test as a safe harbour; and
- Cross-border workers who have to register as an IR56 taxpayer may find this an onerous obligation; and
- The NRCT threshold tests should be increased to at least $50,000.

Should you wish to discuss this submission further please contact John Cuthbertson or Teri Welham.

Yours sincerely

John Cuthbertson FCA
**CA ANZ NZ Tax Leader**

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**Tax Advisory Group Chair**



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# Contents

PAYE, FBT and ESCT....4
Overview....4
Territorial approach....8
FBT and ESCT obligations....11
Transfer employment related tax obligations to New Zealand entity....12
Questions for submitters....14
PAYE, FBT and ESCT....14
NRCT....15
NRCT withholding thresholds....15
Simplification of threshold tests....17
NRCT flexibility....18
Exemption certificates....19
Alternatives to exemption certificates....21
Bonds given by a non-resident contractor....22
Questions for submitters....23
NRCT....23
Technical and remedial measures....24
Superannuation contributions: FBT liability....24
Trailing payments and FBT....25
Shadow payrolls: recognition of income....25
Non-resident contractors' threshold tests do not apply to non-resident entertainers....26



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# PAYE, FBT and ESCT

## Overview

Since the introduction of PAYE in 1958 the number of employees who work in New Zealand for a non-resident employer has grown. Feedback from non-resident employers demonstrates that the PAYE rules need to be clearer and that they should be more flexible.

At page 12 of the Issues Paper, it is stated:

> *"Non-resident employees are not always comparable to local employees, which may justify a different policy approach ."*

Section CW 27 of the Income Tax Act 2007 and our double tax agreements contain an exemption from New Zealand income tax for persons who come to New Zealand to work for a short period of time (92 days and 183 days respectively). These exemptions are subject to specified conditions being met in addition to a day-count test. Concerns have been raised that these tests are not fit for purpose.

Officials are of the view that the day-count tests remain appropriate. However, they do agree that where the day-count test has been breached, the process to correct the employee's tax position can be complex, time consuming and the compliance costs can be disproportionate to the amount of tax involved.



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> *"Officials recognise that it is not always practical to collect PAYE from the income of cross-border employees under normal arrangements and, therefore, enabling greater PAYE flexibility for such employees is desirable.[1]"*

Officials consider only employers who operate a shadow payroll[2] should be allowed to operate PAYE, FBT and ESCT on a more flexible basis in respect of cross-border employees linked to that shadow payroll. Shadow payrolls would be identified on an employers' employment income information form. Normal PAYE rules apply to cross-border employees paid from an ordinary New Zealand payroll.

## Proposal: Catch-up facility

If an employee breaches the day-count threshold when the employer reasonably believed an exemption would apply, a catch-up payment should be allowed. PAYE, FBT and ESCT would be calculated from the first day of presence in New Zealand although payment would be due within 28 days of the employer first becoming aware of breach. This would be the earlier of the time the employer knows the threshold has been breached and the time the employer expects the threshold to be breached. In addition, the employer is required to have taken reasonable measures to manage their employment-related obligations.

Reasonable measures could include taking tax advice relating to the assignment; asking questions about the employee's New Zealand connections; keeping records of the assignment, including any review of business travel etc; monitoring employee time in New Zealand; and taking prompt action to discharge tax obligations when the employee's circumstances change.

[1] Issues Paper page 13
[2] A payroll that records details of the employee's remuneration for the purposes of the host country revenue authority.



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## Comment 1.

CA ANZ supports the introduction of flexible PAYE arrangements that permit a catch-up payment if an employee has breached the day-count threshold. We recommend increasing the period to correct the situation beyond 28 days. In many cases, collecting the necessary information from the home country employer takes far longer than 28 days. The practicalities of obtaining the information, performing the calculations, having the calculations checked and authorised, and obtaining the payment from the home country employer can take at least 3 months. We also note that obtaining Inland Revenue numbers for cross-border employees who do not have New Zealand bank accounts frequently takes longer than 28 days.

## Proposal: Flexible PAYE arrangements

Two options proposed:

### Modified PAYE arrangements - based on the UK model.

Under an agreement payroll is operated on an estimated basis for employees. The employer must tax equalise the employee's general earnings e.g., salary bonus and cash equivalent of any non-cash benefits in kind; tax is calculated on a gross-up basis and the employer must undertake an in-year review of the reported compensation to capture any material changes. Final adjustments can be made in each employee's self-assessment tax return.



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## In-year square-ups via PAYE system (similar to catch-up facility above)

Allow employer additional time to capture all compensation items for each employee. The employer would report these items and make a "catch-up" payment. The payment should occur no later than 28 days from the employer first becoming aware of the need to adjust or report the employee's remuneration. Final adjustment would be made via the employee's self-assessment tax return.

# Comment 2.

Bolstering the PAYE system by allowing in-year square ups for those employees on a shadow payroll will be welcomed by many employers (but would continue to exclude those employers who, for whatever reason, do not operate a shadow payroll). We reiterate our earlier comments, the 28-day period should be increased to provide employers with ample time to collect the information necessary.

In our view, in-year square ups should not be limited to shadow payroll employees only (shadow payrolls can be expensive). Will Inland Revenue systems recognise if the foreign employee is on the ONLY payroll (as being a 'shadow payroll') i.e., there is no other 'ordinary' payroll.

In addition, we recommend you examine the merits of an end-of-year square-up via the PAYE system for employees on shadow payrolls. This would simplify the compliance and allow employers to "report once, report right" rather than continually having to make catch-up payments.

# Proposal: repeal PAYE employer bond

Repeal of the PAYE bond employer bond provision.

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## Comment 3.

CA ANZ supports the repeal of the PAYE employer bond provision.

# Territorial approach

The Paper confirms the approach taken in draft operation statement ED0223, whether an employer is subject to New Zealand laws is determined by assessing whether the employer has a sufficient presence in New Zealand.

Officials suggest a threshold test operate alongside "sufficient presence test". Where a threshold is met, regardless of whether the employer had a sufficient presence, the employer would have to apply the PAYE, FBT and ESCT rules.

If an employer did not have a sufficient presence and did not meet the threshold there would be no obligation to apply the rules. However, they could still choose to assume responsibility for employment-related taxes.

## Comment 4.

We acknowledge applying a territorial limitation to PAYE ensures the effectiveness of the collection mechanism against the employer. The decision not to extend the territorial approach to NRCT,[3] suggests a pragmatic approach has been adopted for PAYE.

Whilst we understand the rationale for not extending the territorial approach to NRCT, because the PAYE rules apply to both PAYE and NRCT, the lack of

[3] Paragraph 3.5 page 23



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consistency is concerning. We recommend further analysis and support for the position taken on territoriality be provided.

## Proposal: Threshold that demonstrates a sufficient presence

The threshold should be the lower of:

1. $500,000 of gross employment-related taxes per current year, or
2. Five employees present in New Zealand (full and part-time employees) whether they are tax resident in New Zealand or not.

## Comment 5.

CA ANZ supports the introduction of a threshold test. However, we recommend consideration be given to using the threshold test as a safe harbour. Where the threshold is not met, a non-resident employer would be treated as not having a sufficient presence in New Zealand. This would be a simpler way for non-resident employers to establish whether they had an obligation to apply the PAYE, FBT and ESCT rules.

## Proposal: elect in when there is no obligation

Employer can choose to assume responsibility where the threshold is not met. They would remain responsible until they made alternative arrangements, e.g., use a local payroll provider, arrange a related New Zealand entity to assume the obligation, or no longer need to make employment-related tax payments.



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## Comment 6.

We believe it is sensible to allow employers to assume the obligation.

## Proposal: threshold - non-resident associated person employees included

The threshold would apply to employees of non-resident associated persons.

## Comment 7.

We agree, to support the integrity of the threshold employees of non-resident associated persons should be included but they should only be encompassed to the extent that the activities of the associated persons are linked. That is, there is a reasonable connection In many instances large corporate groups have entirely separate divisions that never connect or impact on each other.

## Proposal: employee obligations

Where the threshold is not met and no New Zealand entity is willing to take on the PAYE and other tax obligations, the employee would need to register as an employer and report taxes to Inland Revenue under an IR 56 arrangement. Officials do not think it is appropriate to extend the proposals to increase PAYE flexibility to IR 56 arrangements.[4]

[4] Paragraph 2.49



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## Comment 8.

In our view there is a significant difference between a New Zealand taxpayer such as a domestic worker who is an IR 56 taxpayer and cross-border workers.

There is an implicit assumption in the issues paper that a non-resident employer will support an employee situated in New Zealand or provide some external support to help them meet this obligation. This may not be the case. Complying with this obligation may be onerous for many employees who do not have the necessary skills. To meet New Zealand tax obligations an understanding of New Zealand tax laws is required, for example an employee will need to understand the rules around employer provided accommodation and expenditure on account, which allowances are taxable, and which are non-taxable, which benefits are subject to FBT or ESCT and when it is necessary to gross-up payments. In addition, complex calculations are often required. Further consideration should be given to how these issues can be addressed and whether there is an alternative solution.

PAYE flexibility should apply to "IR 56" cross-border workers. Breaching the day-count threshold is also a risk that these workers face.

## FBT and ESCT obligations

As a consequence of the territorial approach to PAYE, a non-resident employer who does not have a sufficient presence in New Zealand has no liability for FBT or ESCT.

## Proposal: equalise tax treatment for FBT and ESCT

A liability for FBT and ESCT will arise regardless of an employer's presence in New Zealand.



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## Comment 9.

We support extending the tax obligation to include FBT and ESCT. This is a sensible policy decision that prevents a fiscal loss to the New Zealand tax base when the salary packages of non-resident employees include non-cash benefits and superannuation contributions.

## Proposal: employee accounts for FBT and ESCT

An employee of an employer with no New Zealand presence to be liable to account for FBT and ESCT.

## Comment 10.

Although we support equalising the FBT and ESCT treatment we are concerned that this cost may be borne by the employee from their after-tax earnings when the taxes are designed to be met by the employer. In addition, the administrative and compliance burden that is being placed on cross-border workers (refer Comment 8. makes us uneasy.

## Transfer employment related tax obligations to New Zealand entity

Where employees come to work for New Zealand entities on assignment or they are in practice working for a New Zealand entity, Officials consider it is appropriate for the New Zealand entity to discharge the non-resident employer's employment tax obligations, regardless of any formal arrangement.



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On the other hand, where an employee is present in New Zealand and their work only benefits their home country employer and that employer does not have a sufficient presence in New Zealand, two options exist:

- a related New Zealand entity may choose to assume liability for the employment related tax obligations; or
- the liability may be automatically transferred to the related New Zealand entity.

Officials do not favour the compulsory transfer of the employment related tax obligations to a related New Zealand entity.

## Proposal: transfer employment related tax obligations to a related New Zealand entity

Where a related New Zealand entity chooses to assume liability, that entity should notify Inland Revenue, the liability has been transferred. The home country employer and the New Zealand entity would have joint and several liability for tax compliance.

## Comment 11.

The proposal to allow the transfer of employment related tax obligations to a related New Zealand entity is a practical solution that many non-resident employers will welcome. It is an approach commonly adopted by non-resident employers, despite there currently being no legislative backing. We also do not favour the compulsory transfer of employment related obligations. In many instances a non-resident employer may not be willing to transfer these obligations to a related entity, e.g., for confidentiality reasons.



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# Questions for submitters

# PAYE, FBT and ESCT

| Questions | Comment |
|---|---|
| Should PAYE flexibility be available to a wider group of employees than those on shadow payrolls? If so, which other groups of employees should be included? | Yes. Refer Comment 2. Comment 8. |
| Do you see any practical issues or concerns in permitting PAYE flexibility? For example, what would be the impact on split-paid employees? | Refer Comment 1. Comment 2. |
| Which option to increase PAYE flexibility do you prefer and why? | |
| Do you support removal of the PAYE employer bond requirement? | Yes. Refer Comment 3. |
| Should the PAYE obligation for non-resident employers have a threshold test? If so, is a threshold of the lower of:<br>— $500,000 of gross employment-related taxes per current tax year, or<br>— five employees present in New Zealand appropriate? | Refer Comment 4. Comment 5. |
| Do you consider it appropriate to transfer PAYE, FBT and ESCT obligations to a New Zealand entity? | Refer Comment 11. |
| What problems or issues do you see, if any, with the transfer of the obligations? | |

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# NRCT

A person who pays a non-resident contractor is required to withhold non-resident contractors' tax (NRCT), a schedular tax, from the contract payment. NRCT is collected via the PAYE system.

It can apply to contracts where both payer and contractor are non-residents and only the activity takes place in New Zealand. There is no intention to extend the territorial approach to NRCT, as this would exclude the payer from the withholding obligation.

## Comment 12.

Whilst we understand the rationale for not extending the territorial approach to NRCT, because the PAYE rules apply to both PAYE and NRCT, the lack of consistency is worrying. We recommend further analysis and support for the position taken on territoriality be provided.

## NRCT withholding thresholds

There are two exemptions where:

1. the non-resident contractor is present in New Zealand for 92 days or less in a 12-month period and is entitled to full relief under a double tax agreement;

2. the total payments received by the non-resident contractor are $15,000 or less in a 12-month period.

Both exemptions are problematic because the payer must consider matters unrelated to the contract payment in question, e.g., work performed for another payer or holidays. This is an "all circumstances" view. It requires full disclosure



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from the contractor, however the payer bears costs of non-compliance if exemption breached.

Officials consider "all circumstances" view imposes an excessive compliance burden on the payer.

## Proposal: "single payer" view

Payer will only need to consider the thresholds relating to their contract with the non-resident contractor. The single payer view should include related payers, such as members of a consolidated group.

## Comment 13.

We welcome the "single payer" view. As acknowledged at paragraph 3.8 the current "all circumstances" view is difficult to comply with in practice. The "single payer" view should alleviate some of the difficulties payers face. However, we envisage that payers will still experience some difficulties in complying with the "single payer" view. For example, where the contract is a fixed price the non-resident contractor may still need to provide information so the payer can track the number of days the non-resident contractor works on the contract.

## Proposal: reporting of non-resident contractors to Inland Revenue

Report would include payee's name, New Zealand or home country address and New Zealand IRD number or foreign tax identification number.

Reports would be due on 15th of each month. The first due, 15 days after the end of the month in which the first payment was made to the non-resident contractor.



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## Comment 14.

To some extent the proposed reporting requirements duplicate information already provided. Currently non-resident contractors are required to complete form IR330C and provide it to the payer. They provide their full name, IRD number, tax rate and schedular payment activity number. The schedular payment activity number for a non-resident contractor is 26 (not a company) and 27 (a company). Where NRCT is deducted and paid to Inland Revenue some of this information will be provided on form IR348.

However, we acknowledge the proposed reporting requirements will give Inland Revenue a more complete picture. It will include non-resident contractors who are exempt from withholding.

The paper does not state how the extra reporting signalled at paragraph 3.11 would be effected. If Inland Revenue is intending for the extra NRCT information to be reported via payroll reporting then this could be problematic. In most organisations there are tight controls maintained around an entity's payroll. Those responsible for the payroll do not welcome ad hoc additions as these all add to the audit burden and risk of fraud. Payroll is usually managed by HR, non-resident contractors are managed in the business. Larger businesses consider that including all NRCT reporting in their payroll reporting would excessively add to their compliance costs/burden.

# Simplification of threshold tests

Officials consider that by moving to a "single payer" view and enabling greater flexibility for corrections, reform of the threshold tests is unnecessary.



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## Comment 15.

We disagree with the view that there is no need for reform of the threshold tests. The $15,000 de minimis has not been adjusted since it was first introduced in 2003. It is too low and should be increased to at least $50,000. We do not agree with the assertion that leaving it where it is could leave to revenue loss. The primary risk of revenue loss with an NRCT arises from its complexity and entities being unaware that it could even apply. Lifting the threshold would reduce a compliance burden for the compliant.

## NRCT flexibility

Factors outside the payer or contractor's control can mean thresholds are breached. Officials consider flexibility of NRCT can be improved.

## Proposal: NRCT code

To distinguish NRCT from other withholding taxes a separate NRCT code is proposed.

## Comment 16.

The proposal to use a separate NRCT code is sensible. This may eliminate the current need for a separate activity code (refer form IR 330C).

## Proposal catch-up payment

Allow a catch-up payment via ordinary NRCT filing to account for NRCT due for the prior period where payer can demonstrate that they made reasonable enquiries or took reasonable steps to confirm thresholds would not be exceeded.



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The correction should be made within 28 days from the date when it became apparent a threshold would be breached.

## Comment 17.

We reiterate our previous comments, the 28-day period should be extended.

## Exemption certificates

Where thresholds do not apply, non-resident contractors can obtain an exemption certificate where they meet one or more of the following conditions:

- The payment is not assessable income;
- The contractor provides a bond or other security;
- The contractor has a "good compliance history" in the previous 24 months that is expected to continue.

To improve the flexibility of the current exemption certificate system it is proposed:

## Proposal: retroactive certificates of exemption

Where the exemption certificate is issued after first payment, it would also cover payments before its issue date. Retroactive period should be set at 92 days.

## Proposal: broader certificates of exemption

The exemption certificate would be issued for a two-year period where it is granted based on good compliance history



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## Comment 18.

We welcome improvements to the exemption certificate system that would allow certificates to be issued for a two-year period and certificates that have retrospective effect. However, we recommend there should be an alternate mechanism for taxpayers to apply for the term of a particular contract This would avoid the need to seek subsequent certificates for a short period of time freeing up both taxpayer and Inland Revenue resources.

Further, there is no good reason to limit the retroactive period to 92 days. The entities approaching Inland Revenue are trying to comply under the NRCT framework. A 92-day limit could incentivise an entity to take no further action and, where that entity is entitled to relief under a DTA, there is no impact on the tax base in any case.

## Proposal: role of nominated taxpayer

Where the non-resident contractor cannot show good compliance history (say because they use separate project vehicles for each contract) a nominated taxpayer could establish a good compliance history for the purpose of obtaining exemption certificates for related non-resident contractors. The approach could also include income tax, GST, and other tax obligations.

The nominated taxpayer would inform Inland Revenue it was acting as agent and would have joint and several liability for the tax obligations of the non-resident contractor.

## Comment 19.

The proposed amendment that allows a non-resident contractor to nominate a taxpayer to act as agent so they can obtain an exemption certificate is positive.



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Nonetheless, in our view, it is unfair to make the agent joint and severally liable for the tax obligations of the non-resident contractor. This requirement may actively discourage taxpayers from acting as agent.

## Alternatives to exemption certificates

Two alternatives to current exemption process have been considered:

1. Self-certification
2. Register of exempt non-resident contractors

Self-certification is not attractive to Officials. It does not simplify administration, compliance, or address flight risk concerns.

## Proposal: searchable register

Searchable register would include a list of active certificates of exemption and their exemption periods. The register would be limited to certificates issued for good compliance history. Where the contractor is an individual, the New Zealand and home country privacy laws would have to be considered.

## Comment 20.

On the face of it the introduction of a searchable register is positive. However, the exclusion of individuals and limiting it to those contractors who have an exemption for good compliance reduces its value.



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We note sole traders are included on the searchable NZBN register. Similarly, the Financial Service Providers Register (FSPR) includes individuals. A searchable register of active certificates of exemption that includes individuals appears to be comparable to the NZBN register and FSPR. Alternatively, would it be possible to anonymise the register by listing holders by IRD number or foreign tax number.

## Bonds given by a non-resident contractor

A non-resident contractor may apply for an exemption certificate on the basis that they have provided a bond. The provision is rarely used.

## Proposal: repeal bond provision

Repeal the provision that allows a non-resident contractor to apply for an exemption certificate on the basis they have provided a bond.

## Comment 21.

We support the repeal of the provision that allows a non-resident contractor to provide a bond.



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# Questions for submitters

# NRCT

| Questions | Comment |
| --- | --- |
| Do you support changing the withholding exemptions from an "all circumstances" requirement to a "single payer" requirement? Do you see any issues with this change? | Refer Comment 13. |
| Do you support the introduction of a reporting obligation for payers of payments to non-resident contractors? Would you have difficulties in reporting information to Inland Revenue? If so, what issues arise and what could be made easier? | Refer Comment 14. |
| Is further reform of the NRCT thresholds desirable? If so, what reforms would you suggest and how would any resulting integrity risks be managed? | Refer Comment 15. |
| Do you support the proposal to enable greater NRCT flexibility by permitting corrections to be made via catch-up payments? What issues could arise from this approach? | Refer Comment 17. |



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# Technical and remedial measures

## Superannuation contributions: FBT liability

Currently, FBT applies where an employer contributes to a superannuation scheme. Many of our trading partners tax superannuation contributions under PAYE-equivalent systems, consequently unrelievable double tax may arise.

## Proposal: contributions to foreign superannuation schemes and/or a sickness, accident, or death benefit

It is proposed that contributions to foreign superannuation schemes and contributions to a sickness, accident or death benefit fund be made subject to PAYE rather than FBT.



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# Trailing payments and FBT

## Proposal: FBT liability not triggered

The receipt of a trailing payment (e.g., bonus or employment share scheme income) after an employee has left New Zealand but which is taxable in New Zealand does not trigger a liability to FBT except to the extent the benefits relate to time spent working in New Zealand.

# Shadow payrolls: recognition of income

Currently a person whose income is reported for New Zealand tax purposes on a shadow payroll is treated as deriving a PAYE income payment on the 20th day following payment (the pay date). The rule deems the pay date to be recognised for tax purposes as well as reporting purposes. It was intended to allow employers additional time to collate employment income information for reporting purposes.

## Proposal: shadow payroll rule

Amend the shadow payroll rule so that the income would be recognised when paid. This aligns the rule with the ordinary rules for taxing PAYE income payments. Employment income information reporting requirements and withholding tax payment dates would not change.

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## Non-resident contractors' threshold tests do not apply to non-resident entertainers

### Proposal: day-count and monetary thresholds

Clarify the legislation to confirm day count and monetary threshold tests for non-resident contractors do not apply to non-resident entertainers.

### Comment 22.

The proposed technical and remedial amendments suggested above are sensible.



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