

# **Taxation (Neutralising Base Erosion and Profit Shifting) Bill**

Government Bill

## **Explanatory note**

### **General policy statement**

The Taxation (Neutralising Base Erosion and Profit Shifting) Bill introduces amendments to the following enactments:

- Income Tax Act 2007
- Tax Administration Act 1994.

Base Erosion and Profit Shifting (BEPS) activities are used by some multinationals to pay little or no tax anywhere in the world. The Bill proposes a package of measures to counter the particular BEPS strategies observed in New Zealand.

BEPS strategies distort investment decisions, allow multinationals to benefit from unintended competitive advantages over more compliant or domestic companies, and result in the loss of substantial corporate tax revenue. More fundamentally, the perceived unfairness resulting from BEPS jeopardises citizens' trust in the integrity of the tax system as a whole.

In brief, the proposed measures in this Bill will prevent multinationals from using:

- artificially high interest rates on loans from related parties to shift profits out of New Zealand (interest limitation rules);
- artificial arrangements to avoid having a taxable presence (a permanent establishment) in New Zealand;
- transfer pricing payments to shift profits into their offshore group members in a manner that does not reflect the actual economic activities undertaken in New Zealand and offshore; and
- hybrid and branch mismatches that exploit differences between countries' tax rules to achieve an advantageous tax position.

These and some other policy measures contained in this Bill are further described below.

### **Interest limitation rules**

#### *Pricing related party debt*

When borrowing from a third-party, there are commercial pressures for the borrower to try to obtain as low an interest rate as possible—for example, by providing security on a loan and by ensuring their credit rating is not adversely affected by the amount being borrowed.

These same pressures do not exist for related party loans, as an interest payment from a New Zealand subsidiary to a multinational parent is not a true expense from the perspective of the multinational's shareholders. Indeed, it can be profitable to try to increase the interest rate on related-party debt—for example, to shift profits out of New Zealand into a low tax country. This is because the interest paid to the parent is deductible to the subsidiary, thereby reducing its taxable income in New Zealand.

There are 2 main ways to push up the interest rate charged on related party debt:

- First, the foreign parent can excessively debt fund the New Zealand subsidiary, to depress the subsidiary's credit rating and make it look more risky as an investment, and therefore justify a higher interest rate.
- Second, a foreign parent can add terms and conditions into the debt instrument itself to justify a higher interest rate. For example it can subordinate the debt or make the debt have a long duration—both of which would increase the interest rate compared to if they were dealing with each other at arms' length.

To address profit-shifting, the Bill proposes new rules which will limit the interest rate on related party debt. It does this by setting specific rules and parameters to:

- establish the credit rating of the New Zealand borrower; and
- determine (in combination with the credit rating rule) the amount of interest on the debt.

The proposed new rules will require that a group credit rating will apply to the New Zealand borrower—being the foreign parent's credit rating minus 1 notch unless the borrower's own credit rating is equal or higher than its foreign parent's credit rating—in cases where there is a high BEPS risk. A high BEPS risk is when the New Zealand borrower has:

- a high level of debt in New Zealand (more than 40% of its assets); or
- high interest costs; or
- borrowed through a low or no tax jurisdiction.

Taxpayers are also able to choose to use the group credit rating as a safe harbour to reduce compliance costs.

In other cases where the presumed credit rating does not apply, the proposed new rules will allow the borrower's standalone rating to be used, taking into account any

implicit parental support. Under this approach there is still a strong presumption that the New Zealand borrower would be supported by its foreign parent when it is part of a multinational group—and therefore is a less risky borrower compared to an unrelated New Zealand entity.

Where a New Zealand borrower has a high BEPS risk but no identifiable parent they will be required to use a restricted credit rating—being the borrower’s own credit rating if they had no higher than 40% debt and the credit rating cannot be lower than BBB–.

Aside from making the borrower appear riskier with excessive debt funding, the other way interest rates can be inflated is by imposing conditions on the lending that would not normally be found in standard third party debt.

The Bill therefore proposes rules that will generally require the following terms and conditions to be disregarded when pricing related party loans:

- loan terms of more than 5 years;
- subordination; and
- other exotic features (such as interest payment deferral and convertibility to equity at the option of the borrower) that are generally not seen with third-party lending.

However, in some cases the New Zealand borrower may have borrowed from related parties using the same terms and conditions as their third party debt. In such cases, they will be able to retain equivalent conditions when pricing their related party loans, so long as the relevant third party loans comprise at least 25% of their total related party debt. This reflects the fact that when borrowing from a third party, there are commercial pressures to try to obtain a low interest rate, so the borrower is unlikely to agree to unnecessary conditions that increase the interest rate.

#### *Allowable debt levels*

The Income Tax Act 2007 includes some existing thin capitalisation rules that limit the amount of debt that a foreign-owned subsidiary can claim deductions for interest paid. Interest deductions are generally denied to the extent the debt exceeds 60% of the subsidiary’s assets.

The Bill proposes several changes to make the existing thin capitalisation rules more effective.

The most significant change is a proposal to reduce the measure of “assets” by subtracting “non-debt liabilities” (that is, liabilities other than interest-bearing debt). Examples of non-debt liabilities are trade credits, provisions, out-of-the-money derivatives and interest free loans. Australia’s thin capitalisation rules require a similar adjustment for non-debt liabilities.

The concern with the current treatment of non-debt liabilities is that it allows companies to have higher levels of debt (and therefore higher interest deductions) relative to the capital invested in a company by its shareholders. For example, at present if a company purchases some inventory on deferred payment terms, the amount of debt

allowed under the thin capitalisation rules will increase (because the new inventory has increased its assets but its interest bearing debts have stayed the same).

The Bill also proposes a revised anti-avoidance rule targeted at taxpayers who repay a loan immediately before a measurement date.

The Bill also proposes tighter rules for valuing assets. The existing measure of assets typically uses the values reported in the company's published financial statements, with an alternative option to use the current market value of an asset instead. The Bill proposes placing tighter conditions on the current market value option so it is available only if the valuation is made or verified by an independent expert valuer.

The Bill also proposes a tighter limit on the ability for companies owned by a group of non-residents to use related-party debt. It does this by preventing these companies from using the existing 110% limit for their related party debt so that they cannot claim any interest deductions on related party debt to the extent to which the company's debt level exceeds 60% of its assets minus non-debt liabilities.

The Bill proposes 2 exemptions from the thin capitalisation rules to reduce the burden on taxpayers in cases where there is little risk of BEPS. The first exemption is an extension of the de minimis in the outbound rules to the inbound rules, whereby the thin capitalisation rules will not apply if a taxpayer has interest deductions of less than \$1m and does not have any owner-linked debt.

The second exemption applies to infrastructure contracts entered into with the central government or Crown entities. This exemption allows all of an infrastructure project's third party debt to be deductible even if the debt levels exceed the normal thin capitalisation limits, provided the debt only has recourse against the assets associated with the infrastructure project and the income arising from those assets. The purpose of this rule is to improve the competitiveness in the bidding process for Public Private Partnership (PPP) procurement contracts by allowing investors that are subject to the thin capitalisation rules to make bids on a level playing field with investors that are not subject to the thin capitalisation rules.

### **Permanent establishment rules**

New Zealand has 40 Double Tax Agreements (DTAs) with other jurisdictions. Where one of these DTAs applies, New Zealand is only able to tax a non-resident on its income from sales to New Zealand customers if the non-resident has a permanent establishment in New Zealand.

The problem is that some multinationals are able to structure their operations so that their New Zealand sales and associated profits are booked in an offshore entity which under current rules is not considered to have a permanent establishment in New Zealand, despite the fact that, in substance, the sales are generated by New Zealand-based salespeople. As a consequence New Zealand is unable to apply income tax to the multinational's New Zealand sales.

The OECD has recently updated their model tax treaty to address this issue and New Zealand is adopting this into many of our DTAs by signing the OECD's *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS*.

However, a domestic law change is necessary to cover cases where the relevant DTA does not yet include the OECD's new recommendation.

The Bill therefore proposes a new anti-avoidance rule that will deem a multinational to have a permanent establishment in New Zealand if:

- the non-resident supplies goods or services to a person in New Zealand;
- the non-resident is part of a multinational group that is required to file Country-by-Country reports (i.e. the multinational group has more than EUR €750m of consolidated global turnover);
- related entity (either associated or commercially dependant) carries out an activity in New Zealand in connection with that particular sale for the purpose of bringing it about, unless the activity is only preparatory or auxiliary; and
- the arrangement has a more than merely incidental purpose of tax avoidance.

Australia and the UK have already implemented similar permanent establishment avoidance rules in their domestic laws.

The new permanent establishment avoidance rule will not apply if the relevant DTA includes the OECD's new BEPS-related updates to the permanent establishment definition.

### Source rules

New Zealand can only tax non-residents on income that has a New Zealand source under the source rules of the Income Tax Act 2007. The Bill proposes several amendments to expand and strengthen the rules for taxing New Zealand-sourced income:

- An amount of income will be deemed to have a source in New Zealand if New Zealand has a right to tax that income under any applicable DTA. This ensures that whenever New Zealand negotiates taxing rights under a DTA that we can also tax this income under our source rules. This is the same position which Australia takes under its DTAs, and the proposed rule already applies to all income covered by our DTA with Australia.
- In cases where a non-resident business is a resident of a jurisdiction that New Zealand does not have a DTA with, a new definition of permanent establishment may apply to deem any business income earned through a New Zealand permanent establishment to have a New Zealand source. This new definition of permanent establishment is outlined in schedule 23 of the Bill. It is based on the permanent establishment definition in New Zealand's model DTA and includes the BEPS-related updates recommended by the OECD.
- A potential weakness of the life insurance source rules is addressed by ensuring that no deductions are available for the reinsurance of life policies if the premi-

um income on that policy is not taxable in New Zealand, including where the income is not subject to New Zealand tax by operation of a DTA.

### **Transfer pricing rules**

Transfer pricing rules guard against multinationals using related party payments to shift profits offshore by requiring these payments to be consistent with an arm's length/market price that unrelated parties would agree to.

The Bill proposes amendments to strengthen the transfer pricing rules so they align with the OECD's transfer pricing guidelines and Australia's transfer pricing rules. This involves amending New Zealand's transfer pricing rules so that:

- they refer to using the 2017 OECD transfer pricing guidelines as guidance for how the rules are applied;
- the economic substance and actual conduct of the parties have priority over the terms of the legal contract. This is achieved by requiring the transfer pricing transaction to be “accurately delineated” consistent with section D.1 of chapter I of the new OECD guidelines;
- transfer pricing arrangements which are not commercially rational because they include unrealistic terms that third parties would not be willing to agree to can be disregarded or replaced. This is consistent with the chapter I, section D.2 of the new OECD guidelines;
- the legislation specifically refers to arm's length conditions (as per Australia's legislation) to clarify that the transfer pricing rules can be used to adjust conditions other than the price;
- the onus of proof for demonstrating that a taxpayer's transfer pricing position aligns with arm's length conditions is shifted from Inland Revenue to the taxpayer (consistent with the onus of proof being on the taxpayer for other tax matters);
- the time bar that limits Inland Revenue's ability to adjust a taxpayer's transfer pricing position is increased from 4 to 7 years (in line with Australia);
- in addition to applying to transactions between related parties, the transfer pricing rules will also apply when non-resident investors “act in concert” to effectively control a New Zealand entity, such as through a private equity manager;
- the new legislation codifies the requirement for large multinationals to provide Inland Revenue with the information required to comply with the OECD's Country-by-Country reporting initiative.

### **Administrative measures for investigating large multinational groups**

It can be difficult and resource intensive for Inland Revenue to assess and engage in disputes with multinationals in practice. This is partly due to the difficulties Inland Revenue faces in obtaining the relevant information.

To address these issues, the Bill proposes strengthening Inland Revenue's powers to investigate large multinationals (with at least EUR €750m of global revenues) that do

not cooperate with a tax investigation. This involves amending the Tax Administration Act 1994 to allow Inland Revenue to:

- collect any tax owed by a member of a large multinational group from any wholly-owned group member, provided the non-resident fails to pay the tax itself;
- use section 17 of the Tax Administration Act 1994 to request information that is held offshore by another group member of the large multinational group;
- more readily assess a large multinational group's tax position based on the information available to Inland Revenue in cases where the group has failed to adequately respond to an information request. A failure to provide the requested information to Inland Revenue can also prevent the information from being subsequently admitted as evidence in court proceedings. These proposals are based on an existing provision in section 21 of the Tax Administration Act 1994 which currently applies to deductible payments; and
- impose a new civil penalty of up to \$100,000 for large multinational groups which fail to provide requested information (which replaces the current \$12,000 maximum criminal penalty).

### **Hybrid and branch mismatches**

Hybrid and branch mismatches are cross-border arrangements that exploit differences in the tax treatment of an entity, branch, or instrument under the laws of 2 or more countries to create a tax advantage.

There are a number of ways this can be achieved, including:

- through a payment being deductible for a payer in 1 country but not included as taxable income for the payee in the other country;
- a single payment being able to be deducted against different income streams in 2 countries;
- other arrangements that result in double non-taxation outcomes through the use of hybrid instruments, entities, or branches.

The OECD has made a number of recommendations as to how countries can improve their domestic rules to prevent mismatches arising and neutralise their effect when they do arise. These recommendations relate to Action 2 of the OECD/G20 BEPS Action Plan: Neutralising the Effects of Hybrid Mismatch Arrangements.

To address hybrid mismatch BEPS strategies the Bill proposes law changes that represent a comprehensive adoption of the OECD recommendations on hybrid and branch mismatch arrangements with suitable modifications for the New Zealand context. Some examples of these modifications are to ensure that New Zealand companies with simple foreign branch structures are not caught by the rules, or that the rules do not apply to purely domestic firms, and not introducing rules when an adequate New Zealand provision already exists.

The OECD recommends 2 kinds of rules. The first are rules specifically designed to reduce the likelihood of hybrid mismatches arising. The second are “linking rules”, which apply to payments that give rise to a deduction in more than 1 country, or which give rise to a deduction in 1 country but are not taxed as income in another country due to a hybrid or branch mismatch. These generally only apply to:

- arrangements between related parties (25% or more commonly owned) or control groups (50% or more commonly owned); or
- structured arrangements—generally, arrangements between non-associated parties which intentionally exploit such mismatches.

The linking rules operate on the basis of “primary” and “secondary” taxing rights to reflect their cross-border nature. This means that 1 country is allocated the primary right to counter the tax benefits of the arrangement. If the country with this primary right does not have hybrid and branch mismatch rules, then the other country involved has a secondary right to counter the tax benefits. As a result, the relevant rules contained in this Bill have separate provisions to cover situations when New Zealand has the primary right and when it has the secondary right. This is necessary to ensure that all hybrids with a New Zealand resident party are within the scope of the rules.

A further issue concerns cross-border hybrid financial instruments that are treated as debt in New Zealand but equity in an overseas jurisdiction. To address this, the Bill proposes a new hybrid mismatch rule which allows New Zealand to charge non-resident withholding tax on payments under such instruments if New Zealand allows an interest deduction for the payment. This rule would override our double tax agreements and would apply retrospectively, but contains a “savings” provision for taxpayers that have adopted a contrary position prior to the introduction of the Bill.

### **Departmental disclosure statement**

The Inland Revenue Department is required to prepare a disclosure statement to assist with the scrutiny of this Bill. The disclosure statement provides access to information about the policy development of the Bill and identifies any significant or unusual legislative features of the Bill.

A copy of the statement can be found at <http://legislation.govt.nz/disclosure.aspx?type=bill&subtype=government&year=2017&no=3>

### **Regulatory impact statement**

The Inland Revenue Department produced 4 regulatory impact statements to help inform the main policy decisions taken by the Government relating to the contents of this Bill.

Copies of these regulatory impact statements can be found at—

- <http://taxpolicy.ird.govt.nz/publications/type/ris>
- <http://www.treasury.govt.nz/publications/informationreleases/ris>

### Clause by clause analysis

*Clause 1* gives the title.

*Clause 2* gives the dates on which the clauses come into force. Under *subclause (1)*, most come into force on 1 July 2018. Under *subclause (2)*, a pair of provisions come into force retrospectively on 1 April 2008. Under *subclause (3)*, another pair of provisions come into force retrospectively on 1 January 2016. Under *subclause (4)*, several provisions come into force on the day on which the Act receives the Royal assent.

## Part 1

### Amendments to Income Tax Act 2007

*Clause 3* provides that *Part 1* amends the Income Tax Act 2007

*Clause 4* amends section BH 1, which relates to double tax agreements, by amending subsection (4) to exclude *new sections GB 54 and RF 11C* from the effect of a double tax agreement. The exclusion of *section RF 11C* is made retrospectively.

*Clause 5* inserts *new section CH 10B*, recognising income arising under *section FE 7B* when a participant in a public project is required to apportion interest expenditure arising from public project debt.

*Clause 6* inserts a *new heading and section CH 12*, recognising income arising under *new subpart FH*, which matches deductions and income from multi-jurisdictional arrangements.

*Clause 7* inserts a *new heading and section CX 64*, recognising excluded income arising under *new subpart FH*, which matches deductions and income from multi-jurisdictional arrangements.

*Clause 8* inserts a *new heading and section DB 57B*, recognising deductions arising, and the denial of deductions for amounts, under *new subpart FH*, which matches deductions and income from multi-jurisdictional arrangements.

*Clause 9* amends section DR 3 to deny a deduction for a life reinsurance premium paid to a non-resident life reinsurer if the premium is not taxed as income of the life reinsurer.

*Clause 10* amends section EX 20D, to insert references to non-debt liabilities in calculations, reflecting the amendments to section FE 12.

*Clause 11* amends section EX 20E, to insert references to non-debt liabilities in calculations, reflecting the amendments to section FE 12.

*Clause 12* amends section EX 44 to include a reference to *new section EX 47B*, which limits the calculation methods for calculating FIF income or loss from a returning share transfer under a structured arrangement.

*Clause 13* amends section EX 46 to limit the options available for calculating FIF income or loss from a returning share transfer under a structured arrangement.

*Clause 14* inserts *new section EX 47B*, which requires the use of a particular calculation method for calculating FIF income or loss from a returning share transfer under a structured arrangement in some circumstances.

*Clause 15* amends section EX 52 by inserting *new subsection (14C)*, which introduces an exception to a calculation method for calculating FIF income or loss from a returning share transfer if it is part of a structured arrangement.

*Clause 16* amends section EX 53 by inserting *new subsection (16C)*, which introduces an exception to a calculation method for calculating FIF income or loss from a returning share transfer if it is part of a structured arrangement.

*Clause 17* inserts *new section FE 4B*, defining *public project asset*, *public project debt*, and *public project participant debt*, which are defined terms used in *new section FE 7B*.

*Clause 18* amends section FE 5, which sets, for excess debt entities, the thresholds used by the thin capitalisation rules in the apportionment of interest. *Subclauses (1) and (2)* amend subsection (1), and *subclause (6)* inserts *new subsection (6)*, to provide for new rules applying to an excess debt entity controlled by a group of non-residents or a group of non-residents acting in concert. *Subclauses (3) to (5)* make amendments consequential on the amendments to section FE 12, changing the way in which debt percentages are calculated to include non-debt liabilities.

*Clause 19* amends section FE 6, which provides for the apportionment required by section FE 5 for interest expenditure of excess debt entities. *Subclause (1)* amends the formula in subsection (2) by inserting a new item providing for the denial of interest amounts under *subpart FH*. *Subclause (2)* amends section FE 6(3)(a) to exclude from that item in the formula the effect of *subpart FH*. *Subclause (3)* inserts *new section FE 6(3)(aba)*, which defines the item inserted by *subclause (1)*. *Subclause (4)* amends section FE 6(3)(ac), as it relates to a concession increasing the amount of deductions available after apportionment of interest. *Subclauses (5) and (6)* amend section FE 6(3)(e) by providing for the apportionment of interest expenditure by an excess debt entity owned by a non-resident owning body or a group of non-residents acting in concert. *Subclause (7)* provides for the period of application of the amendments in *subclauses (1) to (4)*. *Subclause (8)* provides for the period of application of *subclauses (5) and (6)* and refers to *section FZ 8*, which provides for a transition period before some excess debt entities are fully affected by the amendments.

*Clause 20* inserts *new section FE 7B*, which applies the thin capitalisation rules separately to the debt and assets that are associated with a public project for a participant in the public project. The public project is treated as if it were the sole business of the participant and the public project debt and public project assets were the participant's sole debt and assets. The treatment of the interest expenditure on public project debt depends on whether the public project debt is provided by other participants in the public project and whether the public project debt is secured solely against public project assets.

*Clause 21* amends section FE 8 to insert references to non-debt liabilities, consequential on the amendments to section FE 12.

*Clause 22* amends section FE 10 to insert references to non-debt liabilities, consequential on the amendments to section FE 12.

*Clause 23* replaces section FE 11 to provide for the effect of *new section GB 51B* by excluding from calculations under the interest apportionment rules the fluctuations to which that section applies.

*Clause 24* amends the formula in section FE 12 for calculating the debt percentage of a group. Under the amended formula, the value of the group's non-debt liabilities is subtracted from the group's assets.

*Clause 25* amends section FE 14 to insert references to non-debt liabilities, consequential on the amendments to section FE 12.

*Clause 26* amends section FE 15 to exclude, from the definition of total group debt, financial arrangements for which deductions are denied under *new section FH 3, FH 7, or FH 11*.

*Clause 27* amends section FE 16 to provide for the valuation of assets for the purposes of the interest apportionment rules.

*Clause 28* inserts *new section FE 16B*, which defines *total group non-debt liabilities* for the purpose of the amendments to section FE 12.

*Clause 29* amends section FE 18, which provides for the measurement of the debts and assets of a worldwide group. *Subclauses (1) and (2)* insert references to non-debt liabilities, consequential on the amendments to section FE 12. *Subclause (3)* extends the description of debts that are not included in the total group debts to include debt from an owner who has made significant settlements on a trustee that is a member of the group.

*Clause 30* inserts *new subpart FH*, which provides for the matching of deductions and income arising from arrangements between parties in more than 1 jurisdiction having different taxation law. The subpart contains *new sections FH 1 to FH 15*. A brief description of the background and general scheme and effect of the sections is given by *section FH 1*.

*Clause 31* inserts *new heading and section FZ 8*, which gives the rules relating to a transition period for excess debt entities owned by a non-resident owning body, or a group of non-residents acting in concert, and affected by some of the amendments to sections FE 5 and FE 6.

*Clause 32* amends section GB 2 by amending a heading in a cross-reference.

*Clause 33* inserts *new section GB 51B*, which provides for calculations under the interest apportionment rules to ignore fluctuations in value caused by an action or omission or arrangement with a purpose or effect of defeating the intent and application of the rules.

*Clause 34* inserts *new heading and section GB 54*, which treats a non-resident that is a large multinational group or is a member of a large multinational group, under the

new definition, as having a permanent establishment in New Zealand if the non-resident makes a supply of goods and services in New Zealand with the help of a facilitator in New Zealand.

*Clause 35* amends section GC 6, which provides for the purpose and effect of the transfer pricing rules. *Subclauses (2) and (5)* insert in subsections (1) and (2) references to *control group*, rather than association, as the test for the application of the transfer pricing rules to the parties to an arrangement. *Subclause (3)* inserts *new subsection (1B)*, which provides that the transfer pricing rules apply consistently with the OECD transfer pricing guidelines. *Subclause (4)* inserts *new subsection (1C)*, which provides for the effect of *new sections GC 15 to GC 18* to be taken into account in the application of the transfer pricing rules in sections GC 7 to GC 14.

*Clause 36* amends section GC 13, which provides for the calculation of arm's length amounts for a transfer pricing arrangement. *Subclause (1)* replaces *subsection (1)*, which specifies the approach to calculating an arm's length amount. *Subclause (2)* updates the list of methods that may be used for the calculation. *Subclause (3)* replaces *subsections (4) and (5)*, which specify how arm's-length conditions for a transfer pricing arrangement are determined as part of determining an arm's length amount. *Subclause (4)* inserts *new subsection (6)* which provides that the time limit for a reassessment under the transfer pricing rules is 7 tax years after the tax year in which a return of income is made for the assessed income year.

*Clause 37* inserts *new heading and sections GC 15 to GC 18*, which relate to the treatment of loans under the transfer pricing rules. The new sections provide for adjustments to the credit rating of the borrower and the disregarding of features of the loan that would increase the interest rate paid by a borrower under an equivalent loan from an independent lender. *Section GC 15* provides that the adjustments to credit ratings under *sections GC 16 and GC 17*, and the disregarding of loan features under *section GC 18*, are to be made before the other transfer pricing rules are applied. The section also gives the meaning of 3 terms used in the sections, which are *insuring or lending person*, which relates to a person having loans that are affected by regulatory requirements, *cross-border related loan*, and *indirect associated funding arrangement*.

*Clause 38* inserts *new section HD 30*, which provides that a member of a wholly-owned large multinational group is an agent of another member of the wholly-owned large multinational group for tax obligations.

*Clause 39* amends section IA 2 to provide for the treatment of mismatch amounts that arise under *new section FH 8* and are later treated as ordinary losses under *new section FH 12(8)*.

*Clause 40* amends section LE 1, to introduce an exception to the availability of a tax credit for an imputation credit from a share affected by a returning share transfer. The exception applies if the parties to the returning share transfer are related or the returning share transfer is a structured arrangement.

*Clause 41* amends section RF 2C by introducing an item in the formula in subsection (4) that removes from the calculation amounts that are denied as deductions under new sections FH 3, FH 7, and FH 11.

*Clause 42* inserts new section RF 11C, which provides that a payment by a non-resident company to another non-resident company of non-resident passive income that consists of interest is treated by the NRWT rules as consisting of interest, even if a double tax agreement would otherwise require the payment to be treated as a dividend. The amendment resolves an issue regarding the effect of tax treaty provisions on New Zealand's right to impose withholding tax on such instruments. It comes into force on 1 April 2008. *Subclause (2)* provides for an exception if a person has taken a tax position, for a payment, that is inconsistent with the amendment.

*Clause 43* amends section YA 1, which contains definitions. *Subclause (2)* inserts a new definition of *act together*. *Subclause (3)* amends the definition of *arm's length amount* by correcting a heading in a cross-reference. *Subclause (4)* inserts a new definition of *branch mismatch report*, by reference to section FH 15. *Subclause (5)* inserts a new definition of *control group*, by reference to section FH 15. *Subclause (6)* inserts a new definition of *country-by-country report* by reference to section 78G of the Tax Administration Act 1994, which requires a large multinational group to make such a report. *Subclause (7)* amends the definition of *deductible foreign equity distribution* to allow for the effect of hybrid mismatch legislation. *Subclause (8)* inserts a new definition of *financial instrument*, by reference to section FH 15. *Subclause (9)* amends the definition of *goods* by inserting cross-references to sections GB 54 and YD 4B. *Subclause (10)* inserts a new definition of *hybrid mismatch legislation*, by reference to section FH 15. *Subclause (11)* inserts a new definition of *hybrid mismatch report*, by reference to section FH 15. *Subclause (12)* inserts a new definition of *large multinational group*, as a consequence of the obligation to provide information imposed by new section 78G of the Tax Administration Act 1994. *Subclause (13)* amends the definition of *life reinsurer* by correcting a cross-reference. *Subclause (14)* inserts a new definition of *mismatch amount*, by reference to section FH 15. *Subclause (15)* inserts a new definition of *mismatch situation*, by reference to section FH 15. *Subclause (16)* inserts a new definition of *OECD transfer pricing guidelines*. *Subclause (17)* inserts a new definition of *permanent establishment* by reference to section YD 4B. *Subclause (18)* inserts new definitions of *public project asset*, *public project debt*, and *public project participant debt*, by reference to section FE 4B. *Subclause (19)* inserts a new definition of *related*, by reference to section FH 15. *Subclause (20)* amends the definition of *related-party debt* so that the definition applies generally. *Subclause (21)* amends the definition of *returning share transfer* to remove a requirement that the share be listed. *Subclause (22)* amends the definition of *services* to include new cross-references. *Subclause (23)* inserts a new definition of *structured arrangement*, by reference to section FH 15. *Subclause (24)* inserts a new definition of *surplus assessable income*, by reference to section FH 15. *Subclause (25)* inserts a new definition of *total group non-debt liabilities* by reference to new section FE 16B. *Subclause (26)* amends the definition of *transfer pricing arrange-*

ment by correcting a heading in a cross-reference. *Subclause (27)* inserts a new definition of *wholly-owned large multinational group*.

*Clause 44* amends section YD 4, which gives classes of income having a New Zealand source, by inserting *new subsection (17C)*, which relates to income from a permanent establishment in New Zealand, and *new subsection (17D)*, which relates to income taxable by New Zealand under a double tax agreement.

*Clause 45* inserts *new section YD 4B*, which defines a *permanent establishment* in New Zealand by reference to the definition of the term in an applicable double tax agreement, or by reference to *new schedule 23* if there is no applicable double tax agreement.

*Clause 46* inserts *new section YD 5(1BA)*, which excludes from the section business activities carried on through a permanent establishment, as a consequence of the insertion of *new section YD 5B*.

*Clause 47* inserts *new section YD 5B*, which provides for the apportionment of income from business activities carried on through a permanent establishment in New Zealand.

*Clause 48* inserts *new schedule 23*, containing the definition of a permanent establishment for a resident of a jurisdiction with which New Zealand does not have an applicable double tax agreement.

## Part 2

### Amendments to Tax Administration Act 1994

*Clause 49* provides that *Part 2* amends the Tax Administration Act 1994

*Clause 50* amends section 17 by inserting *new subsection (1CB)*, which provides when information is in the knowledge, possession, or control of a member of a large multinational group for the purposes of sections 139AB, 143, and 143A.

*Clause 51* inserts *new section 21BA*, which limits the availability, as evidence in proceedings, of information that is not provided by a member of a large multinational group when required by the Commissioner. The Commissioner must notify a member of the consequences of not providing the information and that the Commissioner may exercise her powers relying on the information already held by the Commissioner.

*Clause 52* inserts *new section 78G*, which requires a large multinational group with an ultimate parent in New Zealand to provide a country-by-country report to the Commissioner.

*Clause 53* inserts *new section 139AB*, which provides for a civil penalty of an amount determined by the Commissioner if a member of a large multinational group fails to provide information within the knowledge, information, or control of the member under *new section 17(1CB)*.

*Clause 54* amends section 143 to provide a member of a large multinational group with a defence against a charge under that section of failing to provide information

that is presumed by *new section 17(ICB)* to be within the knowledge, information, or control of the member.

*Clause 55* amends section 143A to provide a member of a large multinational group with a defence against a charge of an offence under that section of failing to provide information that is presumed by *new section 17(ICB)* to be within the knowledge, information, or control of the member.

*The schedule* contains *new schedule 23*, which is inserted by *clause 48* and gives the meaning of *permanent establishment* applicable when no double tax agreement applies.



*Hon Stuart Nash*

# **Taxation (Neutralising Base Erosion and Profit Shifting) Bill**

Government Bill

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The Parliament of New Zealand enacts as follows:

- 1 Title**
- This Act is the Taxation (Neutralising Base Erosion and Profit Shifting) Act **2017**.
- 2 Commencement** 5
- (1) This Act comes into force on 1 July 2018, except as provided in this section.
- (2) **Sections 4(1) and 42** come into force on 1 April 2008.
- (3) **Sections 43(6) and 52** come into force on 1 January 2016.
- (4) **Sections 38, 43(12), 50, 51, 53, 54, and 55** come into force on the day on which this Act receives the Royal assent. 10

**Part 1**

**Amendments to Income Tax Act 2007**

- 3 Income Tax Act 2007**
- This Part amends the Income Tax Act 2007.
- 4 Section BH 1 amended (Double tax agreements)** 15
- (1) In section BH 1(4), words before paragraph (a), replace “subsection (5)” with “subsection (5), or **section RF 11C** (Interest paid by non-resident companies to non-residents)”.
- (2) In section BH 1(4), words before paragraph (a), replace “section BG 1 (Tax avoidance),” with “section BG 1 or **GB 54** (which relate to tax avoidance) or”. 20
- (3) **Subsection (1)** applies for a person for the 2008–09 and later income years except for a payment of non-resident passive income made before the date of introduction of the Taxation (Neutralising Base Erosion and Profit Shifting) Bill, for which the person has adopted a tax position that is inconsistent with the amendment made by **subsection (1)**. 25
- 5 New section CH 10B inserted (Interest apportionment: public project debt)**
- (1) After section CH 10, insert:

**CH 10B Interest apportionment: public project debt**

*When this section applies*

- (1) This section applies when an excess debt entity is required under **section FE 7B** (Interest on public project debt for certain excess debt entities) to apportion its interest expenditure arising from public project debt. 5

*Income*

- (2) The amount calculated under **section FE 7B(3)** is income of the excess debt entity for the income year.

Defined in this Act: amount, excess debt entity, income, income year, interest, public project debt

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018. 10

**6 New heading and section CH 12 inserted**

- (1) After section CH 11, insert:

*Financial instruments and hybrid mismatches*

**CH 12 Income from hybrid mismatch arrangement**

An amount is assessable income if it is treated as assessable income under **subpart FH** (Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements). 15

Defined in this Act: amount, assessable income

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**7 New heading and section CX 64 inserted** 20

- (1) After section CX 63, insert:

*Financial instruments and hybrid mismatches*

**CX 64 Income from financial instrument**

An amount is excluded income if it is treated as excluded income under **subpart FH** (Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements). 25

Defined in this Act: amount, excluded income

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**8 New heading and section DB 57B inserted**

- (1) After section DB 57, insert: 30

*Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements*

**DB 57B Matching of deductions and income from multi-jurisdictional arrangements**

*Deduction denied*

5

- (1) An amount is not a deduction of a person if the deduction is denied under **subpart FH** (Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements).

*Deduction*

- (2) An amount treated as a deduction of a person under **subpart FH** is a deduction of the person. 10

*Link with subpart DA*

- (3) **Subsection (1)** overrides, and **subsection (2)** supplements, the general permission. The general limitations still apply.

Defined in this Act: amount, deduction, general limitation, general permission

15

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**9 Section DR 3 amended (Life reinsurance outside New Zealand)**

- (1) In section DR 3, replace the subsection heading with “*No deduction for premiums under certain policies*”.

- (2) In section DR 3, as subsection (2), insert: 20

*No deduction for premiums paid to certain life reinsurers*

- (2) A life insurer is denied a deduction for a life reinsurance premium paid to a life reinsurer who is resident in a country or territory outside New Zealand if the life reinsurance premium is—

- (a) not assessable income of the life reinsurer: 25  
(b) excluded from taxation by New Zealand under a double tax agreement between New Zealand and the country or territory.

- (3) In section DR 3, list of defined terms, insert “assessable income”, “double tax agreement”, “life reinsurer”, and “pay”.

- (4) **Subsection (2)** applies for income years beginning on or after 1 July 2018. 30

**10 Section EX 20D amended (Adjustment of cost fraction for excessively debt funded CFC)**

- (1) In section EX 20D(4), formula, after “assets”, insert “— total CFC’s non-debt liabilities”.

- (2) In section EX 20D (5), replace “subsections (6) to (8)” with “subsections (6) to **(8B)**”. 35

- (3) After section EX 20D(8), insert:

|           |  |    |
|-----------|--|----|
|           | <i>Total CFC's non-debt liabilities</i>  |    |
| (8B)      | <b>Total CFC's non-debt liabilities</b> is the total value of the CFC's non-debt liabilities determined under generally accepted accounting practice.  |    |
| (4)       | In section EX 20D, list of defined terms, insert "generally accepted accounting practice".   | 5  |
| <b>11</b> | <b>Section EX 20E amended (Relative debt-asset ratio for CFC)</b>  |    |
| (1)       | In section EX 20E(3), formula, replace "total group assets" with "(total group assets – total group non-debt liabilities)".  |    |
| (2)       | In section EX 20E (4), replace "subsections (5) and (6)" with "subsections (5), (6), and <b>(6B)</b> ".  | 10 |
| (3)       | After section EX 20E(6), insert:   |    |
|           | <i>Total group non-debt liabilities</i>  |    |
| (6B)      | <b>Total group non-debt liabilities</b> is the total value of the group's non-debt liabilities determined under generally accepted accounting practice.  |    |
| (4)       | In section EX 20E, list of defined terms, insert "generally accepted accounting practice".   | 15 |
| <b>12</b> | <b>Section EX 44 amended (Five calculation methods)</b>  |    |
| (1)       | In section EX 44(2), after "EX 47," insert " <b>EX 47B</b> ,".   |    |
| (2)       | <b>Subsection (1)</b> applies for income years beginning on or after 1 July 2018.  |    |
| <b>13</b> | <b>Section EX 46 amended (Limits on choice of calculation methods)</b>   | 20 |
| (1)       | After section EX 46(6)(d), insert:   |    |
|           | (e) the person is the share user of the share under a returning share transfer to which <b>section EX 47B</b> applies.   |    |
| (2)       | After section EX 46(10)(d), insert:  |    |
|           | (db) an interest in a non-resident if—   | 25 |
|           | (i) the non-resident is related to the person holding the interest, or the interest is or is part of a structured arrangement; and   |    |
|           | (ii) the non-resident is not a foreign PIE equivalent; and   |    |
|           | (iii) the non-resident is allowed a deduction against income or an equivalent tax relief, under the taxation law of a country or territory, for the payment of a dividend arising from the interest: | 30 |
| (3)       | In section EX 46, list of defined terms, insert "dividend", "non-resident", "pay", "returning share transfer", "share supplier", and "structured arrangement".                                       |    |
| (4)       | <b>Subsections (1) and (2)</b> apply for income years beginning on or after 1 July 2018.   | 35 |

**14 New section EX 47B inserted (Method required for shares subject to certain returning share transfers)**

(1) After section EX 47, insert:

**EX 47B Method required for shares subject to certain returning share transfers**

A person must use the comparative value method to calculate FIF income or FIF loss for an income year from an attributing interest that is a share subject to a returning share transfer if— 5

- (a) the person is the share user; and
- (b) the share supplier is resident in a country or territory outside New Zealand (the **foreign jurisdiction**); and 10
- (c) the person is related to the share supplier or the returning share transfer is or is part of a structured arrangement; and
- (d) the taxation law of the foreign jurisdiction treats the share supplier as owning the shares subject to the returning share transfer. 15

Defined in this Act: attributing interest, comparative value method, FIF income, FIF loss, income year, New Zealand, related, returning share transfer, share, share supplier, share user, structured arrangement 15

(2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**15 Section EX 52 amended (Fair dividend rate annual method)**

(1) Replace section EX 52(14C), other than the heading, with: 20

(14C) For a person using the fair dividend rate annual method to calculate FIF income for an attributing interest in a FIF that is an original share subject to a returning share transfer, the attributing interest is treated as being held by the share supplier, except if—

- (a) the share user is related to the share supplier: 25
- (b) the returning share transfer is or is part of a structured arrangement.

(2) In section EX 52, list of defined terms, insert “related” and “structured arrangement”.

(3) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**16 Section EX 53 amended (Fair dividend rate periodic method)** 30

(1) Replace section EX 53(16C), other than the heading, with:

(16C) For a person using the fair dividend rate annual method to calculate FIF income for an attributing interest in a FIF that is an original share subject to a returning share transfer, the attributing interest is treated as being held by the share supplier, except if— 35

- (a) the share user is related to the share supplier:
- (b) the returning share transfer is or is part of a structured arrangement.

- (2) In section EX 53, list of defined terms, insert “fair dividend rate annual method”, “related”, “share user”, and “structured arrangement”.
- (3) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**17 New section FE 4B inserted (Meaning of public project asset, public project debt, and public project participant debt) 5**

- (1) After section FE 4, insert:

**FE 4B Meaning of public project asset, public project debt, and public project participant debt**

*Meaning of public project asset*

- (1) **Public project asset** means an interest in an asset in New Zealand— 10
  - (a) arising from a project performed under a contract—
    - (i) with the Sovereign in right of New Zealand or a public authority; and
    - (ii) for which borrowing by the Crown or public authority is approved by the Minister of Finance under the Public Finance Act 1989 or the Crown Entities Act 2004; and 15
    - (iii) for a period of 10 years or more; and
    - (iv) requiring the persons performing the project to provide, upgrade, or create assets in New Zealand and to operate or maintain the assets in New Zealand; and 20
    - (v) requiring that, after completion of the contract, the assets be owned by the Sovereign in right of New Zealand or the public authority; and
  - (b) that each person performing the contract is not permitted under the terms of the contract to dispose of within 10 years from the beginning of the project, except to a public authority, as provided by the contract, or to another person performing the project; and 25
  - (c) the income from which has a source in New Zealand for each person performing the contract.

*Meaning of public project debt* 30

- (2) **Public project debt**, for an excess debt entity and a project, means a total amount of debt, each part of which is for a loan to the excess debt entity, or for the excess debt entity’s proportion of a loan made to the persons performing the project, and—
  - (a) is applied to the project to give rise to public project assets; and 35
  - (b) is secured against a public project asset arising from the project or income derived from such a public project asset; and

- (c) is not a source of funds, exceeding a minor or incidental amount, that the excess debt entity lends to a person who is not an associated person performing the project; and
- (d) gives rise to interest expenditure that the excess debt entity incurs in New Zealand.

5

*Meaning of public project participation debt*

- (3) **Public project participant debt**, for an excess debt entity and a project, means an amount of public project debt corresponding to the excess debt entity's proportion, as 1 of the persons performing the project (the **project participants**), of a loan—

10

- (a) made by a creditor who is a project participant, or a person associated with a project participant; and
- (b) that would meet the requirements of paragraph (a) of the definition of a non-resident owning body for a company (the **performance subsidiary**) if—

15

- (i) the performance subsidiary were treated as holding the public project assets and performing all the activities required for the performance of the project; and
- (ii) the project participants were treated as being non-resident owners of the performance subsidiary having ownership interests that are in the same proportion as their interests in the project; and
- (iii) the creditor made the loan to the performance subsidiary under an arrangement corresponding to the arrangement for the loan to the project participants.

20

Defined in this Act: amount, associated person, company, dispose, excess debt entity, income, interest, loan, New Zealand, non-resident, non-resident owning body, ownership interest, public authority, public project asset, public project debt, public project participant debt, source in New Zealand

25

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**18 Section FE 5 amended (Thresholds for application of interest apportionment rules)**

30

- (1) In section FE 5(1)(a), replace the words before subparagraph (i) with “the excess debt entity is none of an excess debt outbound company, a company that is described in section FE 2(1)(cb), an excess debt entity that is controlled by a group of persons meeting the requirements of **subsection (6)**, and a trustee who is described in section FE 2(1)(g), and—”.

35

- (2) After section FE 5(1)(a), insert:

- (ab) the excess debt entity is a company described in section FE 2(1)(cb), or is an excess debt entity controlled by a group of persons meeting the requirements of **subsection (6)**, and—

- (i) the debt percentage of its New Zealand group for the income year is more than 60%; and
- (ii) the debt percentage of its New Zealand group for the income year is more than 100% of the debt percentage of the worldwide group; or
- (3) Replace section FE 5(1B)(a) with:
- (a) a ratio of 90% or greater is obtained by dividing the amount for its New Zealand group of the total group assets measured under section FE 16 and reduced by the total group non-debt liabilities, measured under **section FE 16B**, by the amount for its worldwide group of the total group assets measured under section FE 18 and reduced by the total group non-debt liabilities, measured under section FE 18:
- (4) In section FE 5(1BB)(d), replace “goodwill” with “goodwill and reduced by total group non-debt liabilities”.
- (5) In section FE 5(1C), words before paragraph (a), replace “assets” with “assets and total group non-debt liabilities”.
- (6) After section FE 5(5), insert:
- Group acting in concert*
- (6) A group of persons meets the requirements of this subsection if the members of the group act in concert and each is described in section FE 2(1)(a) to (db).
- (7) In section FE 5, list of defined terms, insert “total group non-debt liabilities”.
- (8) **Subsections (1), (2), and (6)** apply for income years beginning on or after 1 July 2018, except as provided in **section FZ 8** (Transition period for amendments to interest apportionment rules).
- 19 Section FE 6 amended (Apportionment of interest by excess debt entity)**
- (1) In section FE 6(2), formula, after “total deduction” insert “– mismatch”.
- (2) In section FE 6(3)(a), words before subparagraph (i), replace “allowed under” with “that would be allowed, in the absence of **subpart FH** (Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements), under”.
- (3) After section FE 6(3)(a), insert:
- (aba) **mismatch** is the total of amounts denied as deductions in the income year under **section FH 3** (Payments under financial instruments producing deduction without income) as unrecognised amounts under **section FH 3(2)** and under **sections FH 7 and FH 11** (which provide for the matching of deductions and income from multi-jurisdictional arrangements):
- (4) Replace section FE 6(3)(ac)(i), with:

|           |  |    |
|-----------|--|----|
| (i)       | zero, if the excess debt entity is not a natural person or trustee described in section FE 2(1)(g) and not a party to a financial arrangement that is removed under section FE 18(3B) from the measurement of total group debt for the excess debt entity; or  |    |
| (5)       | Replace section FE 6(3)(e)(i) with:  | 5  |
| (i)       | if the excess debt entity is none of an excess debt outbound company, a company that is described in section FE 2(1)(cb), a company that is controlled by a group of persons meeting the requirements of <b>section FE 5(6)</b> , and a trustee who is described in section FE 2(1)(g), the greater of 60% and 110% of the debt percentage of their worldwide group: | 10 |
| (6)       | After section FE 6(3)(e)(iii), insert:   |    |
| (iiib)    | if the excess debt entity is a company that is described in section FE 2(1)(cb) or is controlled by a group of persons meeting the requirements of <b>section FE 5(6)</b> , the greater of 60% and 100% of the debt percentage of their worldwide group:   | 15 |
| (7)       | <b>Subsections (1) to (4)</b> apply for income years beginning on or after 1 July 2018.  |    |
| (8)       | <b>Subsections (5) and (6)</b> apply for income years beginning on or after 1 July 2018, except as provided in <b>section FZ 8</b> (Transition period for amendments to interest apportionment rules).   | 20 |
| <b>20</b> | <b>New section FE 7B inserted (Interest on public project debt for certain excess debt entities)</b>   |    |
| (1)       | After section FE 7, insert:  |    |
|           | <b>FE 7B Interest on public project debt for certain excess debt entities</b>  | 25 |
|           | <i>Who this section applies to</i>   |    |
| (1)       | This section applies to an excess debt entity that—  |    |
| (a)       | is a person meeting the requirements of section FE 2(1)(b), (c), (e), or (f); and  |    |
| (b)       | has an amount of public project debt for a project.  | 30 |
|           | <i>Debt percentages for public project debt</i>  |    |
| (2)       | Debt percentages relating to the excess debt entity and the public project debt are determined under this subpart as if—   |    |
| (a)       | the excess debt entity has no debt other than the public project debt for the project and no assets other than the public project assets for the project and assets used in performing the project; and  | 35 |
| (b)       | the value of the interest of the excess debt entity in the public project assets is the value of the public project assets multiplied by the fraction  |    |

|   |    |
|---|----|
| that is the proportion held by the excess debt entity of the interest in the whole project; and   |    |
| (c) the New Zealand group of the excess debt entity is the excess debt entity.  |    |
| <i>Income</i>   |    |
| (3) If the debt percentage of the excess debt entity's New Zealand group exceeds the threshold debt percentage given by section FE 5(1), the excess debt entity is treated as deriving an amount of income under <b>section CH 10B</b> (Interest apportionment: public project debt) that is calculated, treating the value of a fraction with a zero denominator as being zero, using the formula— | 5  |
| $(\text{limit interest} \times \text{limit excess} \div \text{limit debt}) + (\text{rec interest} \times \text{rec excess} \div \text{rec debt}) + (\text{partic interest} \times \text{partic excess} \div \text{partic debt})$ .  | 10 |
| <i>Definition of items in formula</i>   |    |
| (4) In the formula,—  |    |
| (a) <b>limit interest</b> is the amount of interest expenditure incurred by the excess debt entity from the amount of public project debt (the <b>limited recourse debt</b> ) that is not public project participant debt and for which the creditor has security for repayment that is limited to—   | 15 |
| (i) interests of the excess debt entity in the public project assets from the project; and  |    |
| (ii) income that the excess debt entity derives from the public project assets:   | 20 |
| (b) <b>limit excess</b> is—   |    |
| (i) zero, if the amount of limited recourse debt does not exceed the value (the <b>asset portion value</b> ), of the excess debt entity's interest in the public project assets, used in calculating the debt percentage for the excess debt entity's New Zealand group for the income year:  | 25 |
| (ii) the amount by which the limited recourse debt exceeds the asset portion value, if <b>subparagraph (i)</b> does not apply:  |    |
| (c) <b>limit debt</b> is the amount of the limited recourse debt:   | 30 |
| (d) <b>rec interest</b> is the amount of interest expenditure incurred by the excess debt entity from the amount of public project debt referred to in the item recourse debt:  |    |
| (e) <b>rec excess</b> is—   |    |
| (i) zero, if the amount of public project debt that is not public project participant debt does not exceed the amount (the <b>threshold debt amount</b> ) obtained by multiplying the value of the public project assets by the threshold debt percentage given by section FE 5(1) for the excess debt entity's New Zealand group:  | 35 |

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|--|----------|
| <ul style="list-style-type: none"> <li>(ii) the amount of the item recourse debt, if the amount of limited recourse debt equals or exceeds the threshold debt amount:</li> <li>(iii) the amount by which the amount of public project debt that is not public project participant debt exceeds the threshold debt amount, if <b>subparagraphs (i) and (ii)</b> do not apply:</li> </ul>  | 5        |
| <ul style="list-style-type: none"> <li>(f) <b>rec debt</b> is the amount of public project debt for which the creditor has security for repayment that is not limited to the public project assets of the excess debt entity and the income that the excess debt entity derives from the public project assets:</li> </ul>   |          |
| <ul style="list-style-type: none"> <li>(g) <b>partic interest</b> is the amount of interest expenditure incurred by the excess debt entity from public project participant debt:</li> </ul>  | 10       |
| <ul style="list-style-type: none"> <li>(h) <b>partic excess</b> is— <ul style="list-style-type: none"> <li>(i) zero, if the amount of public project debt does not exceed the threshold debt amount:</li> <li>(ii) the amount of public project participant debt, if the amount of public project debt that is not public project participant debt equals or exceeds the threshold debt amount:</li> <li>(iii) the amount by which the amount of public project debt exceeds the threshold debt amount, if <b>subparagraphs (i) and (ii)</b> do not apply:</li> </ul> </li> </ul>  | 15<br>20 |
| <ul style="list-style-type: none"> <li>(i) <b>partic debt</b> is the amount of public project participant debt.</li> </ul> <p><i>Public projects treated separately</i></p>  |          |
| <ul style="list-style-type: none"> <li>(5) This section applies separately to each project of an excess debt entity for which the excess debt entity has public project debt.</li> </ul> <p><i>Public project debt and assets excluded for other applications</i></p>  | 25       |
| <ul style="list-style-type: none"> <li>(6) Public project debt and public project assets and other assets taken into account in the application of this section to an excess debt entity for a project are excluded from the debt and assets of the excess debt entity taken into account in the apportionment of interest expenditure for another project or under another section of this subpart.</li> </ul> <p>Defined in this Act: amount, company, excess debt entity, excess debt outbound company, income, income year, interest, public project asset, public project debt, public project participant debt</p> | 30       |
| <ul style="list-style-type: none"> <li>(2) <b>Subsection (1)</b> applies for income years beginning on or after 1 July 2018.</li> </ul>  |          |
| <p><b>21 Section FE 8 amended (Measurement dates)</b></p>  |          |
| <ul style="list-style-type: none"> <li>(1) In section FE 8(1), words before paragraph (a), replace “debt and total group assets” with “debt, total group assets, and total group non-debt liabilities”.</li> </ul>   | 35       |
| <ul style="list-style-type: none"> <li>(2) In section FE 8, list of defined terms, insert “total group non-debt liabilities”.</li> </ul>   |          |
| <ul style="list-style-type: none"> <li>(3) <b>Subsection (1)</b> applies for income years beginning on or after 1 July 2018</li> </ul>   |          |

**22 Section FE 10 amended (Currency)**

- (1) In section FE 10(1)(a), replace “debt and an amount of total group assets” with “debt, an amount of total group assets, and an amount of total group non-debt liabilities”.
- (2) In section FE 10, list of defined terms, insert “total group non-debt liabilities”. 5
- (3) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**23 Section FE 11 replaced (Temporary increases or decreases in value)**

- (1) Replace section FE 11 with:

**FE 11 Disregarded increases or decreases in value**

*When this section applies*

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- (1) This section applies when the effect of an increase or decrease in a value on a calculation under this subpart (the **affected calculation**) is disregarded under **section GB 51B** (Increases or decreases in value).

*Increase or decrease excluded from calculation*

- (2) The affected calculation is made excluding the effect of the increase or decrease. 15

Defined in this Act: income year

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**24 Section FE 12 amended (Calculation of debt percentages)**

- (1) Replace section FE 12(3) with: 20

*Debt percentage of group*

- (3) A debt percentage of a group is the amount calculated, on a consolidated basis and for an income year or accounting year as applicable, using the formula—  

$$\text{group debt} \div (\text{group assets} - \text{non-debt liabilities}).$$

*Definition of items in formula*

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- (3B) In the formula,—

- (a) **group debt** is the amount of the total group debt defined in section FE 15 for a New Zealand group and section FE 18 for a worldwide group:

- (b) **group assets** is the amount of the total group assets defined in section FE 16 for a New Zealand group and section FE 18 for a worldwide group: 30

- (c) **non-debt liabilities** is the amount of the total group non-debt liabilities defined in **section FE 16B** for a New Zealand group and section FE 18 for a worldwide group. 35

- (2) In section FE 12, list of defined words, insert “total group non-debt liabilities”.

- (3) **Subsection (1)** applies for income years beginning on or after 1 July 2018.
- 25 Section FE 14 amended (Consolidation of debts and assets)**
- (1) In section FE 14(3B),—
- (a) replace “debts and assets” with “liabilities and assets”;
- (b) replace “total group debt and total group assets” with “total group debt, total group assets, and total group non-debt liabilities”. 5
- (2) In section FE 14(4), words before paragraph (a), replace “total group debt and total group assets and” with “total group debt, total group assets, and total group non-debt liabilities and in”.
- (3) In section FE 14, list of defined words, insert “total group non-debt liabilities”. 10
- (4) **Subsections (1) and (2)** apply for income years beginning on or after 1 July 2018.
- 26 Section FE 15 amended (Total group debt)**
- (1) In section FE 15(1)(a)(ii), replace “deduction:” with “deduction; and”.
- (2) After section FE 15(1)(a)(ii), insert: 15
- (iii) the deduction is not denied under **section FH 3** (Payments under financial instruments producing deduction without income) as an unrecognised amount under **section FH 3(2)** or under **section FH 7 or FH 11** (which provide for the matching of deductions and income from multi-jurisdictional arrangements): 20
- (3) **Subsections (1) and (2)** apply for income years beginning on or after 1 July 2018.
- 27 Section FE 16 amended (Total group assets)**
- (1) After section FE 16(1), insert:
- Determining net current value of asset* 25
- (1BAA) For the purpose of subsection (1)(b) and (e), a net current value of an asset must be determined by a valuation of the asset by—
- (a) an independent person who is an expert in the valuation of such assets:
- (b) an employee, or other person associated with the excess debt entity, with experience in the valuation of assets and using a methodology, assumptions, and data, approved by a person qualified to give a valuation of the asset under **paragraph (a)**. 30
- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.
- 28 New section FE 16B inserted (Total group non-debt liabilities)**
- (1) After section FE 16, insert: 35

**FE 16B Total group non-debt liabilities**

*Meaning for New Zealand group*

- (1) In this subpart, for a New Zealand group, **total group non-debt liabilities** for an income year means the total of the outstanding balances of liabilities shown in the financial statements of a natural person, or an excess debt entity, or another member of the New Zealand group, reduced by the total of liabilities, each of which is— 5
- (a) included in the calculation of total group debt under section FE 15:
  - (b) under a financial arrangement, other than an agreement for the sale and purchase of property or services, entered into by a company that is a member of the group with a shareholder that is a member of the group, if the financial arrangement provides funds to the company and— 10
    - (i) the funding is provided under an arrangement between shareholders and the amount of the funds provided by each shareholder is proportional to the shareholding of each shareholder at the time: 15
    - (ii) the shareholder and associated persons hold 10% or more of the voting interests in the company:
  - (c) a share in a company that is a member of the group held by a shareholder, if— 20
    - (i) the share was issued as part of a share issue to shareholders and the number of shares issued to each shareholder was proportional to the shareholding of each shareholder at the time: 20
    - (ii) the shareholder and associated persons hold 10% or more of the voting interests in the company:
  - (d) a provision for dividends: 25
  - (e) a deferred liability of a person for tax if—
    - (i) the deferred liability arises from a difference between the value shown in the financial statements of the person for an asset and the adjusted tax value, or other value for tax purposes, of the asset; and 30
    - (ii) the deferred liability is for an amount of tax that would not arise if the asset were sold for the value shown in the financial statements; and
    - (iii) the value shown in the financial statements for the asset is calculated by reference to the amount that the person is allowed as a deduction or depreciation loss for the asset. 35

*Meaning for worldwide group*

- (2) In this subpart, for a worldwide group, **total group non-debt liabilities** for an income year means the total of the outstanding balances of liabilities shown in the financial statements of the worldwide group, reduced by the total of liabilities— 40

ities that are included in the total group debt and the total of liabilities under financial arrangements that are removed under section FE 18(3B) from the measurement of total group debt.

Defined in this Act: adjusted tax value, agreement for the sale and purchase of property or services, associated person, company, deduction, depreciation loss, dividend, excess debt entity, financial arrangement, financial statements, income year, share, shareholder, tax, total group debt, total group non-debt liabilities, voting interest

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018. 5
- 29 Section FE 18 amended (Measurement of debts and assets of worldwide group)** 10
- (1) In section FE 18(1), words before paragraph (a),—
- (a) replace “total group debt and the amount of total group assets” with “total group debt, the amount of total group assets, and the amount of total group non-debt liabilities”:
- (b) replace “is calculated” with “are calculated”. 15
- (2) In section FE 18(2), words before paragraph (a), replace “total group debt and the amount of total group assets” with “total group debt, the amount of total group assets, and the amount of total group non-debt liabilities”.
- (3) Replace section FE 18(3B)(c) with:
- (c) the owner— 20
- (i) has direct ownership interests in a member of the group of 5% or more:
- (ii) has made a settlement on a trust, having a trustee who is a member of the group, of 5% or more of the value of total settlements on the trust; and 25
- (4) In section FE 18, list of defined words, insert “total group non-debt liabilities”.
- (5) **Subsections (1) to (3)** apply for income years beginning on or after 1 July 2018.
- 30 New subpart FH inserted (Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements)** 30
- (1) After subpart FG, insert:
- Subpart FH—Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements
- FH 1 Subpart implements OECD recommendations for domestic law**
- Background, scheme, and effect of subpart* 35
- (1) This section and **section FH 2** are intended to be a guide to the background and general scheme and effect of this subpart.

*OECD recommendations*

(2) This subpart implements recommendations, for the domestic law of countries and territories, that are made by the OECD in the hybrid mismatch report and the branch mismatch report (the **reports**) and are intended to be implemented as rules neutralising certain mismatches—

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- (a) arising from arrangements called hybrid mismatch arrangements and branch mismatch arrangements in the reports; and
- (b) between income assessed and deductions against income or equivalent tax relief allowed for parties to international transactions; and
- (c) resulting from differences, between the taxation laws of different countries and territories having rights to tax the parties, in the classification of financial arrangements or the tax treatment of entities or branches.

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*Recommendations for primary and defensive rules*

(3) If 2 rules are recommended by a report for a situation, the recommended rules are called primary and defensive by the report, which states that the defensive rule should not apply to the situation except if the country or territory in the position to apply the recommended primary rule has not implemented the recommendation.

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*Implementation of individual recommendations*

(4) In this subpart,—

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- (a) **section FH 3** implements the primary version of the rule for recommendation 1 of the hybrid mismatch report, called the hybrid financial instrument rule in the report:
- (b) **section FH 4** implements the defensive version of the rule for recommendation 1 of the hybrid mismatch report:
- (c) **section FH 5** implements the primary version of the rule for recommendation 3 of the hybrid mismatch report, called the disregarded hybrid payments rule in the report, and the rule for recommendation 3 of the branch mismatch report:
- (d) **section FH 6** implements the defensive version of the rule for recommendation 3 of the hybrid mismatch report, and a defensive version of the rule for recommendation 3 of the branch mismatch report:
- (e) **section FH 7** implements recommendation 4 of the hybrid mismatch report, called the reverse hybrid rule in the report, and recommendation 2 of the branch mismatch report:
- (f) **section FH 8** implements the primary version of the rule for recommendation 6 of the hybrid mismatch report, called the deductible hybrid payments rule in the report:
- (g) **section FH 9** implements the defensive version of the rule for recommendation 6 of the hybrid mismatch report:

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| (h)  | <b>section FH 10</b> implements recommendation 7 of the hybrid mismatch report, called the dual-resident payer rule in the report:   |    |
| (i)  | <b>section FH 11</b> implements recommendation 8 of the hybrid mismatch report, called the imported mismatch rule in the report, and recommendation 5 of the branch mismatch report.   | 5  |
|  | <i>Additional rules</i>  |    |
| (5)  | In addition to the recommended rules,—   |    |
| (a)  | <b>section FH 12</b> provides for the setting off, against amounts called surplus assessable income, of amounts called mismatch amounts that arise under several of the sections and, until set off, represent deductions denied or assessable income derived: | 10 |
| (b)  | <b>section FH 13</b> provides for an election, by a borrower under a financial arrangement, that the financial arrangement be treated as a share issued by the borrower to the lender:   |    |
| (c)  | <b>section FH 14</b> provides for an irrevocable election, by an owner of a hybrid entity, that the hybrid entity be treated as a company.   | 15 |
|  | <i>Definitions</i>   |    |
| (6)  | <b>Section FH 15</b> contains definitions for the purpose of the Act of terms used in the report.  |    |
|  | <i>Variations of recommendations</i>   | 20 |
| (7)  | Variations of the implementing provisions from details of the recommendations in the report are intended to assist in the implementation and application of the recommendations.   |    |
|  | Defined in this Act: arrangement, assessable income, deduction, financial arrangement, hybrid entity, hybrid mismatch report, income, share  | 25 |
| <b>FH 2 Order of application of provisions</b> |  |    |
|  | <i>Order of application for sections disallowing deductions</i>  |    |
| (1)  | If more than 1 provision in this subpart may deny an amount of expenditure of loss as a deduction or identify the amount as a mismatch amount in a situation, the provisions are applied in the order given by the sections, which is—                         | 30 |
| (a)  | <b>section FH 3:</b>   |    |
| (b)  | <b>section FH 5:</b>   |    |
| (c)  | <b>section FH 7:</b>   |    |
| (d)  | <b>section FH 11:</b>  |    |
| (e)  | <b>section FH 8:</b>   | 35 |
| (f)  | <b>section FH 9:</b>   |    |
| (g)  | <b>section FH 10.</b>  |    |

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|-------------|--|----|
|             | <i>Order of application for sections treating receipts as assessable income</i>  |    |
| (2)         | If more than 1 provision in this subpart may identify an amount received as a mismatch amount in a situation, the provisions are applied in the order given by the sections, which is—   |    |
| (a)         | <b>section FH 4:</b>   | 5  |
| (b)         | <b>section FH 6.</b>   |    |
|             | Defined in this Act: amount, loss  |    |
| <b>FH 3</b> | <b>Payments under financial instruments producing deduction without income</b>   |    |
|             | <i>When this section applies</i>   | 10 |
| (1)         | This section applies when a person (the <b>payer</b> ) is a party to a financial instrument (the <b>payment instrument</b> ) and, if the person incurs in an income year an amount of expenditure (the <b>incurred amount</b> ) relating to a payment under the payment instrument,— |    |
| (a)         | the incurred amount is allowed as a deduction for the payer in the absence of this section and <b>sections FH 5 and FH 7 to FH 11</b> ; and  | 15 |
| (b)         | the taxation law of a country or territory outside New Zealand (the <b>payee jurisdiction</b> ) treats the payment as being received by a person or other entity (the <b>payee</b> ) in the payee jurisdiction; and  |    |
| (c)         | the payment instrument is or is part of a structured arrangement or the payer is related to the payee when the expenditure is incurred; and  | 20 |
| (d)         | the tax treatment by the payee jurisdiction of the payment meets the requirements of <b>subsection (2) or (3)</b> .  |    |
|             | <i>Amount not recognised</i>   |    |
| (2)         | The tax treatment of a payment under the payment instrument meets the requirements of this subsection if—  | 25 |
| (a)         | an amount of the payment (the <b>unrecognised amount</b> ) is not recognised by the payee jurisdiction as giving rise to income meeting the requirements of <b>subsection (9)</b> , received under a financial instrument, of the payee; and   | 30 |
| (b)         | the unrecognised amount would be recognised as giving rise to ordinary income of the payee under <b>subsection (9)</b> received under a financial instrument, if the classification of the payment or payment instrument were varied.  |    |
|             | <i>Delayed recognition of amount</i>   | 35 |
| (3)         | The tax treatment of a payment under the payment instrument meets the requirements of this subsection if—  |    |

- (a) an amount of the payment is recognised as giving rise to ordinary income of the payee under **subsection (9)** received under a financial instrument; and
- (b) the amount is recognised with a timing that does not meet the requirements of **subsection (6)**; and 5
- (c) the duration, including possible extensions, of the financial instrument may be more than 3 years.
- Amount of deduction denied*
- (4) The payer is denied a deduction for expenditure equal to the amount calculated, for a payment, using the formula— 10
- $\text{incurred amount} \times (1 - \text{payee tax} \div \text{ordinary tax}).$
- Definition of items in formula*
- (5) In the formula in **subsection (4)**,—
- (a) **incurred amount** is the amount of the expenditure incurred by the payer relating to the amount received by the payee including, for an amount meeting the requirements of **subsection (2)** and paid under a financial instrument denominated in the currency of a country or territory other than New Zealand, amounts arising from a fluctuation in the value of the currency in relation to New Zealand currency: 15
- (b) **payee tax** is the total of amounts— 20
- (i) calculated by multiplying the amount of the payment that is recognised by the payee jurisdiction as income arising from the payment received by the payee in the income year by the rate of tax imposed by the taxation law of the payee jurisdiction on the class of income that the payee is recognised as receiving: 25
- (ii) of income tax imposed by a jurisdiction on a person (the **CFC payee**) other than the payee, on an amount of income corresponding to CFC income relating to the payment and attributed to the CFC payee in the income year plus the amount of any credit for withholding tax on the payment taken into account in determining the amount of income tax imposed: 30
- (c) **ordinary tax** is the amount calculated by multiplying the amount of the income arising from the payment received by the payee by the rate of tax imposed by the taxation law of the payee jurisdiction on ordinary income under **subsection (9)** received under a financial instrument by the payee. 35
- Timing of recognised income*
- (6) The timing of the recognition by a tax jurisdiction of an amount meets the requirements of this subsection if the amount is, or is reasonably expected to be, recognised as being derived— 40

|             |  |    |
|-------------|--|----|
| (a)         | over a period of time during which the amount can reasonably be treated as accruing:   |    |
| (b)         | in an accounting period beginning within 24 months of the end of the income year to which a deduction of the payer for the incurred expenditure would be attributed:   | 5  |
|             | <i>Effect of delayed recognition</i>   |    |
| (7)         | If an amount of the payment for which a deduction has been denied under <b>subsection (4)</b> is recognised as income of the payee derived at a time not meeting the requirements of <b>subsection (6)</b> , the payer is allowed a deduction, when the amount is recognised, equal to the denied deduction.   | 10 |
|             | <i>Payer deriving income from financial instrument: excluded income</i>  |    |
| (8)         | If a payer that derives income (the <b>affected income</b> ) in an income year from a financial instrument would, as a consequence of unrecognised amounts under <b>subsection (2)</b> of payments, be denied by <b>subsection (4)</b> a deduction for a fraction (the <b>affected fraction</b> ) of expenditure incurred by the payer in the income year on payments under the financial instrument, an amount of the payer's affected income, calculated by multiplying the affected income by the affected fraction, is excluded income of the payer. | 15 |
|             | <i>Ordinary income</i>   |    |
| (9)         | An amount of income is ordinary income under this subsection for a country or territory and a person or entity if the income is—   | 20 |
| (a)         | taxed by the country or territory at the full marginal rate of the person or other entity for the income from financial instruments; and   |    |
| (b)         | not eligible for an exemption, exclusion, credit, or tax relief, under the laws of the country or territory, other than a credit or tax relief for a withholding tax or similar tax imposed on the amount of the income by the laws of another country or territory.   | 25 |
|             | Defined in this Act: accounting period, amount, CFC, deduction, excluded income, financial instrument, income, income tax, income year, New Zealand, pay, related, structured arrangement, tax   |    |
| <b>FH 4</b> | <b>Receipts under financial instruments producing deduction without income</b>   | 30 |
|             | <i>When this section applies</i>   |    |
| (1)         | This section applies when a person (the <b>payee</b> ) receives a payment under a financial instrument (the <b>payment instrument</b> ) of an amount that would not give rise to assessable income of the payee in the absence of this section and <b>section FH 6</b> , and—  | 35 |
| (a)         | the taxation law of a country or territory outside New Zealand (the <b>payer jurisdiction</b> ) treats the payment as being made under the payment instrument by a person or other entity (the <b>payer</b> ); and   |    |

- (b) the payer jurisdiction allows the payer or other person or entity to deduct the amount from income or allows an equivalent tax relief for the payment; and
- (c) the payer jurisdiction does not have hybrid mismatch legislation corresponding to **section FH 3** and applying to the payment; and 5
- (d) the payment instrument is or is part of a structured arrangement or the payer is related to the payee when the expenditure is incurred; and
- (e) the payment meets the requirements of **subsection (2) or (3)**.
- Amount not recognised*
- (2) A payment received by the payee meets the requirements of this subsection if— 10
- (a) an amount of the payment does not give rise to assessable income of the payee; and
- (b) the amount would give rise to assessable income of the payee if the classification of the payment or payment instrument were varied. 15
- Delayed recognition of amount*
- (3) A payment received by the payee under a financial instrument meets the requirements of this subsection if—
- (a) the payment gives rise to assessable income of the payee that, in the absence of this section, would be allocated to a period that does not meet the requirements of **subsection (7)**; and 20
- (b) the duration, including possible extensions, of the financial instrument may be more than 3 years.
- Assessable income*
- (4) The payee derives assessable income from the payment— 25
- (a) equal to the amount that would be assessable income of the payee if the classification of the payment or payment instrument were varied, for a payment meeting the requirements of **subsection (2)**;
- (b) allocated under **subsection (6)**.
- Imputation credit not included and not available* 30
- (5) If the payment received by the payee is a replacement payment under a returning share transfer, the amount of an imputation credit attached to the replacement payment is not included in the assessable income under **subsection (4)** and is not available as a tax credit under section LE 1 (Tax credits for imputation credits). 35
- Timing of derivation under subsection (4)*
- (6) The assessable income under **subsection (4)** is allocated to the income year in which—

|             |  |    |
|-------------|--|----|
| (a)         | income from the payment would be derived if the classification of the payment or payment instrument were varied, for a payment meeting the requirements of <b>subsection (2)</b> :   |    |
| (b)         | the payment is received, for a payment meeting the requirements of <b>subsection (3)</b> .   | 5  |
|             | <i>Timing of recognised income</i>   |    |
| (7)         | The period to which an amount of income is allocated meets the requirements of this subsection if the income is, or is reasonably expected to be, derived in an accounting period beginning within 24 months of the end of the accounting period to which a deduction or tax credit of the payer for the incurred expenditure is attributed.               | 10 |
|             | Defined in this Act: accounting period, amount, assessable income, financial instrument, hybrid mismatch legislation, imputation credit, income, income year, pay, related, replacement payment, returning share transfer, structured arrangement, tax credit  |    |
| <b>FH 5</b> | <b>Payments by New Zealand resident or New Zealand branch producing deduction without income</b>   | 15 |
|             | <i>When this section applies</i>   |    |
| (1)         | This section applies when a New Zealand resident, or New Zealand branch of a non-resident, (the <b>payer</b> ) incurs an amount of expenditure relating to a payment to another person, or incurs a charge to the New Zealand branch (the <b>branch charge</b> ) by the non-resident of an amount meeting the requirements of <b>subsection (2)</b> , and— | 20 |
| (a)         | the amount would be allowed as a deduction for the payer in the absence of this section and <b>sections FH 7 to FH 11</b> ; and  |    |
| (b)         | the taxation law of a country or territory outside New Zealand (the <b>payee jurisdiction</b> )—   | 25 |
| (i)         | treats the payment or branch charge as not being received by a person or entity in the payee jurisdiction, because of the tax status of the payer; and   |    |
| (ii)        | would treat the payment or branch charge as being received by a person or other entity (the <b>payee</b> ) in the payee jurisdiction, if the tax status of the payer were different; and   | 30 |
| (c)         | the payment is made under a structured arrangement or, when the expenditure or branch charge is incurred, the payer is in a control group with the payee or is the same person as the payee; and   | 35 |
| (d)         | no country or territory outside New Zealand and the payee jurisdiction is paid tax, on the payment or branch charge, imposed under taxation law that includes rules corresponding to the CFC rules and recognises the payment as the equivalent of attributed CFC income of a person in the same control group as the payee.                               | 40 |

*Incurred amount for transfer by branch*

- (2) A charge of an amount by a non-resident to a branch of the non-resident meets the requirements of this subsection if the amount—
- (a) represents amounts, relating to the activities outside New Zealand of the non-resident, allocated to the branch; and 5
  - (b) is not determined by reference to the amount of a payment by the non-resident, or a member of the same control group as the non-resident, to a person other than the non-resident and the members of the control group; and
  - (c) exceeds expenditure or loss, incurred by the non-resident or a member of the same control group as the non-resident, that— 10
    - (i) belongs to a category of expenditure or loss equivalent to the category to which the charge belongs; and
    - (ii) is the reference by which the amount of the charge is determined.

*Mismatch amount*

- (3) The payer has a mismatch amount for the tax year and the mismatch situation that is the greater of zero and the amount calculated using the formula— 15
- incurred + exchange.

*Definition of items in formula*

- (4) In the formula in **subsection (3)**,— 20
- (a) **incurred** is the incurred amount for the payment:
  - (b) **exchange** is—
    - (i) zero, if the payment is not made under a financial instrument denominated in the currency of a country or territory other than New Zealand; 25
    - (ii) the amount arising for the payment from fluctuations in the value of the currency in which the financial instrument is denominated in relation to New Zealand currency, if the financial instrument is denominated in the currency of a country or territory other than New Zealand. 30

*Deductions denied for mismatch amounts until offset*

- (5) A deduction is denied for expenditure or loss that is a mismatch amount from a mismatch situation until the mismatch amount is set off under **section FH 12** against surplus assessable income under that section from the mismatch situation. 35

Defined in this Act: amount, attributed CFC income, CFC, control group, deduction, financial instrument, loss, New Zealand, New Zealand resident, non-resident, pay, structured arrangement

**FH 6 Receipts from non-resident or foreign branch producing deduction without income**

*When this section applies*

- (1) This section applies when a non-resident, or foreign branch of a New Zealand resident, (the **payer**) is treated by the taxation law of a country or territory outside New Zealand (the **payer jurisdiction**) as making a payment to a person or other entity (the **payee**) in New Zealand that would not give rise to assessable income of the payee in the absence of this section, and—
- (a) the payer jurisdiction allows the payer or other person or entity to deduct the payment against income or allows an equivalent tax relief for the payment; and
  - (b) the payer jurisdiction does not have hybrid mismatch legislation corresponding to **section FH 5** and applying to the payment; and
  - (c) the payment is made under a structured arrangement or, when the expenditure is incurred, the payer is in a control group with the payee or is the same person as the payee; and
  - (d) the payment would give rise to assessable income of the payee if the payer and payee were persons and separate or if the tax status of the payer were different.

*Incurred amount for transfer by branch*

- (2) For the purposes of **subsection (1)**, the amount of a payment treated by the payer jurisdiction as being made to a New Zealand resident by a foreign branch of the New Zealand resident is equal to the amount that—
- (a) represents amounts, relating to the activities of the New Zealand resident in New Zealand, allocated to the branch; and
  - (b) is not determined by reference to the amount of a payment by the New Zealand resident, or a member of the same control group as the New Zealand resident, to a person other than the New Zealand resident and the members of the control group; and
  - (c) exceeds expenditure or loss incurred by the New Zealand resident, or a member of the same control group as the New Zealand resident, that—
    - (i) belongs to a category of expenditure or loss equivalent to the category to which the branch payment belongs; and
    - (ii) is the reference by which the amount of the payment is determined.

*Assessable income*

- (3) The payee derives assessable income from the payment equal to the greater of zero and the amount by which the amount that would be assessable income of the payee, if the payer and payee were persons and separate or if the tax status of the payer were different.

*Timing of derivation under subsection (2)*

- (4) The assessable income under **subsection (3)** is allocated to the income year in which the payment would be derived if the payer and payee were persons and separate or if the tax status of the payer were different.

*Mismatch amounts*

- (5) An amount that is treated as assessable income under **subsection (3)** for a payee and a tax year is a mismatch amount of the payee for the tax year and the mismatch situation.

*Offset of mismatch amounts*

- (6) Mismatch amounts from a mismatch situation are set off under **section FH 12** against surplus assessable income under that section from the mismatch situation.

Defined in this Act: amount, arrangement, assessable income, company, control group, deduction, hybrid mismatch legislation, income, New Zealand, New Zealand resident, non-resident, structured arrangement

**FH 7 Payments to person outside New Zealand producing deduction without income**

*When this section applies*

- (1) This section applies when a person (the **payer**) incurs an amount of expenditure (the **incurred amount**) relating to an amount of a payment to a person (the **payee**) that exists under the law of a country or territory outside New Zealand (the **payee jurisdiction**) and—

(a) the incurred amount would be allowed as a deduction for the payer in the absence of this section and **sections FH 8 to FH 11**; and

(b) under the taxation law of the payee jurisdiction, the amount is treated as being—

(i) received in a country or territory outside the payee jurisdiction:

(ii) income of a person who is in the same control group as the payer; and

(c) the payment is made under a structured arrangement or the payer is in the same control group as the payee when the expenditure is incurred; and

(d) under the taxation law of the countries and territories outside New Zealand, the amount received by the payee is not subject to taxation as income and is not recognised as CFC attributed income, or the equivalent of attributed CFC income, of a person in the same control group as the payee; and

(e) an equivalent payment by the payer would have been subject to taxation—

|  |    |
|--|----|
| <ul style="list-style-type: none"> <li>(i) as income of the payee, under the taxation law of the payee jurisdiction if the equivalent payment were treated as being received by the payee in the payee jurisdiction:</li> <li>(ii) as income of a person who is in the same control group as the payer, under the taxation law of a country or territory, outside New Zealand and the payee jurisdiction, if the equivalent payment were treated as being received by the person in that country or territory.</li> </ul>  | 5  |
| <i>Amount of deduction denied</i>  |    |
| <p>(2) The payer is denied a deduction for the incurred amount and, if the payment is made under a financial instrument denominated in the currency of a country or territory other than New Zealand, for amounts arising from a fluctuation in the value of the currency in relation to New Zealand currency.</p> <p>Defined in this Act: amount, CFC, control group, deduction, financial instrument, income, New Zealand, pay, structured arrangement</p>   | 10 |
| <b>FH 8 Expenditure or loss through hybrid entity or foreign branch producing double deduction without double income</b>   | 15 |
| <i>When this section applies</i>   |    |
| <p>(1) This section applies for a New Zealand resident and an income year when the New Zealand resident is related to a hybrid entity existing under the law of a country or territory outside New Zealand, or has a branch in such a country or territory, and—</p> <ul style="list-style-type: none"> <li>(a) the taxation law of the country or territory allows expenditure or loss of the hybrid entity, or of the New Zealand resident attributed to the branch, in the income year to be set off against income of a person or entity; and</li> <li>(b) the income of the person or entity, other than from a source in New Zealand, is not assessable income.</li> </ul> | 20 |
| <i>Mismatch amount for expenditure</i>   |    |
| <p>(2) The New Zealand resident has a mismatch amount in an income year equal to the amount of expenditure or loss incurred for the income year that—</p> <ul style="list-style-type: none"> <li>(a) is attributed to the hybrid entity or branch; and</li> <li>(b) would, in the absence of this section and <b>sections FH 9 and FH 10</b>, be allowed as a deduction in the income year corresponding to the tax year.</li> </ul>   | 30 |
| <i>Deductions denied for mismatch amounts until offset</i>   |    |
| <p>(3) A deduction is denied for expenditure or loss that is a mismatch amount from a mismatch situation until the mismatch amount is set off under <b>section FH 12</b> against surplus assessable income under that section from the mismatch situation.</p>   | 35 |
| <i>New Zealand resident becoming affected</i>  |    |
| <p>(4) <b>Subsection (5)</b> applies to a person who is a New Zealand resident and meets the requirements of <b>subsection (1)</b> at a time (the <b>transition time</b>) when—</p>  | 40 |

- (a) in a period ending with the transition time (the **unaffected period**), the person is related to a hybrid entity, or has a branch, that exists under the law of a country or territory outside New Zealand but the person does not meet the requirements of **subsection (1)**; and
- (b) the taxation law of the country or territory allows expenditure or loss of the hybrid entity, or of the New Zealand resident attributed to the branch, during the unaffected period to be set off against income that is not assessable income and arises at or after the transition time. 5
- Assessable income*
- (5) The person derives, at the transition time, assessable income equal to the amount of net loss, calculated for the person and the hybrid entity or branch and the unaffected period as if the person's income from the hybrid entity or branch were schedular income. 10
- Mismatch amounts*
- (6) An amount that is treated as assessable income under **subsection (5)** for a person and a tax year is a mismatch amount of the person for the tax year and the mismatch situation. 15
- Defined in this Act: amount, assessable income, deduction, hybrid entity, income, income year, loss, New Zealand, New Zealand resident, ring-fenced tax loss, source in New Zealand, tax year
- FH 9 Expenditure or loss of hybrid entity, or non-resident through branch, producing double deduction without double income** 20
- When this section applies*
- (1) This section applies when a resident (the **foreign resident**) in a country or territory outside New Zealand (the **foreign jurisdiction**) is in the same control group as a hybrid entity resident in New Zealand, or has a branch in New Zealand, if— 25
- (a) expenditure or loss of the hybrid entity, or of the foreign resident attributed to the branch, would be allowed as a deduction in the absence of this section and **section FH 10**; and
- (b) the taxation law of a country or territory outside New Zealand allows expenditure of the hybrid entity or attributed to the branch to be deducted against income; and 30
- (c) the foreign jurisdiction does not have hybrid mismatch legislation corresponding to **section FH 8** and applying to expenditure of the hybrid entity or foreign resident. 35
- Mismatch amount*
- (2) The hybrid entity or foreign resident has a mismatch amount in the income year equal to the amount of expenditure or loss that—
- (a) is incurred by the hybrid entity or attributed to the branch in the income year corresponding to the tax year; and 40

|              |  |    |
|--------------|--|----|
| (b)          | would, in the absence of this section, be allowed as a deduction.  |    |
|              | <i>Deductions denied for mismatch amounts until offset</i>   |    |
| (3)          | A deduction is denied for expenditure or loss that is a mismatch amount for a hybrid entity or foreign resident until the mismatch amount is set off under <b>section FH 12</b> against surplus assessable income under that section for the hybrid entity or foreign resident.  | 5  |
|              | Defined in this Act: amount, control group, deduction, hybrid entity, income, income year, loss, New Zealand, resident in New Zealand, tax year  |    |
| <b>FH 10</b> | <b>Expenditure or loss of dual resident company producing double deduction without double income</b>   | 10 |
|              | <i>When this section applies</i>   |    |
| (1)          | This section applies for a company that is a New Zealand resident (the <b>dual resident</b> ) and under the taxation law of another country or territory outside New Zealand (the <b>dual tax jurisdiction</b> ) is liable to income tax in the dual tax jurisdiction through domicile, residence, or place of incorporation.  | 15 |
|              | <i>Mismatch amount</i>   |    |
| (2)          | The dual resident has a mismatch amount equal to the amount of expenditure that would, in the absence of this section, be allowed as a deduction in the income year.   |    |
|              | <i>Deductions denied for mismatch amounts until offset</i>   | 20 |
| (3)          | A deduction is denied for expenditure or loss that is a mismatch amount from a mismatch situation until the mismatch amount is set off under <b>section FH 12</b> against surplus assessable income under that section from the mismatch situation.  |    |
|              | Defined in this Act: amount, assessable income, company, deduction, hybrid entity, income, income tax, income year, New Zealand, New Zealand resident, ring-fenced tax loss, tax year  | 25 |
| <b>FH 11</b> | <b>Residents, or non-residents with branches, having expenditure funding overseas hybrid mismatches</b>  |    |
|              | <i>When this section applies</i>   |    |
| (1)          | This section applies for a New Zealand resident, or a non-resident with a branch in New Zealand (the <b>funder</b> ), and an income year when the funder makes a payment to a person in a country or territory outside New Zealand that does not have hybrid mismatch legislation and—   | 30 |
| (a)          | the payment provides funds, directly or indirectly, for a payment (the <b>funded payment</b> ) from a person or other entity (the <b>payer</b> ) in a country or territory outside New Zealand (the <b>payer jurisdiction</b> ) to a person or other entity (the <b>payee</b> ), in the same or another country or territory outside New Zealand (the <b>payee jurisdiction</b> ); and | 35 |
| (b)          | the expenditure on the payment would be allowed as a deduction for the funder in the absence of this section and <b>sections FH 8 to FH 10</b> ; and   | 40 |

|   |  |
|---|--|
| <p>(c) the payment is made under a structured arrangement giving rise to the hybrid mismatch referred to in <b>paragraph (d)</b> or the funder, the payer, and the payee, when the expenditure is incurred, are members of a control group; and</p> <p>(d) the funded payment gives rise to a hybrid mismatch; and</p> <p>(e) the payer jurisdiction and the payee jurisdiction do not have hybrid mismatch legislation that counteracts the hybrid mismatch.</p> <p><i>Deduction denied for expenditure funding hybrid mismatch</i></p> <p>(2) The funder is denied a deduction in a tax year for an amount that is given by—</p> <p>(a) <b>subsection (3)</b>, if the payment is made under a structured arrangement giving rise to the hybrid mismatch; or</p> <p>(b) <b>subsection (4)</b>, if <b>paragraph (a)</b> does not apply.</p> <p><i>Amount denied for payment under structured arrangement</i></p> <p>(3) Under this subsection, the amount of the denial is the lesser of—</p> <p>(a) the amount of the deduction that would be allowed for the payment in the absence of this section and <b>sections FH 8 to FH 10</b>;</p> <p>(b) the amount of the funded payment that, if hybrid mismatch legislation were applied by the payer jurisdiction, would be disallowed as a deduction against income or equivalent tax relief.</p> <p><i>Amount denied for other payment</i></p> <p>(4) Under this subsection, the amount of the denial is the amount of the payment that can fairly and reasonably be treated as providing funds for the funded payment.</p> <p><i>Identifying resulting payment</i></p> <p>(5) The amount described in <b>subsection (4)(a)</b> is determined consistently with the approach described in chapter 8 of the hybrid mismatch report.</p> <p>Defined in this Act: amount, control group, deduction, hybrid mismatch, hybrid mismatch legislation, hybrid mismatch report, New Zealand, New Zealand resident, non-resident, pay, structured arrangement, tax year</p> <p><b>FH 12 Offset of mismatch amounts against surplus assessable income</b></p> <p><i>When this section applies</i></p> <p>(1) This section applies when a person has a mismatch amount under <b>sections FH 5, FH 6, and FH 8 to FH 10</b> from a mismatch situation for an income year.</p> <p><i>Offset against surplus assessable income</i></p> <p>(2) The total of mismatch amounts from the mismatch situation for the income year are set off against the person's total surplus assessable income from the mismatch situation under <b>subsection (3)</b>.</p> | <p>5</p> <p>10</p> <p>15</p> <p>20</p> <p>25</p> <p>30</p> <p>35</p> |
|---|--|

*Surplus assessable income*

- (3) The person has an amount of surplus assessable income, for the mismatch situation and the income year, equal to the greater of zero and the amount calculated using the formula—

earlier + assessable + exempt – unrecognised – protected – deductions. 5

*Definition of items in formula*

- (4) In the formula,—

(a) **earlier** is the amount of surplus assessable income for the person from the mismatch situation carried forward to the tax year corresponding to the income year from earlier tax years: 10

(b) **assessable** is the amount of assessable income derived from the mismatch situation by the person in the income year:

(c) **exempt** is zero, except for a person that is a hybrid entity resident in New Zealand and owned by a non-resident, for which it is the amount of income of the hybrid entity that— 15

(i) is exempt income under section CW 10 (Dividend within New Zealand wholly-owned group); and

(ii) for an owner of the hybrid entity, is income subject to tax under the taxation law of another country or territory without a credit for tax, other than a withholding tax on the dividend, paid by the person paying the dividend: 20

(d) **unrecognised** is the amount of the assessable income of the person from the mismatch situation for the income year that is not subject to tax under the taxation law of the foreign jurisdiction because of the residence of another person or the source of the income: 25

(e) **protected** is the amount of taxable income for which the income tax liability of the person would equal foreign tax credits under subpart LJ (Tax credits for foreign income tax) allowed for the assessable income from the mismatch situation for the income year:

(f) **deductions** is the amount of deductions allowed for expenditure incurred by the person in the income year in deriving assessable income from the mismatch situation, not including expenditure giving rise to mismatch amounts. 30

*Mismatch receipt set off against surplus assessable income from later tax year*

- (5) If a mismatch amount from a mismatch situation for a person is set off under **subsection (2)** in the tax year corresponding to an income year against an amount of surplus assessable income of the person from the mismatch situation, the payee has a deduction for the income year equal to the amount of the offset. 35

*Mismatch amounts carried forward*

- (6) If a mismatch amount from a mismatch situation is not an offset in the tax year corresponding to an income year, the remaining amount is carried forward to the next tax year if it meets the requirements of **subsection (8)** for that tax year.

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*Surplus assessable income carried forward*

- (7) If an amount of surplus assessable income from a mismatch situation is not an offset in an income year,—

(a) the amount is reduced by the amount of corresponding income, that is recognised and taxed as income arising from the mismatch situation by the taxation law of a foreign country or territory, for which the income tax liability of the person would equal credits, equivalent to foreign tax credits under subpart LJ, allowed by the foreign country or territory for the income from the mismatch situation for the income year; and

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(b) the amount remaining is carried forward to the next income year if it meets the requirements of **subsection (8)** for that income year.

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*Continuity requirement for carrying forward amounts*

- (8) A mismatch amount, or surplus assessable income, from a mismatch situation may be carried forward to a tax year corresponding to an income year (the **carry year**) if, for the tax year in which the amount arises (the **initial year**) and the carry year, a tax loss of the payee could be carried forward from the initial year to the carry year in the absence of offsets.

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*Mismatch amounts under section FH 8(3)*

- (9) A mismatch amount under **section FH 8(3)** that is available to be carried forward from a tax year corresponding to an income year is included as a tax loss component of the New Zealand resident for the next tax year (the **release year**) if—

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(a) the hybrid entity, or the New Zealand resident with the branch to which the mismatch amount is attributed, ceases to exist before the end of the income year corresponding to the release year; and

30

(b) expenditure or loss of the hybrid entity, or of the New Zealand resident attributed to the branch, has not been set off under the taxation law of a country or territory outside New Zealand against income, for the income year in which the mismatch amount arose or for a later income year, that is not assessable income of a person or entity.

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Defined in this Act: amount, assessable income, deductions, exempt income, foreign tax, hybrid entity, income year, loss, New Zealand resident, non-resident, resident in New Zealand, tax, tax loss, tax loss component, tax year, taxable income

**FH 13 Election by borrower under financial arrangement**

*Who may make election*

- (1) A person who is a borrower under a financial arrangement may make an election under this section if a payment by the person to the lender under the financial arrangement would be an unrecognised amount under **section FH 3(2)** and denied as a deduction under **section FH 3**. 5

*Treatment of financial arrangement after election*

- (2) The result of an election by the person is that, while the person is eligible to make an election, the financial arrangement is, for all purposes of the Act, a share held by the lender in the person. 10

*Notification of election*

- (3) The person must notify the Commissioner of the election, specifying the date on which the election is effective, which must be on or after the date of the notice.

*Transitional treatment of financial arrangement*

- (4) On the date on which the election is effective, the person is treated as— 15
- (a) paying the lender under the financial arrangement the amount owing under the loan (the **repayment amount**); and
  - (b) receiving the repayment amount, reduced by any withholding tax, from the lender as the subscription for a share. 20

*Expiry of election*

- (5) When the person ceases to be eligible to make an election for the financial arrangement because a deduction would be allowed for a payment of interest under the financial arrangement, the person is treated as— 25
- (a) paying to the lender the amount owing under the loan as a payment for cancellation of a non-participating redeemable share; and
  - (b) receiving, as a loan under the financial arrangement, from the lender the amount referred to in **paragraph (a)**, reduced by any withholding tax.

*NRWT rules*

- (6) The NRWT rules apply to the amount of the payment under **subsections (4)(a) and (5)(a)**. 30

Defined in this Act: amount, deduction, financial arrangement, loan, non-participating redeemable share, notify, NRWT rules, pay, share

**FH 14 Irrevocable election by owner of hybrid entity**

*Who may make election*

- (1) A New Zealand resident (the **owner**) who has, or is a member of a wholly-owned group that has, all the ownership interests in a hybrid entity may make an election under this section if the hybrid entity— 35

|  |  |
|--|--|
| <p>(a) is treated by the taxation law of a country or territory outside New Zealand (the <b>foreign jurisdiction</b>) as being resident in the foreign jurisdiction; and</p> <p>(b) is wholly owned by the owner or the owner’s wholly-owned group on the date on which the Taxation (Neutralising Base Erosion and Profit Shifting) Bill is introduced.</p> <p><i>Treatment of hybrid entity after election</i></p> <p>(2) The result of an election by the owner is that the hybrid entity is, for all purposes of the Act for the owner, a company.</p> <p><i>Notification of election</i></p> <p>(3) The owner must notify the Commissioner of the election before the due date for the return of income for the first income year in which the hybrid mismatch legislation applies to the owner.</p> <p><i>When election effective</i></p> <p>(4) The election is effective for the first income year in which the hybrid mismatch legislation applies to an owner and later income years.</p> <p><i>Transitional treatment of hybrid entity</i></p> <p>(5) For the period for which the election is effective, the hybrid entity is treated as—</p> <p style="padding-left: 20px;">(a) at the beginning of the period,—</p> <p style="padding-left: 40px;">(i) selling the undertaking of the hybrid entity at market value; and</p> <p style="padding-left: 40px;">(ii) buying the undertaking as a company (the <b>new subsidiary</b>), in which the owner has ownership interests, that is resident in the foreign jurisdiction; and</p> <p style="padding-left: 20px;">(b) during the period, making as a company each distribution to the owner.</p> <p><i>Total available subscribed capital</i></p> <p>(6) The total available subscribed capital of the new subsidiary is the amount by which the market value of the assets acquired by the new subsidiary exceeds the market value of the liabilities assumed by the new subsidiary.</p> <p><i>Election irrevocable</i></p> <p>(7) An election under this section for a hybrid entity is irrevocable.</p> <p>Defined in this Act: available subscribed capital, company, hybrid entity, hybrid mismatch legislation, income year, market value, New Zealand, New Zealand resident, notify, return of income, wholly-owned group</p> <p><b>FH 15 Definitions</b></p> <p><i>Definitions</i></p> <p>(1) In this Act,—</p> | <p>5</p> <p>10</p> <p>15</p> <p>20</p> <p>25</p> <p>30</p> <p>35</p> |
|--|--|

**act together**, for 2 persons or other entities (the **holders**) that each have rights or interests (the **rights and interests**) in a person or entity and for the ownership or control of the rights and interests, means—

- (a) the holders are associated under section YB 4 (Two relatives):
- (b) a holder typically acts in the way preferred by the other holder: 5
- (c) the holders have entered into an arrangement having an effect on the value or control of the rights or interests that is more than incidental:
- (d) the actions of the holders relating to the interests are legally controlled, are typically controlled, or are expected to be controlled, by a third person or group of persons (the **co-ordinator**) that does not meet the requirements of **subsection (2)**: 10
- (e) the holders and a co-ordinator that does not meet the requirements of **subsection (2)** enter an arrangement affecting the ownership or control of the rights and interests and having an effect on the value or control of the rights and interests that is more than incidental: 15
- (f) the holders agree with a co-ordinator that does not meet the requirements of **subsection (2)** that the co-ordinator can act on behalf of the holders in relation to the rights and interests

**branch mismatch report** means the report OECD (2017), *Neutralising the Effects of Branch Mismatch Arrangements, Action 2: Inclusive Framework on BEPS*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris 20

**control group**, means a group of persons in which, for each member and each other member,—

- (a) the members are— 25
  - (i) consolidated, or required to be consolidated, for accounting purposes:
  - (ii) members of a group of companies for which an applicable financial reporting standard requires the preparation of group financial statements for an accounting period: 30
- (b) the members are companies that are associated under section YB 2 (Two companies):
- (c) 1 of the members is a company and the other person has— 35
  - (i) a voting interest in the company of 50% or more, applying the general aggregation rule in section YB 3(3):
  - (ii) if a market value circumstance exists for the company, a market value interest in the company of 50% or more, applying the general aggregation rule in section YB 3(3):
- (d) the members are associated under section YB 4 (Two relatives):

- (e) the members are associated under sections YB 5 to YB 11 (which relate to a trustee or settlor of a trust):
- (f) 1 of the members is a partnership, or is a limited partnership, and the other member,—
- (i) if the partnership is a limited partnership, is a general partner or is a limited partner that has a partnership share of more than 50% in a right, obligation, or other property, status, or thing of the limited partnership, applying the general aggregation rule in section YB 12(3) (Partnership and partner): 5
- (ii) if the partnership is not a limited partnership, is a partner that has a partnership share of more than 50% in a right, obligation, or other property, status, or thing of the partnership, applying the general aggregation rule in section YB 12(3): 10
- (g) 1 of the members, or a group consisting of 1 of the members and persons that are related to or act together with that member, effectively controls the other member: 15
- (h) a person or group of persons, together with persons who are related to or act together with the person or a person in the group, effectively controls each of the 2 members: 20
- financial instrument** means— 20
- (a) a financial arrangement:
- (b) a share:
- (c) an annuity:
- (d) a farm-out arrangement:
- (e) a share-lending arrangement: 25
- (f) a loan in New Zealand currency described in section EW 5(10) (What is an excepted financial arrangement?):
- hybrid entity**, for 2 countries or territories, means an entity that is—
- (a) recognised in 1 of the countries or territories (the **resident jurisdiction**) as being a resident of the resident jurisdiction and subject to taxation under the taxation law of the resident jurisdiction; and 30
- (b) not recognised in the other country or territory (the **overseas jurisdiction**) as being a person, or other entity, subject to taxation under the taxation law of the overseas jurisdiction in relation to income with a source in the overseas jurisdiction 35
- hybrid mismatch** for a payment by a payer in a country or territory (the **payer jurisdiction**) to a payee in another country or territory (the **payee jurisdiction**), means a deduction for an amount of the payment if, in the absence of hybrid mismatch legislation,—
- (a) under the taxation law of— 40

- (i) the payer jurisdiction, the amount is taken into account as a deduction against income or equivalent tax relief in calculating the income of the payer subject to tax; and
- (ii) the payee jurisdiction, the amount is not recognised as ordinary income of a person or other entity within a reasonable period of time: 5
- (b) under the taxation law of—
  - (i) the payer jurisdiction, the amount is taken into account as a deduction against income or equivalent tax relief in calculating the income of the payer subject to tax; and 10
  - (ii) a jurisdiction other than the payer jurisdiction, the amount is taken into account as a deduction against income or equivalent tax relief in calculating the income of the payer subject to tax
- hybrid mismatch legislation** means—
  - (a) this subpart: 15
  - (b) legislation of a country or territory outside New Zealand having an intended effect corresponding to the effect of this subpart
- mismatch amount** means an amount, arising from a mismatch situation under a provision of this subpart, for which a deduction is allowed under **section FH 12** when the amount is set off in a tax year against an amount of surplus assessable income 20
- mismatch situation** means a situation in which differences between the taxation law of New Zealand and the taxation law of another country or territory in the tax treatment of entities or branches give rise to adjustments to deductions or income under **sections FH 5, FH 6, FH 8, FH 9, or FH 10** 25
- hybrid mismatch report** means the publication OECD (2015), *Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris
- related**, for 2 persons, means a relationship under which—
  - (a) the 2 persons are companies— 30
    - (i) that are associated under section YB 2 (Two companies):
    - (ii) for which a group of persons exists whose total voting interests in each company, determined under section YB 2, are 25% or more:
    - (iii) if a market value circumstance exists for either company, for which a group of persons exists whose total market value interests in each company, determined under section YB 2, are 25% or more: 35
  - (b) 1 of the persons is a company and the other person is not a company and the 2 persons are associated under section YB 3 (Company and person other than company): 40

- (c) the 2 persons are associated under section YB 4 (Two relatives):
- (d) the 2 persons are associated under sections YB 5 to YB 11 (which relate to a trustee or settlor of a trust):
- (e) 1 of the persons is a limited partnership and the other person is a general partner, or is a limited partner and the 2 persons are associated under section YB 12 (Partnership and partner): 5
- (f) 1 of the persons is a partnership and the other person is a partner and the 2 persons would be associated under section YB 12(2) if the partnership were a limited partnership and the partner were a limited partner:
- (g) 1 of the persons, or a group consisting of the person and persons who act together with the person, controls the other person: 10
- (h) a person or group of persons, together with persons who are related to or act together with the person or a person in the group, controls each of the persons
- structured arrangement** means an arrangement for which the terms— 15
- (a) provide for a price of a transaction under or involving the arrangement that assumes the existence of a hybrid mismatch:
- (b) are intended to produce a hybrid mismatch
- surplus assessable income** means an amount, arising from a mismatch situation under a provision of this subpart and determined under **section FH 12**, against which a mismatch amount from the mismatch situation may be set off under **section FH 12**. 20
- Exception to test for acting together*
- (2) A co-ordinator meets the requirements of this subsection for rights or interests in a person or entity held separately by 2 holders if— 25
- (a) the co-ordinator manages an investment fund through which 1 of the holders has the holder’s rights or interests in the person or entity; and
- (b) the co-ordinator manages another investment fund through which the other holder has the holder’s rights or interests in the person or entity; and 30
- (c) the 2 funds do not act together in relation to the rights and interests of the holders.
- Defined in this Act: accounting period, act together, arrangement, associated, branch mismatch report, company, control group, financial instrument, general partner, group of companies, hybrid entity, hybrid mismatch, hybrid mismatch legislation, hybrid mismatch report, limited partner, limited partnership, market value circumstance, market value interest, mismatch amount, mismatch situation, partner, partnership, related, relative, structured arrangement, surplus assessable income, voting interest 35
- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018, subject to **subsections (3) and (4)**. 40

- (3) **Sections FH 3 and FH 4**, as inserted by **subsection (1)**, do not apply for a payment—
- (a) under a financial instrument entered, on or before 6 September 2016 by a person who is—
- (i) a member of the New Zealand banking group of a registered bank, on terms intended to allow the financial instrument to qualify as capital for the purposes of the regulatory capital requirements imposed as a condition of registration under the Reserve Bank of New Zealand Act 1989, or imposed under corresponding legislation of a country or territory outside New Zealand:
- (ii) a licensed insurer, for the direct or indirect purpose of complying with regulatory capital requirements imposed as a condition of licence under the Insurance (Prudential Supervision) Act 2010, or imposed under corresponding legislation of a country or territory outside New Zealand; and
- (b) before the first date on which the person has an unconditional right to call or otherwise cancel the financial instrument without penalty.
- (4) **Section FH 11(2)(b) and (4)**, as inserted by **subsection (1)**, apply for a payment in an income year beginning on or after 1 January 2020.
- 31 New heading and section FZ 8 inserted**
- After section FZ 7, insert:

*Interest apportionment rules*

**FZ 8 Transition period for amendments to interest apportionment rules**

*What this section does*

- (1) This section gives the effect, for an excess debt entity meeting the requirements of **subsection (2)**, of the amendments (the **affected amendments**) to section FE 5 (Thresholds for application of interest apportionment rules) made by **section 18(1), (2), and (6)** of the Taxation (Neutralising Base Erosion and Profit Shifting) Act 2017 and to section FE 6 (Apportionment of interest by excess debt entity) made by **section 19(5) and (6)** of that Act.

*Requirements for section to apply*

- (2) An excess debt entity meets the requirements of this subsection if, using the method of calculating debt percentages as amended by the provisions referred to in **subsection (1)**,—
- (a) the excess debt entity is a company described in section FE 2(1)(cb) (When this subpart applies) or is controlled by a group of persons that act in concert and are each described in section FE 2(a) to (db); and

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| <p>(b) the debt percentage of the excess debt entity’s New Zealand group is greater than 60% on the date given by <b>subsection (5)</b> (the <b>transition date</b>); and</p> <p>(c) the debt percentage of the excess debt entity’s New Zealand group on the transition date is greater than 100% of the debt percentage of the excess debt entity’s worldwide group on the transition date.</p> <p><i>Transition period</i></p> <p>(3) For an excess debt entity meeting the requirements of <b>subsection (2)</b>, the affected amendments apply as varied by <b>subsection (4)</b> for a period of 5 income years (the <b>transition period</b>) beginning from the first balance date after 1 July 2018.</p> <p><i>Method and threshold values for calculations</i></p> <p>(4) For the period from the transition date to the end of the transition period, in determining whether the excess debt entity is required to apportion its interest expenditure under subpart FE (Interest apportionment on thin capitalisation) and in determining the apportionment of the excess debt entity’s interest expenditure under section FE 6,—</p> <p>(a) the method of calculating debt percentages is applied as amended; and</p> <p>(b) the threshold value for the debt percentage of the excess debt entity’s New Zealand group for the income year is 60%; and</p> <p>(c) the threshold value for the ratio of the debt percentage of the excess debt entity’s New Zealand group for the income year to the debt percentage of the excess debt entity’s worldwide group is the lesser of 110% and the corresponding ratio calculated for the transition date.</p> <p><i>Transition date</i></p> <p>(5) For the purposes of this section, the transition date is whichever the excess debt entity elects, in a return of income for the first transition year, of—</p> <p>(a) the date (the <b>introduction date</b>) on which the Taxation (Neutralising Base Erosion and Profit Shifting) Bill is introduced;</p> <p>(b) the date that is the last measurement date under section FE 8 (Measurement dates) preceding the introduction date.</p> <p><small>Defined in this Act: company, excess debt entity, income year, return of income</small></p> | <p>5</p> <p>10</p> <p>15</p> <p>20</p> <p>25</p> <p>30</p> |
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| <p><b>32 Section GB 2 amended (Arrangements involving transfer pricing)</b></p> <p>In section GB 2(3), replace “Purpose of rules and nature of arrangements” with “Purpose and application of rules and nature of arrangements”.</p> | <p>35</p> |
| <p><b>33 New section GB 51B inserted (Increases or decreases in value)</b></p> <p>(1) After section GB 51, insert:</p>   |           |

**GB 51B Increases or decreases in value**

*When this section applies*

- (1) This section applies when there is an increase or decrease in a value that affects, or would affect, the result of a calculation (the **affected calculation**) under subpart FE (Interest apportionment on thin capitalisation) and the increase or decrease is— 5

(a) caused by an action or omission that has, or would have, a purpose or effect of defeating the intent and application of subpart FE:

(b) produced by an arrangement that has an effect of defeating the intent and application of subpart FE. 10

*Increase or decrease excluded from calculation*

- (2) The effect on the affected calculation of the increase or decrease in the value is disregarded for the purposes of subpart FE.

Defined in this Act: arrangement, income year

- (2) **Subsection (1)** applies for income years beginning on or after 1 July 2018. 15

**34 New heading and section GB 54 inserted**

After section GB 53, insert:

*Arrangements involving establishments and non-resident businesses*

**GB 54 Arrangements involving establishments**

*When this section applies* 20

- (1) This section applies when—

(a) a non-resident makes, under an arrangement, a supply (the **facilitated supply**) that is of goods or services to—

(i) a person in New Zealand (the **recipient**):

(ii) a person in New Zealand (the **intermediary**), who makes under the arrangement a supply of the goods or services to another person in New Zealand (the **recipient**); and 25

(b) a person (the **facilitator**), who is not an intermediary for the facilitated supply, carries out in New Zealand under the arrangement an activity for the purpose of bringing about the facilitated supply to the recipient; and 30

(c) the facilitator—

(i) is associated with the non-resident:

(ii) derives 80% or more of the facilitator's assessable income from services provided to the non-resident or to persons associated with the non-resident; and 35

(d) the activity is more than preparatory or auxiliary to making the facilitated supply; and

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| <p>(e) income of the non-resident from the facilitated supply is not within the scope of a double tax agreement that—</p> <p style="padding-left: 20px;">(i) incorporates article 12(1) of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting;</p> <p style="padding-left: 20px;">(ii) includes a provision having a scope equal to or greater than the scope of the article referred to in <b>subparagraph (i)</b> and being negotiated after 7 June 2017; and</p> <p>(f) <b>section YD 4B(3)</b> (Meaning of permanent establishment) does not determine whether the non-resident has a permanent establishment in New Zealand; and</p> <p>(g) income of the non-resident from the supply is not attributable, other than under this section, to a permanent establishment in New Zealand of the non-resident; and</p> <p>(h) the arrangement has a purpose of affecting the imposition on the non-resident of income tax, or of income tax and the income tax of a country or territory other than New Zealand, by directly or indirectly—</p> <p style="padding-left: 20px;">(i) altering the incidence of income tax;</p> <p style="padding-left: 20px;">(ii) relieving a person from liability to pay income tax or from a potential or prospective liability to future income tax;</p> <p style="padding-left: 20px;">(iii) avoiding, postponing, or reducing a liability to income tax or a potential or prospective liability to future income tax; and</p> <p>(i) the purpose is more than merely incidental; and</p> <p>(j) the non-resident, or a group of persons that include the non-resident, is a large multinational group.</p> <p><i>Income and activities attributed to permanent establishment</i></p> <p>(2) The non-resident is treated as having a permanent establishment in New Zealand—</p> <p style="padding-left: 20px;">(a) through which the non-resident makes the facilitated supply in the course of a business carried on in New Zealand; and</p> <p style="padding-left: 20px;">(b) to which activities of the facilitator referred to in <b>subsection (1)(b)</b> are attributed.</p> <p><small>Defined in this Act: arrangement, assessable income, associated, business, double tax agreement, goods, income, income tax, large multinational group, New Zealand, non-resident, permanent establishment, services, supply</small></p> | <p>5</p> <p>10</p> <p>15</p> <p>20</p> <p>25</p> <p>30</p> <p>35</p> |
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**35 Section GC 6 amended (Purpose of rules and nature of arrangements)**

- (1) In section GC 6, heading, after “**Purpose**”, insert “**and application**”.

- (2) In section GC 6(1), replace “terms of a cross-border arrangement with an associated person” with “conditions of a cross-border arrangement with a person in the same control group”.
- (3) After section GC 6(1), insert:
- Rules apply consistently with OECD transfer pricing guidelines* 5
- (1B) This section and sections GC 7 to GC 14 apply consistently with the OECD transfer pricing guidelines.
- (4) After **section GC 6(1B)**, insert:
- Conditions of loans between persons in control group* 10
- (1C) If a transfer pricing arrangement includes a financial arrangement under which a non-resident makes a loan to a person or group of persons (the **borrower**) for which the loan is related-party debt, or that are in the same control group as the non-resident, sections GC 7 to GC 14 are applied to the transfer pricing arrangement as if the adjustments required by **sections GC 15 to GC 18** had been made to the credit rating of the borrower and the conditions of the financial arrangement. 15
- (5) Replace section GC 6(2)(b) with:
- (b) the supplier and acquirer are in the same control group; and
- (6) In section GC 6, list of defined terms, insert “control group”, “financial arrangement”, “loan”, “OECD transfer pricing guidelines”, and “related-party debt”. 20
- (7) **Subsections (2) and (3)** apply for income years beginning on or after 1 July 2018.
- (8) **Subsection (4)** applies to a person and a financial arrangement—
- (a) on and after the first balance date of the person (the **first balance date**) on or after 1 July 2018, for a financial arrangement that the person enters before the first balance date: 25
- (b) on and after the date on which the person enters the financial arrangement, for a financial arrangement that the person enters on or after the first balance date. 30
- 36 Section GC 13 amended (Calculation of arm’s length amounts)**
- (1) Replace section GC 13(1), other than the heading, with:
- (1) An arm’s length amount of consideration must be determined by applying whichever 1 or a combination of the methods listed in subsection (2) produces the most reliable measure of the amount that independent parties after real and independent bargaining would have agreed upon as the price for a transaction corresponding to the supply and acquisition under the transfer pricing arrangement if the transaction occurred under the arm’s length conditions identified under **subsections (4) and (5)**. 35

- (2) Replace section GC 13(2)(d) and (e) with:
- (d) the transactional profit split method:
  - (e) the transactional net margin method.
- (3) Replace section GC 13(4) and (5) with:
- Determination of arm's length conditions* 5
- (4) The arm's length conditions for a transaction corresponding to a supply and acquisition under a transfer pricing arrangement are determined by—
- (a) accurately delineating the transfer pricing arrangement using the approach given in the OECD transfer pricing guidelines, chapter I, section D.1; and 10
  - (b) identifying the conditions (the **arm's length conditions**)—
    - (i) for a transaction between 2 persons who are not in the same control group that occurs in circumstances comparable to the transfer pricing arrangement as delineated under **paragraph (a)**; and
    - (ii) that might be expected to be agreed upon by independent parties after real and independent bargaining. 15
- Transaction and arm's length conditions with different legal effects*
- (5) If the requirements of the OECD transfer pricing guidelines, paragraph 1.122, are met, the approach described in the OECD transfer pricing guidelines, chapter I, section D.2 may be used to identify a transaction and arm's length conditions involving— 20
- (a) no supply and acquisition; or
  - (b) a supply and acquisition that differs in its legal effects from the supply and acquisition under the transfer pricing arrangement.
- (4) After **section GC 13(5)**, insert: 25
- Amendment of assessment*
- (6) Despite the time bar, the Commissioner may amend an assessment for a tax year (the **assessed year**) in order to give effect to this section and to sections GC 6 to GC 12 and GC 14 to **GC 18** at any time in the period of 7 tax years after the tax year in which a return of income is made for the assessed year. 30
- (5) In section GC 13, list of defined terms, insert “arm's length amount”, “assessment”, “associated person”, “OECD transfer pricing guidelines”, “return of income”, “tax year”, “time bar”, “transfer pricing arrangement”.
- (6) **Subsections (1) to (4)** apply for an arrangement and income years beginning on or after 1 July 2018, except for an arrangement that complies with an advance pricing agreement issued by the Commissioner before 1 July 2018. 35
- 37 New heading and sections GC 15 to GC 18 inserted**
- (1) After section GC 14, insert:

*Cross-border related loans*

**GC 15 Aspects of loan adjusted for application of sections**

*Adjustment of aspects of loan*

- (1) If a transfer pricing arrangement includes a financial arrangement (the **cross-border related loan**) under which a non-resident (the **lender**) provides funds to a person, or group of persons, (the **borrower**) and that is a cross-border related loan under **subsection (3)**, sections GC 7 to GC 14 are applied to the transfer pricing arrangement as if—
- (a) the borrower had the credit rating required by—
- (i) **section GC 16**, if the borrower is not an insuring or lending person under **subsection (2)**;
- (ii) **section GC 17**, if the borrower is an insuring or lending person under **subsection (2)**; and
- (b) conditions of the cross-border related loan were disregarded, as required by **section GC 18**.

*Insuring or lending person*

- (2) A borrower is an insuring or lending person under this subsection if the borrower is—
- (a) a member of the New Zealand banking group of a registered bank for the purposes of subpart FE (Interest apportionment on thin capitalisation);
- (b) a licensed insurer under the Insurance (Prudential Supervision) Act 2010 or an associated person under that Act of a licensed insurer;
- (c) a non-bank deposit taker under the Non-bank Deposit Takers Act 2013 or an associated person or related person under that Act of a non-bank deposit taker;
- (d) a member of a group of persons having a main business activity of providing funds to persons who are not associated persons of the members of the group;
- (e) a member of a group of persons, consisting of members of the New Zealand group of a person not referred to in **paragraphs (a) to (d)**, having a main business activity of providing funds to persons who are not associated persons of the members of the group.

*Cross-border related loan*

- (3) A financial arrangement is a cross-border related loan under this subsection if, under the financial arrangement,—
- (a) a non-resident person (the **lender**) provides funds to another person (the **borrower**) when—
- (i) the lender and borrower are associated persons:

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| <ul style="list-style-type: none"> <li>(ii) the funding is provided through an indirect associated funding arrangement described in <b>subsection (4)</b>:</li> <li>(iii) the lender is a member of a non-resident owning body, or of a group of non-residents who act in concert and are each described in section FE 2(1)(a) to (db) (When this subpart applies), and the members of the non-resident owning body or of the group have a total ownership interest, within the meaning set out in paragraph (a) of the definition of that term, in the borrower of 50% or more; and</li> </ul> | <p>5</p>  |
| <ul style="list-style-type: none"> <li>(b) expenditure arises for the borrower for which the borrower is allowed a deduction.</li> </ul>  | <p>10</p> |
| <p><i>Indirect associated funding arrangement</i></p>   |           |
| <p>(4) An indirect associated funding arrangement exists under this subsection when,—</p>   |           |
| <ul style="list-style-type: none"> <li>(a) under an arrangement, a non-resident person (the <b>indirect lender</b>) provides funds or pays money, directly or indirectly, to another person (the <b>direct lender</b>) who provides funds to a third person (the <b>borrower</b>)—</li> </ul>   | <p>15</p> |
| <ul style="list-style-type: none"> <li>(i) in order for the funds to be provided to the borrower, or to reimburse the direct lender or compensate them, for providing the funds to the borrower; and</li> <li>(ii) with the purpose or effect that this section and sections GC 6 to GC 14 and <b>GC 16 to GC 18</b> do not apply to the arrangement; and</li> </ul>  | <p>20</p> |
| <ul style="list-style-type: none"> <li>(b) the indirect lender is associated with the borrower; and</li> <li>(c) the lender is not associated with the borrower and is not described in <b>subsection (3)(a)(iii)</b>.</li> </ul>   | <p>25</p> |
| <p>Defined in this Act: associated person, financial arrangement, loan, non-resident, non-resident owning body, ownership interest, transfer pricing arrangement</p>  |           |
| <p><b>GC 16 Credit rating of borrower: other than insuring or lending person</b></p>  |           |
| <p><i>Adjustment of long-term issuer credit rating</i></p>  |           |
| <p>(1) For the purposes of sections GC 7 to GC 14, a borrower that is not referred to as an insuring or lending person in <b>section GC 15(2)</b> has a long-term issuer credit rating for a loan given by—</p>   | <p>30</p> |
| <ul style="list-style-type: none"> <li>(a) <b>subsection (7)</b>, if the borrower has debt under cross-border related loans including the loan, of less than \$10,000,000 on the most recent calculation date given for the loan by <b>subsection (4)</b>:</li> </ul>   | <p>35</p> |
| <ul style="list-style-type: none"> <li>(b) <b>subsection (7)</b>, if the borrower is controlled by a group of persons (a <b>co-ordinated group</b>) that is a non-resident owning body or a group of persons that act in concert and are each described in section FE 2(1)(a) to (db) (When this subpart applies) and—</li> </ul>   | <p>40</p> |
| <ul style="list-style-type: none"> <li>(i) <b>paragraphs (a) and (d)</b> do not apply; and</li> </ul>   | <p>40</p> |

- (ii) on the most recent calculation date given for the loan by **subsection (4)**, the borrower's New Zealand group under subpart FE (Interest apportionment on thin capitalisation) has a debt percentage under section FE 12(3) (Calculation of debt percentages) of less than 40%; and 5
  - (iii) for each lender, the lender's ultimate parent is resident in the same country or territory as the lender or, under the tax law of the country or territory in which the lender is resident, income from the borrower's cross-border related loans is, or would be for a company having the usual tax status of a company, subject to taxation at a rate of 15% or more; and 10
  - (iv) for the borrower's New Zealand group and the period given by 1 of the paragraphs of **subsection (6)**, the income-interest ratio calculated using the formula in **subsection (2)**, is greater than 3.3: 15
- (c) **subsection (8)**, if the borrower is controlled by a co-ordinated group and **paragraphs (a) and (b)** do not apply:
- (d) **subsection (9)**, if the borrower is not controlled by a co-ordinated group and—
  - (i) **paragraph (a)** does not apply; and 20
  - (ii) the borrower elects to use the credit rating given by **subsection (7)**, for the loan, in a return of income made when or before the credit rating is determined:
- (e) **subsection (7)**, if the borrower is not controlled by a co-ordinated group and— 25
  - (i) **paragraphs (a) and (d)** do not apply; and
  - (ii) on the most recent calculation date given for the loan by **subsection (4)**, the borrower's New Zealand group under subpart FE has a debt percentage under section FE 12(3) that is less than 40% or less than 110% of the debt percentage of the borrower's world-wide group under subpart FE; and 30
  - (iii) for each lender, the lender's ultimate parent is resident in the same country or territory as the lender or, under the tax law of the country or territory in which the lender is resident, income from the borrower's cross-border related loans is, or would be for a company having the usual tax status of a company, subject to taxation at a rate of 15% or more; and 35
  - (iv) for the borrower's New Zealand group and the calculation period given by 1 of the paragraphs of **subsection (6)**, the income-interest ratio calculated using the formula in **subsection (2)**, is greater than 3.3: 40

- (f) **subsection (9)**, if the borrower is not controlled by a co-ordinated group and **paragraphs (a), (d), and (e)** do not apply.
- Income-interest ratio*
- (2) The income-interest ratio for the borrower's New Zealand group is calculated using the formula— 5
- $$(\text{net} + \text{net interest} + \text{depreciation} + \text{amortisation}) \div \text{net interest.}$$
- Definition of items in formula*
- (3) In the formula,—
- (a) **net** is the net profit or loss of the group before tax using generally accepted accounting practice, treating a net loss as a negative amount: 10
- (b) **net interest** is the deductions for interest allowed to the group under sections DB 6 to DB 9 (which relate to deductions for interest) from a financial arrangement providing funds to the group, reduced by the income of the group from a financial arrangement on arm's-length terms providing funds to a person who meets the requirements of section FE 13(3) (Financial arrangements entered into with persons outside group): 15
- (c) **depreciation** is the depreciation for the group using generally accepted accounting practice:
- (d) **amortisation** is the amortisation for the group using generally accepted accounting practice. 20
- Calculation dates for loan*
- (4) A calculation date under **subsection (1)(a), (b)(ii), or (e)(ii)** for a loan is a date—
- (a) that is the first balance date of the borrower on or after 1 July 2018, if the loan exists before 1 July 2018: 25
- (b) on which the borrower enters the loan, if the borrower enters the loan on or after 1 July 2018:
- (c) on which the loan is renewed, extended, or renegotiated. 30
- Approximate calculation if calculation date not balance date* 30
- (5) If a calculation date under **subsection (4)** is not a measurement date under section FE 8 (Measurement dates) for which the borrower measures the amounts of total group debt and total group assets, and follows a measurement date for which the borrower has made such measurements, the debt percentage may be calculated by making appropriate adjustments to the debt percentage calculated for the most recent measurement date. 35
- Calculation periods for income-interest ratio*
- (6) The calculation period under **subsection (1)(b)(iv) or (e)(iv)** for the calculation of the income-interest ratio for a borrower may be 1 of—

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| <ul style="list-style-type: none"> <li>(a) the period consisting of the 4 most recent quarters for which data are available when the calculation is performed:</li> <li>(b) the 12-month period ending with the most recent balance date for which data are available when the calculation is performed:</li> <li>(c) the 2-year period ending with the most recent balance date for which data are available when the calculation is performed:</li> <li>(d) the 3-year period ending with the most recent balance date for which data are available when the calculation is performed.</li> </ul> | 5  |
| <i>Borrower's credit rating</i>   |    |
| <ul style="list-style-type: none"> <li>(7) The credit rating of a borrower under this subsection is the credit rating that the borrower has for long-term senior unsecured debt.</li> </ul>   | 10 |
| <i>Restricted credit rating</i>   |    |
| <ul style="list-style-type: none"> <li>(8) The credit rating of a borrower under this subsection is the higher of— <ul style="list-style-type: none"> <li>(a) BBB–, or an equivalent rating, given by a rating agency approved by the Reserve Bank of New Zealand under section 86 of the Non-bank Deposit Takers Act 2013:</li> <li>(b) the credit rating that the borrower would have if the borrower's New Zealand group under subpart FE had a debt percentage equal to the lesser of 40% and the debt percentage of the New Zealand group.</li> </ul> </li> </ul>                              | 15 |
| <i>Group credit rating</i>  |    |
| <ul style="list-style-type: none"> <li>(9) The credit rating of a borrower under this subsection is the higher of— <ul style="list-style-type: none"> <li>(a) the credit rating that the borrower has for long-term senior unsecured debt:</li> <li>(b) the highest credit rating for long-term senior unsecured debt, of a member of the borrower's worldwide group under subpart FE, reduced by the smallest division within the credit rating category or between credit rating categories.</li> </ul> </li> </ul>   | 20 |
| <p style="margin: 0;">Defined in this Act: financial arrangement, generally accepted accounting practice, loan, net loss, non-resident owning body, quarter, return of income, ultimate parent</p>  |    |
| <b>GC 17 Credit rating of borrower: insuring or lending person</b>  | 30 |
| <p style="margin: 0;">For the purposes of sections GC 7 to GC 14, a borrower that is referred to as an insuring or lending person in <b>section GC 15(2)</b> has a credit rating for a loan that is equal to the highest credit rating for senior unsecured debt, of a member of the borrower's worldwide group under subpart FE (Interest apportionment on thin capitalisation).</p>   | 35 |
| <p style="margin: 0;">Defined in this Act: loan</p>   |    |

**GC 18 Loan features disregarded by rules for transfer pricing arrangements**

*General rule*

- (1) When sections GC 7 to GC 14 are applied to a borrower and a transfer pricing arrangement including a financial arrangement (the **loan**) that is a cross-border related loan, as referred to in **section GC 15(1)**, a feature of the loan is disregarded, or adjusted as required by this section, for the purposes of applying the sections if—
- (a) the borrower has debt under cross-border related loans, including the loan, of \$10,000,000 or more on the most recent calculation date given for the loan by **section GC 16(4)**; and
  - (b) the feature may increase the rate of interest payable by the borrower under the loan and—
    - (i) is referred to in **subsection (2)**; and
    - (ii) is not included in an exception under **subsections (8) and (9)**.

*Loan features disregarded or adjusted if no exception*

- (2) A feature of a financial arrangement that is a cross-border related loan may be disregarded or adjusted under this section if the feature—
- (a) allows the reduction of a liability for interest or principal by a provision of value other than a payment;
  - (b) allows a deferral of a liability to pay interest;
  - (c) provides for a change in the rate of interest payable that is contingent on an event within the control of the borrower or the lender;
  - (d) excludes the exercise of a lender’s usual rights to enforce the payment of interest or repayment of principal;
  - (e) provides that a liability to pay interest or repay principal is contingent on an event within the control of the borrower or the lender;
  - (f) provides that the term of the loan from when the financial arrangement is entered is more than 5 years;
  - (g) provides that the borrower’s obligations under the loan are subordinate to other financial arrangements of the borrower.

*Term of loan*

- (3) A term of more than 5 years for a cross-border related loan may be adjusted under **subsection (7)** if the cross-border loan has features that do not reflect requirements, relating to features of loans, referred to in **subsection (9)(a), (c), or (e)**.

*Quantities affecting adjustment to term*

- (4) Whether an adjustment is required under **subsection (7)**, and the amount of a required adjustment, is found for the date (the **calculation date**) on which the loan is entered or renewed or extended using—

|      |  |    |
|------|--|----|
| (a)  | the figure (the <b>threshold term</b> ) calculated using the formula in <b>subsection (5)</b> for financial arrangements having a term of more than 5 years—   |    |
| (i)  | included in the total group debt of the borrower’s worldwide group under subpart FE (Interest apportionment on thin capitalisation); or  | 5  |
| (ii) | between members of the borrower’s New Zealand group under subpart FE and persons other than associated persons:  |    |
| (b)  | the value of the financial arrangements used in calculating the threshold term, expressed as a fraction (the <b>threshold fraction</b> ) of—   | 10 |
| (i)  | the total group debt of the borrower’s worldwide group, if the threshold term is calculated under <b>paragraph (a)(i)</b> ; or   |    |
| (ii) | the total value of loans to members of the borrower’s New Zealand group by persons other than associated persons, if the threshold term is calculated under <b>paragraph (a)(ii)</b> .                                       | 15 |
|      | <i>Threshold term</i>  |    |
| (5)  | The threshold term for the purposes of <b>subsection (4)(a)</b> is the total of amounts, each of which is calculated using the formula—<br>$\text{term} \times \text{term debt} \div \text{total debt}.$                     |    |
|      | <i>Definition of items in formula</i>  |    |
| (6)  | In the formula,—   | 20 |
| (a)  | <b>term</b> is the period of the loan term, calculated from the most recent date on which each loan is entered or renewed or extended:   |    |
| (b)  | <b>term debt</b> is the total value on the calculation date of the principal amounts of loans with the loan term:  | 25 |
| (c)  | <b>total debt</b> is—  |    |
| (i)  | the total group debt of the borrower’s worldwide group, if the threshold term is calculated for financial arrangements described in <b>subsection (4)(a)(i)</b> ; or   |    |
| (ii) | the total value of loans to members of the borrower’s New Zealand group by persons other than associated persons, if the threshold term is calculated for financial arrangements described in <b>subsection (4)(a)(ii)</b> . | 30 |
|      | <i>Term of loan: adjustment</i>  |    |
| (7)  | The term of a loan is adjusted to equal—   | 35 |
| (a)  | the threshold term under <b>subsection (4)(a)</b> , if—  |    |
| (i)  | the term of the loan exceeds the threshold term; and   |    |
| (ii) | the total value of loans to members of the borrower’s New Zealand group by associated persons and having a term of more than   |    |

|     |  |    |
|-----|--|----|
|     | 5 years, expressed as a proportion of the total value of loans to members of the borrower's New Zealand group by associated persons, does not exceed the threshold fraction under <b>subsection (4)(b)</b> ; or  |    |
| (b) | 5 years, if when the loan is included, the total value of loans to members of the borrower's New Zealand group by associated persons and having a term of more than 5 years,—  | 5  |
|     | (i) expressed as a proportion of the total value of loans to members of the borrower's New Zealand group by associated persons, exceeds the threshold fraction under <b>subsection (4)(b)</b> :  | 10 |
|     | (ii) is more than 4 times the total value of financial arrangements with the feature that are included in total group debt of the borrower's worldwide group, when the threshold fraction is determined under <b>subsection (4)(b)(i)</b> :  |    |
|     | (iii) is more than 4 times the total value of financial arrangements with the feature that are included in the debt that is financial arrangements between members of the borrower's New Zealand group and persons other than associated persons, when the threshold fraction is determined under <b>subsection (4)(b)(ii)</b> . | 15 |
|     | <i>Exceptions for features reflecting other borrowing</i>  | 20 |
| (8) | For a borrower that is not referred to as an insuring or lending person in <b>section GC 15(2)(a), (b), or (c)</b> and a feature of a financial arrangement other than the term of a loan, the feature is not disregarded or adjusted if—  |    |
|     | (a) the feature corresponds to a feature of financial arrangements with a total value that is a fraction (the <b>feature fraction</b> ) of the total value of financial arrangements—  | 25 |
|     | (i) included in the total group debt of the borrower's worldwide group under subpart FE; or  |    |
|     | (ii) between members of the borrower's New Zealand group under subpart FE and persons other than associated persons; and   | 30 |
| (b) | the feature is included in financial arrangements, between members of the borrower's New Zealand group under subpart FE and associated persons, having a total value when the loan is included that,—  |    |
|     | (i) as a fraction of the total value of financial arrangements between the members of the borrower's New Zealand group and associated persons, is less than or equal to the feature fraction; and  | 35 |
|     | (ii) if the feature fraction is determined under <b>paragraph (a)(i)</b> , is less than or equal to 4 times the total value of financial arrangements with the feature that are included in total group debt of the borrower's worldwide group; and  | 40 |

- (iii) if the feature fraction is determined under **paragraph (a)(ii)**, is less than or equal to 4 times the total value of financial arrangements with the feature that are included in the debt that is financial arrangements between members of the borrower's New Zealand group and persons other than associated persons. 5
- Exceptions for borrowing required for some insuring or lending persons*
- (9) For a borrower that is referred to as an insuring or lending person in **section GC 15(2)(a), (b), or (c)** or is associated with such a person, a feature of a financial arrangement is not disregarded or adjusted if,—
- (a) for a borrower referred to in **section GC 15(2)(a)**, the feature reflects regulatory capital requirements that relate to features of loans and are imposed, when the financial arrangement is entered, on a member of the New Zealand banking group of a registered bank as a condition of registration under the Reserve Bank of New Zealand Act 1989: 10
- (b) for a borrower who is associated with a person (the **banking associate**) referred to in **section GC 15(2)(a)**,— 15
- (i) the financial arrangement (the **funding arrangement**) is entered for the purpose of providing funds for a financial arrangement (the **funded arrangement**), to be entered by the banking associate to satisfy regulatory capital requirements; and 20
- (ii) the features of the funding arrangement reflect the features of the funded arrangement; and
- (iii) the feature reflects a feature of the funded arrangement that meets the requirements of **paragraph (a)**: 25
- (c) for a borrower referred to in **section GC 15(2)(b)**, the feature reflects solvency capital requirements that relate to features of loans and are imposed, when the financial arrangement is entered, on a licensed insurer as a condition of licence under the Insurance (Prudential Supervision) Act 2010: 25
- (d) for a borrower who is associated with a person (the **insuring associate**) referred to in **section GC 15(2)(b)**,— 30
- (i) the financial arrangement (the **funding arrangement**) is entered for the purpose of providing funds for a financial arrangement (the **funded arrangement**), to be entered by the insuring associate to satisfy solvency capital requirements; and 35
- (ii) the features of the funding arrangement reflect the features of the funded arrangement; and
- (iii) the feature reflects a feature of the funded arrangement that meets the requirements of **paragraph (c)**: 40
- (e) for a borrower referred to in **section GC 15(2)(c)**, the feature reflects minimum capital ratio requirements that relate to features of loans and

are imposed, when the financial arrangement is entered, on a non-bank deposit taker by the non-bank deposit taker's trust deed and Regulations 8 and 10 of the Deposit Takers (Credit Ratings, Capital Ratios, and Related Party Exposures) Regulations 2010:

- (f) for a borrower who is associated with a person (the **deposit taker associate**) referred to in **section GC 15(2)(c)**,—
  - (i) the financial arrangement (the **funding arrangement**) is entered for the purpose of providing funds for a financial arrangement (the **funded arrangement**), to be entered by the deposit taker associate to satisfy minimum capital ratio requirements; and
  - (ii) the features of the funding arrangement reflect the features of the funded arrangement; and
  - (iii) the feature reflects a feature of the funded arrangement that meets the requirements of **paragraph (e)**.

Defined in this Act: associated, associated person, financial arrangement, interest, loan, New Zealand banking group, payment, transfer pricing arrangement

- (2) **Subsection (1)** applies to a person and a financial arrangement—
  - (a) on and after the first balance date of the person (the **first balance date**) that is on or after 1 July 2018, for a financial arrangement that the person enters before the first balance date:
  - (b) on and after the date on which the person enters the financial arrangement, for a financial arrangement that the person enters on or after the first balance date.

**38 New section HD 30 inserted (Members of wholly-owned large multinational group)**

After section HD 29, insert:

**HD 30 Members of wholly-owned large multinational group**

A member of a wholly-owned large multinational group is treated as an agent of another member of the large multinational group (the **principal member**) in relation to the tax obligations of the principal member if—

- (a) the principal member fails to comply with the tax obligations; and
- (b) the Commissioner notifies the member that the member has the obligations of an agent for the principal member.

Defined in this Act: agent, large multinational group, tax

**39 Section IA 2 amended (Tax losses)**

- (1) After section IA 2(4)(g), insert:

- (h) a person who has a mismatch amount under **section FH 8** (Expenditure or loss through hybrid entity or foreign branch producing double deduction without double income) that is not set off under **section FH 12**

|           |  |    |
|-----------|--|----|
|           | (Offset of mismatch amounts against surplus assessable income), the amount given by <b>section FH 12(8)</b> for the tax year.  |    |
| (2)       | <b>Subsection (1)</b> applies for income years beginning on or after 1 July 2018.  |    |
| <b>40</b> | <b>Section LE 1 amended (Tax credits for imputation credits)</b>   |    |
| (1)       | In section LE 1(2), after “section LE 7”, insert “except if the person is related to the share user or the returning share transfer is a structured arrangement, <i>see section FH 4(5)</i> (Receipts under financial instruments producing deduction without income)”.  | 5  |
| (2)       | In section LE 1, list of defined terms, insert “related” and “structured arrangement”.   | 10 |
| (3)       | <b>Subsection (1)</b> applies for income years beginning on or after 1 July 2018.  |    |
| <b>41</b> | <b>Section RF 2C amended (Meaning of non-resident financial arrangement income)</b>  |    |
| (1)       | In section RF 2C(4), formula, replace “accumulated accruals” with “(accumulated accruals – hybrid deductions)”.  | 15 |
| (2)       | After section RF 2C(5)(b), insert:   |    |
|           | (c) <b>hybrid deductions</b> is an amount equal to the part of the expenditure that the borrower incurs under the arrangement in the period given by paragraph (b) that has been denied as a deduction under <b>subpart FH</b> (Hybrid and branch mismatches of deductions and income from multi-jurisdictional arrangements) when the expenditure is incurred and is not allowed as a deduction under the subpart in that period, on the date referred to in paragraph (b)(ii). | 20 |
| (3)       | In section RF 2C, list of defined terms, insert “arrangement” and “ring-fenced tax loss”.  | 25 |
| (4)       | <b>Subsections (1) and (2)</b> apply for income years beginning on or after 1 July 2018.   |    |
| <b>42</b> | <b>New section RF 11C inserted (Interest paid by non-resident companies to non-residents)</b>  |    |
| (1)       | After section RF 11B, insert:  | 30 |
|           | <b>RF 11C Interest paid by non-resident companies to non-residents</b>   |    |
|           | <i>When this section applies</i>   |    |
| (1)       | This section applies in relation to an amount of non-resident passive income that consists of interest and is paid—  |    |
|           | (a) by a company that is resident in a country or territory outside New Zealand for the purposes of a double tax agreement; and  | 35 |
|           | (b) to a person that is resident in a country or territory outside New Zealand for the purposes of the double tax agreement.   |    |

*Application of NRWT rules to amount*

- (2) The NRWT rules apply to the amount as being interest, despite any provision in a double tax agreement that would otherwise require the NRWT rules to apply to the amount as being a dividend.

Defined in this Act: amount, company, dividend, double tax agreement, interest, New Zealand, non-resident passive income, NRWT rules, pay, tax

5

- (2) **Subsection (1)** applies for a person for the 2008–09 and later income years except for a payment of non-resident passive income made before the date of introduction of the Taxation (Neutralising Base Erosion and Profit Shifting) Bill, for which the person has adopted a tax position that is inconsistent with the amendment made by **subsection (1)**.

10

**43 Section YA 1 amended (Definitions)**

- (1) This section amends section YA 1.

- (2) Insert, in appropriate alphabetical order:

**act together** is defined in **section FH 15(1)** (Definitions)

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- (3) In the definition of **arm’s length amount**, replace “Purpose of rules and nature of arrangements” with “Purpose and application of rules and nature of arrangements”.

- (4) Insert, in appropriate alphabetical order:

**branch mismatch report** is defined in **section FH 15(1)** (Definitions)

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- (5) Insert, in appropriate alphabetical order:

**control group** is defined in **section FH 15(1)** (Definitions)

- (6) Insert, in appropriate alphabetical order:

**country-by-country report** is the report that must be provided to the Commissioner under **section 78G** of the Tax Administration Act 1994

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- (7) In the definition of **deductible foreign equity distribution**,—

(a) in paragraph (a), replace “a deduction is allowed” with “a deduction against income or equivalent tax relief or tax benefit is allowed, or would be allowed in the absence of hybrid mismatch legislation,”;

(b) in paragraph (b)(ii), replace “allowed a deduction” with “allowed, or would be allowed in the absence of hybrid mismatch legislation, a deduction against income or equivalent tax relief or tax benefit”.

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- (8) Insert, in appropriate alphabetical order:

**financial instrument** is defined in **section FH 15(1)** (Definitions)

- (9) In the definition of **goods**, replace “and EA 3 (Prepayments)” with “EA 3 (Prepayments), **GB 54** (Arrangements involving establishments), and **YD 4B** (Meaning of permanent establishment)”.

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- (10) Insert, in appropriate alphabetical order:

- hybrid mismatch legislation** is defined in **section FH 15(1)** (Definitions)
- (11) Insert, in appropriate alphabetical order:  
**hybrid mismatch report** is defined in **section FH 15(1)** (Definitions)
- (12) Insert in appropriate alphabetical order:  
**large multinational group** means a consolidated accounting group that— 5
- (a) has a member resident in New Zealand or income with a source in New Zealand; and
  - (b) has a member resident in a country or territory other than New Zealand; and
  - (c) in the latest complete income year has annual consolidated group revenue equal to or exceeding the exemption threshold referred to in paragraph 5.53 of the OECD transfer pricing guidelines 10
- (13) In the definition of **life reinsurer**, replace “sections EY 12(4)” with “sections EY 12(5)”.
- (14) Insert, in appropriate alphabetical order: 15  
**mismatch amount** is defined in **section FH 15(1)** (Definitions)
- (15) Insert, in appropriate alphabetical order:  
**mismatch situation** is defined in **section FH 15(1)** (Definitions)
- (16) Insert, in appropriate alphabetical order:  
**OECD transfer pricing guidelines** means guidelines published by the Organisation for Economic Co-operation and Development as *OECD 2017, OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* 2017, OECD Publishing, Paris 20
- (17) Insert, in appropriate alphabetical order:  
**permanent establishment** is defined in **section YD 4B** (Meaning of permanent establishment) 25
- (18) Insert, in appropriate alphabetical order:  
**public project asset** is defined in **section FE 4B** (Meaning of public project asset, public project debt, and public project participant debt)  
**public project debt** is defined in **section FE 4B** (Meaning of public project asset, public project debt, and public project participant debt) 30  
**public project participant debt** is defined in **section FE 4B** (Meaning of public project asset, public project debt, and public project participant debt)
- (19) Insert, in appropriate alphabetical order:  
**related** is defined in **section FH 15(1)** (Definitions) 35
- (20) Replace the definition of **related-party debt** with:  
**related-party debt** is defined in—

- (a) section RF 12H (Meaning of related-party debt) for the purposes of the NRWT rules:
- (b) section RF 12H(1), otherwise
- (21) In the definition of **returning share transfer**, paragraph (a)(i), delete “listed on an official list of a recognised exchange”. 5
- (22) In the definition of **services**, paragraph (b), replace “subpart MX, and in” with “and **GB 54** (Arrangements involving establishments), in subpart MX, in section **YD 4B** (Meaning of permanent establishment), and in”.
- (23) Insert, in appropriate alphabetical order:  
**structured arrangement** is defined in **section FH 15(1)** (Definitions) 10
- (24) Insert, in appropriate alphabetical order:  
**surplus assessable income** is defined in **section FH 15(1)** (Definitions)
- (25) Insert, in appropriate alphabetical order:  
**total group non-debt liabilities** is defined in **section FE 16B** (Total group non-debt liabilities) for the purposes of subpart FE (Interest apportionment on thin capitalisation) 15
- (26) In the definition of **transfer pricing arrangement**, replace “Purpose of rules and nature of arrangements” with “Purpose and application of rules and nature of arrangements”.
- (27) Insert, in appropriate alphabetical order: 20  
**wholly-owned large multinational group** means a large multinational group for which a group of persons holds all the ownership interests in each member
- (28) **Subsections (2) to (5), (7) to (11), and (13) to (27)** apply for income years beginning on or after 1 July 2018.
- 44 Section YD 4 amended (Classes of income treated as having New Zealand source)** 25
- (1) After section YD 4(17B), insert:  
*Income through permanent establishment*
- (17C) Income attributable to a permanent establishment in New Zealand has a source in New Zealand, subject to subsections (15) to (17). 30  
*Income taxable under double tax agreement*
- (17D) Income that may be taxed in New Zealand under a double tax agreement has a source in New Zealand.
- (2) In section YD 4, list of defined terms, insert “double tax agreement” and “permanent establishment”. 35
- (3) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**45 New section YD 4B inserted (Meaning of permanent establishment)**

(1) After section YD 4, insert:

**YD 4B Meaning of permanent establishment**

*What this section does*

(1) This section gives the meaning of **permanent establishment** for a person or other enterprise (the **enterprise**) that makes in New Zealand a supply of goods or services. 5

*Double tax agreement with applicable definition*

(2) **Permanent establishment**, for an enterprise that is resident in a country or territory with which New Zealand has a double tax agreement that includes a definition of permanent establishment, has the meaning given by— 10

(a) the double tax agreement:

(b) **section GB 54** (Arrangements involving establishments), if the enterprise meets the requirements of the section. 15

*No double tax agreement with applicable definition*

(3) **Permanent establishment**, for an enterprise that is resident in New Zealand or in a country or territory with which New Zealand does not have a double tax agreement that includes a definition of permanent establishment, has the meaning given by **schedule 23** (Meaning of permanent establishment). 20

*Interpretation of schedule 23*

(4) **Schedule 23** is treated as applying consistently with the guidance relevant to the schedule that is provided by the Commentary on Article 5 of the Model Tax Convention on Income and on Capital, in *Model Tax Convention on Income and on Capital* published by the Organisation for Economic Co-operation and Development, as amended from time to time. 25

Defined in this Act: business, double tax agreement, goods, New Zealand, non-resident, permanent establishment, resident in New Zealand, services

(2) **Subsection (1)** applies for income years beginning on or after 1 July 2018.

**46 Section YD 5 amended (Apportionment of income derived partly in New Zealand)** 30

After section YD 5(1), insert:

*Exception when permanent establishment*

(1BA) This section does not apply to business activities that a person carries on through a permanent establishment in New Zealand.

**47 New section YD 5B inserted (Attribution of income derived through permanent establishment in New Zealand)** 35

After section YD 5, insert:

**YD 5B Attribution of income derived through permanent establishment in New Zealand**

*When this section applies*

- (1) This section applies when a person carries on business activities through a permanent establishment in New Zealand. 5

*Apportionment*

- (2) The amount of income of the person that must be attributed to the permanent establishment is the amount that the permanent establishment might be expected to derive if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the person. 10

Defined in this Act: amount, income, New Zealand, permanent establishment

**48 New schedule 23 inserted (Meaning of permanent establishment)**

- (1) After schedule 22, insert the **schedule 23** in the **schedule**.  
(2) **Subsection (1)** applies for income years beginning on or after 1 July 2018. 15

**Part 2**

**Amendments to Tax Administration Act 1994**

**49 Tax Administration Act 1994**

This Part amends the Tax Administration Act 1994.

**50 Section 17 amended (Information to be furnished on request of Commissioner)** 20

After section 17(1C), insert:

- (1CB) For the purpose of subsection (1) and sections **139AB**, 143(2) and 143A(2), information or a document is treated as being in the knowledge, possession, or control of a member of a large multinational group in an income year, disregarding any law of a foreign country relating to the secrecy of information, if the information or document is in the knowledge, possession, or control of the member or another member of the large multinational group. 25

**51 New section 21BA inserted (Information required to be provided by large multinational group)** 30

After section 21, insert:

**21BA Information required to be provided by large multinational group**

- (1) This section applies if the Commissioner notifies a member of a large multinational group by a notice (the **information demand**) that the member is required under section 17 to provide information relating to the large multinational group. 35

- tional group or to a member of the large multinational group, and the member—
- (a) fails to provide, within 3 months of the date of the information requisition (the **demand date**), a response to the information demand: 5
  - (b) provides, within 3 months of the demand date, a response that the Commissioner considers to be misleading because it contains misleading information or omits relevant information: 5
  - (c) provides, within 3 months of the demand date, a response that the Commissioner considers omits information, whether or not in the knowledge, possession, or control of the member, required by the information demand for the calculation of— 10
    - (i) an arm’s length amount for a cross-border transaction: 10
    - (ii) an amount of profit attributable to a permanent establishment in New Zealand of the member or another member of the large multinational group: 15
  - (d) provides, within 3 months of the information demand date, a response that the Commissioner considers does not fulfil the requirements of the information demand. 15
- (2) The Commissioner must notify the member by a further notice that if the member does not provide a satisfactory response to the information demand before the date (the **information deadline**) that is 1 month after the date of the further notice,— 20
- (a) the Commissioner may rely on the information held by the Commissioner in exercising the Commissioner’s powers to prosecute, penalise, assess, or reassess the member or other members of the large multinational group for a tax year to which the information required by the information demand relates; and 25
  - (b) information required by the information demand and not provided to the Commissioner by the information deadline will not be allowed as evidence for use by the member or other member of the large multinational group in a dispute concerning an action of the Commissioner referred to in **paragraph (a)**. 30
- (3) If a member of a large multinational group disputes a prosecution, imposition of a penalty, assessment, or reassessment, relating to a tax year, and information that is required by an information demand and relates to the tax year is not provided to the Commissioner before the information deadline, the information that is not the subject of a court order under **subsection (4)** is not— 35
- (a) allowed as evidence for use by the member in a disputes procedure under Part 4A: 35
  - (b) admissible as evidence for the member in proceedings under Part 8 or Part 8A, or other proceedings. 40

- (4) A member of a large multinational group is allowed to use information in a way that would otherwise be prevented by **subsection (3)** if a court or Authority—
- (a) determines that obtaining the information in response to the information demand would have required an investment by the member of time and resources that would have been unreasonable in relation to the relevance of the information to the tax issues involved; and 5
  - (b) determines that admission of the evidence is necessary to avoid manifest injustice to the member; and
  - (c) orders that the information be allowed or admissible as evidence in the proceedings. 10

**52 New section 78G inserted (Country-by-country report from large multinational group)**

- (1) Before section 79, insert:

**78G Country-by-country report from large multinational group** 15

- (1) A large multinational group with an ultimate parent under subpart FE of the Income Tax Act 2017 that is a New Zealand resident must provide to the Commissioner a report, for each period set by the Commissioner, that includes:
- (a) the information described in the OECD transfer pricing guidelines, Chapter V, Annex III; and 20
  - (b) other information that is required by the Commissioner.
- (2) The report for a period must be provided to the Commissioner by the date that is 12 months after the end of the period.
- (2) **Subsection (1)** applies for an income year beginning on or after 1 January 2016. 25

**53 New section 139AB inserted (Penalty for member of large multinational group failing to provide information)**

After section 139AA, insert:

**139AB Penalty for member of large multinational group failing to provide information** 30

- (1) A member of a large multinational group is liable to pay a penalty under this section if—
- (a) the Commissioner requires the member under section 17 to provide information or a document that is treated under **section 17(1CB)** as being in the knowledge, possession, or control of the company; and 35
  - (b) the member fails to provide the information or document within the time allowed by the Commissioner.

- (2) The penalty under this section is the amount specified by the Commissioner, which must not exceed \$100,000.

**54 Section 143 amended (Absolute liability offences)**

- (1) In section 143(2)(b), replace “control.” with “control; and”.
- (2) After section 143(2)(b), insert: 5
- (c) if the person is a member of a large multinational group, there is no member of the person’s large multinational group that has the information in the member’s knowledge, possession, or control.

**55 Section 143A amended (Knowledge offences)**

- (1) In section 143A(2)(b), replace “control.” with “control; and” 10
- (2) After section 143A(2)(b), insert:
- (c) if the person is a member of a large multinational group, there is no member of the person’s large multinational group that has the information in the member’s knowledge, possession, or control.

**Schedule**  
**New schedule 23**

**s 48**

**Schedule 23**  
**Meaning of permanent establishment**

5

**s YD 4B(3)**

**Permanent establishment**

- 1 The term **permanent establishment** means a fixed place of business through which the business of a person or other entity (an **enterprise**) is wholly or partly carried on. 10
- 2 The term **permanent establishment** includes especially:
- (a) a place of management; and
  - (b) a branch; and
  - (c) an office; and
  - (d) a factory; and 15
  - (e) a workshop; and
  - (f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.
- 3 A building site, or a construction, installation or assembly project, or supervisory activities in connection with that building site or construction, installation or assembly project, constitutes a permanent establishment if it lasts more than 6 months. 20
- 4 An enterprise shall be deemed to have a permanent establishment in a country or territory (the **State**) and to carry on business through that permanent establishment if for more than 183 days in any 12 month period— 25
- (a) it carries on activities in that State which consist of, or which are connected with, the exploration for or exploitation of natural resources, including standing timber, situated in that State; or
  - (b) it operates substantial equipment in that State.
- 5 Notwithstanding the provisions of **clauses 1 and 2** where an enterprise of a State performs services in another State (the **other State**)— 30
- (a) through an individual who is present in that other State for a period or periods exceeding in the aggregate 183 days in any 12 month period, and more than 50% of the gross revenues attributable to active business activities of the enterprise during this period or periods are derived from the services performed in that other State through that individual; or 35

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- (b) for a period or periods exceeding in the aggregate 183 days in any 12 month period, and these services are performed for the same project or for connected projects through one or more individuals who are present and performing such services in that other State—
- the activities carried on in that other State in performing these services shall be deemed to be carried on through a permanent establishment of the enterprise situated in that other State, unless these services are limited to those mentioned in **clause 7** which, if performed through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that clause. For the purposes of this clause, services performed by an individual on behalf of one enterprise shall not be considered to be performed by another enterprise through that individual unless that other enterprise supervises, directs or controls the manner in which these services are performed by the individual.
- 6 For the sole purpose of determining whether the time period referred to in **clauses 3, 4, and 5**, has been exceeded,—
- (a) where an enterprise of a State carries on activities referred to in **clause 3, 4, or 5** for a period of more than 30 days and these activities are carried on during periods of time that do not last more than the period stipulated in those clauses; and
- (b) connected activities are carried on in that other State during different periods of time, each exceeding 30 days, by one or more enterprises closely related to the first-mentioned enterprise.
- These different periods of time shall be added to the period of time during which the first-mentioned enterprise has carried on the activities referred to in **clause 3, 4, or 5**.
- 7 Notwithstanding the preceding provisions of this section, the term **permanent establishment** shall be deemed not to include—
- (a) the use of facilities solely for the purpose of storage, display, or delivery of goods or merchandise belonging to the enterprise:
- (b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display, or delivery:
- (c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise:
- (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise:
- (e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity:
- (f) the maintenance of a fixed place of business solely for any combination of activities mentioned in **subclauses (a) to (e)**—

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|     | Provided that such activity, or in the case of <b>subclause (f)</b> , the overall activity of the fixed place of business, is of a preparatory or auxiliary character.   |          |
| 7.1 | <b>Clause 7</b> shall not apply to a fixed place of business that is used or maintained by an enterprise if the same enterprise or a closely related enterprise carries on business activities at the same place or at another place in the same State and—  | 5        |
|     | (a) that place or other place constitutes a permanent establishment for the enterprise or the closely related enterprise under the provisions of this section; or  |          |
|     | (b) the overall activity resulting from the combination of the activities carried on by the 2 enterprises at the same place, or by the same enterprise or closely related enterprises at the 2 places, is not of a preparatory or auxiliary character—   | 10       |
|     | Provided that the business activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, constitute complementary functions that are part of a cohesive business operation.  | 15       |
| 8   | Notwithstanding the provisions of <b>clauses 1 and 2</b> but subject to the provisions of <b>clause 9</b> , where a person is acting in a State on behalf of an enterprise and, in doing so—   |          |
|     | (a) habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are—   | 20       |
|     | (i) in the name of the enterprise; or  |          |
|     | (ii) for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use; or  | 25       |
|     | (iii) for the provision of services by that enterprise; or   |          |
|     | (b) manufactures or processes in a State for the enterprise goods or merchandise belonging to the enterprise,—   |          |
|     | that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, unless the activities of such person are limited to those mentioned in <b>clause 7</b> which, if exercised through a fixed place of business (other than a fixed place of business to which <b>clause 7.1</b> would apply), would not make this fixed place of business a permanent establishment under the provisions of that subsection. | 30<br>35 |
| 9   | <b>Clause 8</b> shall not apply where the person acting in a State on behalf of an enterprise of the other State carries on business in the first-mentioned State as an independent agent and acts for the enterprise in the ordinary course of that business. Where, however, a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall  | 40       |

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- not be considered to be an independent agent within the meaning of this clause with respect to any such enterprise.
- 10 The fact that a company which is a resident of a State controls or is controlled by a company which is a resident of the other State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other. 5
- 11 For the purposes of this clause, a person or enterprise is closely related to an enterprise if, based on all the relevant facts and circumstances, 1 has control of the other or both are under the control of the same persons or enterprises. In any case, a person or enterprise shall be considered to be closely related to an enterprise if 1 possesses directly or indirectly more than 50% of the beneficial interest in the other (or, in the case of a company, more than 50% of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) or if another person or enterprise possesses directly or indirectly more than 50% of the beneficial interest (or, in the case of a company, more than 50% of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) in the person and the enterprise or in the 2 enterprises. 10  
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