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Subvention Payments – Change in IRD Policy

We have recently resolved a long standing dispute with the IRD regarding the meaning of “payment” in the context of subvention payments to effect a group company loss offset. In the case in question, the IRD eventually agreed with nsaTax’s view that “payment” should have its ordinary meaning and a subvention payment effected by offsetting an existing liability owing by the loss company to the profit company was acceptable.

This has coincided with the IRD advising (in its March issue of Agent’s Answers) that it has changed its long standing policy of requiring that a physical payment be made for a subvention payment to be valid. Instead, the IRD has stated that “*in the absence of any statutory definition in the context of subvention payment, the meaning of “payment” should be given its ordinary meaning*”. The article then goes on to confirm that other methods of payment are acceptable, such as accounting entries.

This is a significant change, and in our view is a change in the right direction. While we have often advised clients to err on the side of caution and ensure subvention payments were made via a physical payment, we have long considered the IRD’s view on “payment” in relation to subvention payments to be questionable.

The IRD state in TIB Vol.5, No.11, April 1994 in the case of GST second-hand goods claims between associated persons that payment can be made by way of:

- Journal / accounting entries
- Acknowledgement of debt and mortgage back
- Cheque swaps

The IRD now accept that a subvention payment can be effected by any of the above means and a physical payment or cheque swap is no longer required.

Please contact one of the nsaTax consultants if you require further assistance with the tax implications of subvention payments

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LAQC's and Leaky Building Claims

Another (non tax) factor not to overlook when advising your clients on their LAQC options arises where the company owns a leaky building which may give rise to a claim. Some lawyers are advising that if a property which is the subject of a leaky building claim changes hands, this prejudices the ability to continue with the claim.

We understand that this is because the new owner will acquire the property knowing about the defects. Whilst a transition to sole ownership or partnership will be neutral for tax purposes it will clearly be a change of ownership and appropriate legal documentation is required to effect this (for example, a transfer of land must be in writing).

If this is the case and your client does not want to prejudice the claim, the company must continue to own the property, and the only options are to transition from an LAQC to a QC or an LTC.

Keith Turner

Statute Time Bar Issues

The Commissioner of Inland Revenue is not able to increase an income tax assessment if four years have passed from the end of the tax year in which the original assessment is made.

The time bar does not apply where the returns filed are fraudulent, wilfully misleading or omit all mention of income which is of a particular nature or source. Practitioners have raised concerns about IRD seeking to reopen returns where IR10's have been filed which do not specifically identify income of a particular nature or source.

In the IRD's Agents Answers for March 2011, the IRD concede the IR10 does not contain categories covering all income sources and accept that a source of income may not be specified in an IR10, yet is contained in the financial statements (which are not filed). In that case IRD state they would only seek to reopen assessments beyond the time bar if there is conclusive evidence the return is fraudulent or wilfully misleading. The other situation that can arise is where income is not required to be disclosed in the IR10 but is also not in the financial statements and is not included when calculating taxable income. The IRD would consider reopening beyond the four year time bar in that situation,

In previous TIB articles the IRD have also commented on the time bar in situations where specific disclosure forms are required, such as to disclose an interest in a CFC or FIF. If an IR10 does not have a place to disclose this income, but the specific disclosure form is filed, IRD say that the time bar applies. If the income is omitted from the IR 10 and the disclosure form is not filed, it is unclear whether the time bar will still apply if the income is included in financial statements which are filed with IRD. We think not, since a specific disclosure was required but we can't be certain as to the IRD's view.

If your clients are seeking to get the benefit of the time bar then you may wish to file financial statements with the IRD at the time tax returns are filed.

Keith Turner