New Zealand
Bankers' Association

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Clerk of the Committee
Finance and Expenditure Select Committee
Parliament Buildings
WELLINGTON

Dear Madam

Taxation (GST and Remedial Matters) Bill
Submission of the New Zealand Bankers' Association

The following submission is made by the New Zealand Bankers' Association in respect of the Taxation (GST and Remedial Matters) Bill ("the Bill") which was tabled in Parliament on 5 August 2010. The submission concerns four proposed amendments to the Goods and Services Act 1985.

Zero rating of mortgagee sales

It is proposed that land sales between registered persons will be zero rated where the purchaser acquires the land with the intention of making taxable supplies. Clause 20 inserts new section 78F into the GST Act -- section 78F specifies that the supplier must **confirm** that the recipient is intending to use the land in the course of making taxable supplies. The issue that requires resolution is the clarification of the vendors' actions which will be considered to be sufficient to meet this requirement. In accordance with proposed subsection 78F(5), it is possible for the Commissioner to impose the GST liability on the vendor if the requirement is not met.

Banks acting as mortgagees in possession will be subject to new section 78F. We submit that proposed section 78F should be amended so that vendor obligations regarding purchaser intentions are satisfied by a purchaser contractual representation. Such a representation could be built into the standard Auckland District Law Society documentation for the sale and purchase of real estate.

Our reasoning is that it should be certain in law that the vendor has no obligation whatsoever to audit or carry out any due diligence in relation to purchaser intentions or tax position. The vendor should be able to rely on clear written representations made by the purchaser. The banks see a significant risk in the current formulation and the unfettered ability of the Commissioner to seek payment from the vendor in the case of mortgagee sales, given that in general, the bank will be the easiest taxpayer to locate and will certainly have the "deepest pockets". Consequently, the currently proposed wording appears to impose a significant risk on the bank as vendor in the event of purchaser fraud or misrepresentation.

Zero rating of commercial lease rentals (and consequent application of domestic reverse charge)

Land, for the purposes of the proposed zero rating rules, extends to interests in land. Consequently, the supply of a leasehold interest will be subject to the zero rating provisions if the proposed rules are enacted. Reverse charging is proposed (per proposed subsection 20 (3I)) where the supply of leasehold property is made to a person who does not use the land solely for the purposes of making taxable supplies. This potentially creates a significant administrative burden for banks and other financial institutions which habitually lease a large number of premises forming their branch network.

We understand that the extended definition of land is intended to prevent variations on "Phoenix schemes" whereby significant value is attributed to a leasehold interest through manipulation of the underlying rental stream. If the leasehold interest was not the subject of the proposed zero rating rules an amount of GST commensurate with that arising on the sale of the freehold interest in the property would be at stake. While we understand the attractiveness of ensuring that such avenues to circumvent the application of the measures are blocked, we consider that the concomitant impact on normal commercial leasehold transactions is unwarranted. In short, we consider that only specifically targeted measures should be contemplated.

We submit that normal commercial leasehold interests should not be captured by the domestic reverse charge regime and zero rated. Based on information to date, Officials' concerns should be able to be addressed by zero rating only (i) transfers of leases and (ii) prepayments of more than 12 months on leases.

Proposed replacement of change in use adjustment provisions

Banks have recently and are currently undertaking significant systems change to accommodate various tax changes. Making the required changes has resulted in material cost to banks and core business projects being deferred to accommodate these changes. The proposed replacement of the current change in use provisions will require systems changes to be implemented by 1 April 2011 and will place further financial burden on banks and cause further delay of core business projects. As noted below, we consider that an alternative to the proposed methodology should be legislated which would obviate the need for system changes; even so we consider that further consultation will still be required and that it is likely that the Memorandum of Understanding ("MOU") with banks will need to be updated. Consequently, we submit that the effective date of the proposed replacement of the change in use adjustment provisions should be deferred until consultations have been concluded and any amendment to the MOU has been made. We submit that a 1 October 2011 or 1 April 2012 effective date is more appropriate.

Fixed asset 1 April 2011 transition adjustments

We submit that the Bill should be amended to confirm that on transition, assets held for which no GST input tax claim was available on purchase should give rise to a GST input tax claim on transition, and that this input tax claim should be equal to GST component of depreciated tax book value x GST recovery ratio. That is, the transition deemed repurchase should not be treated differently to any other asset purchase under the new regime.

To get to this result the transition deemed sale should not have any net GST implications. For a Bank, this appears achievable on the basis that either (i) the transition deemed sale is not subject to GST as having occurred in the course of an exempt activity, or (ii) if the transition deemed sale is GST taxable (as Bill clause 21G(3)(a) suggests), then a GST input tax claim must arise in relation to the component of tax book value that is GST not claimed from the original acquisition. Either approach should result in net nil GST payable to IRD on the transition deemed sale.

One of these approaches to the transition deemed sale is required, as in the alternative the GST output tax cost that would arise on transition deemed sale will preclude the transitioning of assets by Banks and require the unjustifiable cost of maintaining two fixed asset registers.

We believe that these transition principles should be in the Bill, in particular clause 21G needs to be amended to confirm that a Bank (or other mixed use supplier) does not have net GST payable to the IRD on the deemed sale of transition fixed assets. The detail of the input tax claim arising on the deemed repurchase can then be worked through in the MOU process The resulting transition deemed repurchase GST refund amounts involved should not cause IRD any concern, or alternatively perhaps the GST refund could be spread across say 2 years.

Fixed asset change in use adjustments post 1 April 2011

The change in use adjustment regime is proposed to be radically overhauled such that in the year of acquisition a taxpayer is entitled to claim GST in respect of a supply to the extent that the taxpayer intends to use the supply in the course of a taxable activity.

There are various safe harbours - where the taxable value of the supply is under $5k or the difference between actual use and intended use is 10% (though this does not apply where the actual dollar difference is more than $1k). There are also various thresholds after which further year on year adjustments are not necessary (including a base line for assets related to an asset's estimated useful life). However, we note that a 5% safe harbour between actual use of goods and services and use estimated on acquisition (which Officials proposed in the discussion document) has not found its way into the Bill. Given that this safe harbour was proposed by Officials to reduce taxpayers' compliance costs (and would expect that it would have a significant effect in that regard) we submit that it should be retained and be available to taxpayers.

For banks (and any other financial service provider) the calculation of year on year adjustments as proposed is onerous even with the de minimis safe harbours. Effectively our members will have to develop a database through which we can identify all assets costing more than $5k, filter out the assets which are excluded according to the various safeharbours and adjustment thresholds and then adjust the amount of GST for the remaining assets each year for movements in the recovery ratio, and then make the consequent adjustments to the assets costs base and depreciation charges.

The MOU dictates the GST treatment of various supplies made by and to banks. In our view, the treatment of input tax on the acquisition of assets and the impact of subsequent movements in the recovery ratio should be determined by reference to the MOU. In order to allow this to occur, we submit that the proposed section 21 (per clause 14 of the Bill) should be amended to also allow fair and reasonable methodologies that are agreed between the IRD and a taxpayer or a group of taxpayers.

We understand that while the proposed change in use adjustments reflect the approach taken in Australia, we also understand that in Australia this type of approach is proving too compliance intensive for both large corporations and the ATO and is consequently the subject of reform efforts.

Verbal Submission to Select Committee

NZBA would welcome the opportunity to make a verbal submission in support of this written submission.

If you have any questions please contact Tim Carter at ASB Bank Limited on phone (09) 337 4603.

Yours sincerely

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