

# **Submission**

By

**Business|NZ**

To

**Finance & Expenditure Select Committee**

On

**Taxation (Base Maintenance and  
Miscellaneous Provisions) Bill**

**28 February 2005**

PO Box 1925  
Wellington  
Ph: 04 496 6555  
Fax: 04 496 6550

**TAXATION (BASE MAINTENANCE AND MISCELLANEOUS PROVISIONS) BILL**  
**SUBMISSION BY BUSINESS NEW ZEALAND**  
**28 FEBRUARY 2005**

**1. INTRODUCTION**

- 1.1 Encompassing four regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce, and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 56-member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.
- 1.2 In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.
- 1.3 Business New Zealand's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services). It is widely acknowledged that consistent, sustainable growth well in excess of 4% per capita per year would be required to achieve this goal in the medium term.
- 1.4 The health of the economy also determines the ability of a nation to deliver on the social and environmental outcomes desired by all. First class social services and a clean and healthy environment are possible only in prosperous, first world economies.
- 1.5 The tax system has a critical role to play in attracting investment and fostering a dynamic, productive and innovative economy. High tax rates and complex compliance requirements impose significant costs on the community, including lower investment, output, incomes, and employment as well as distortions in behaviour.
- 1.6 Business New Zealand welcomes the opportunity to comment on the Taxation (Base Maintenance and Miscellaneous Provisions) Bill (referred to as 'the Bill'). While Business New Zealand supports many of the measures contained in the Bill, we wish to make some comments on certain aspects of the Bill that we are concerned about or believe could be enhanced.

## **2. SUMMARY OF RECOMMENDATIONS**

2.1 Notwithstanding Business New Zealand's overall recommendation that the Bill should proceed, we also recommend that:

- (a) The deduction for losses on buildings includes voluntary destruction or disposal;
- (b) Statutory privilege for tax advice provided by accountants also includes factual background matters;
- (c) The Bill's proposal that tax exemptions of non-resident companies for drilling exploratory or seismic survey work relating to petroleum exploration in New Zealand should proceed. However, exemptions should be automatically given rather than having to be applied for, and exemptions should apply to all services associated with drilling and surveying by non-resident contractors;
- (d) The Bill's proposal that the categories and rates for deductible environmental expenditure as outlined in the Bill should proceed. However, the interest rate of 3% on deposits into a restoration account should be revised upwards to make it more commercially aligned; and
- (e) The Bill's proposal to deregister non-residents who do not carry on a taxable activity in New Zealand should not proceed.

2.2 The remainder of this submission is in four parts:

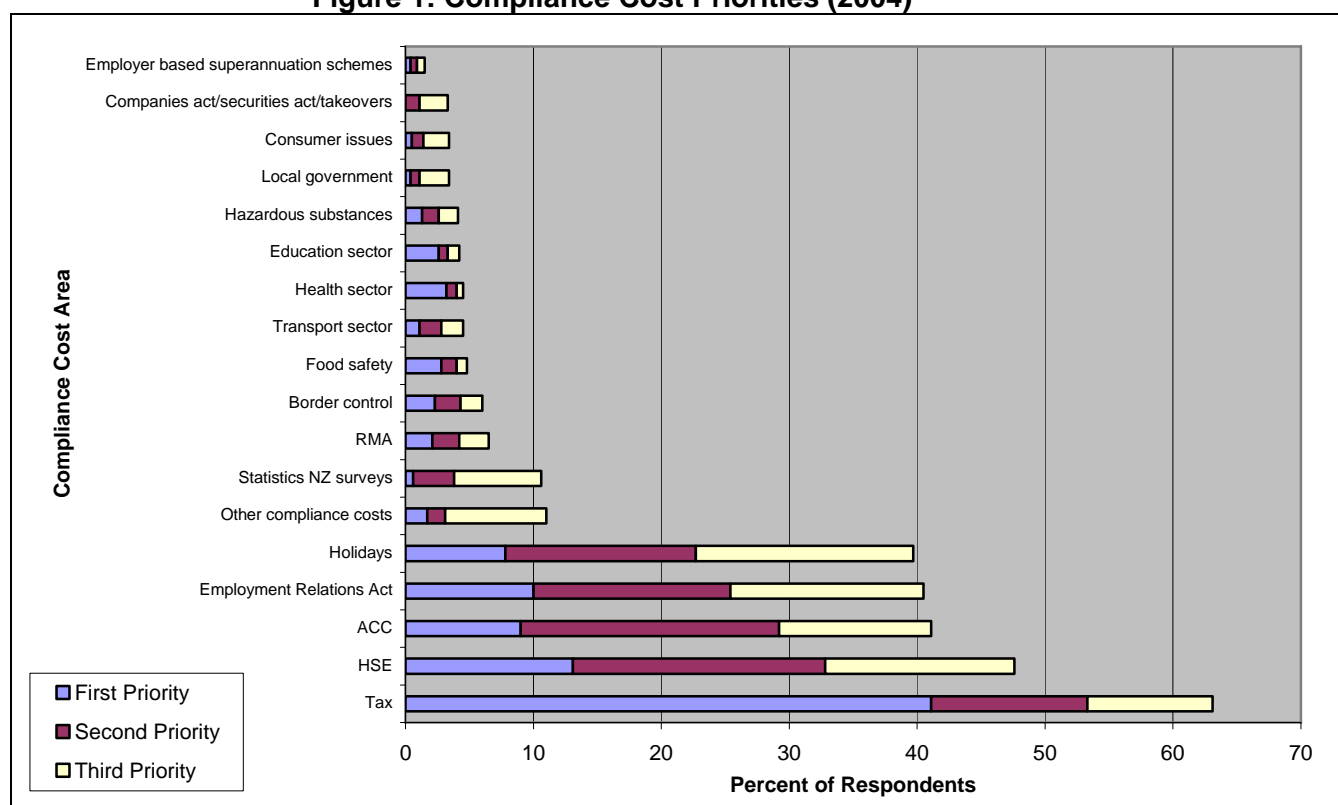
- Part A discusses the main findings concerning tax from the Business New Zealand KPMG Compliance Cost Survey;
- Part B discusses Business New Zealand's views on the main provisions in the Bill; and
- Part C discusses Business New Zealand's views on the other policy matter contained in the Bill.

## PART A – SUMMARY OF FINDINGS CONCERNING TAX FROM THE 2004 BUSINESS NEW ZEALAND – KPMG COMPLIANCE COST SURVEY

### 3. Tax as the Top Priority Concerning Compliance Costs

3.1 As in 2003, the 2004 Business New Zealand and KPMG ran their annual Compliance Cost (see [www.businessnz.org.nz](http://www.businessnz.org.nz) for a copy of the 2004 report). 949 businesses took part in the 2004 survey, covering a wide range of business sizes, industries and regions. Part of the survey asked respondents to assign their three highest priorities to a list of compliance cost areas. The results are shown in Figure 1 below.

**Figure 1: Compliance Cost Priorities (2004)**



**Table 46: Summary Comparison for Tax Compliance Costs (2003 & 2004)**

Overall trend (2004)	Small decrease	
Respondents answering this section (2004)	99.9%	
Internal cost trend (2004)	Small increase	
External cost trend (2004)	Small decrease	
Year	2003	2004
Average total cost	\$15,881	\$14,909
Average total cost per FTE	\$224	\$245
Average mean annual hours spent within enterprise on tax (all sizes)	316	323
Average internal cost	\$6,016	\$6,366
Maximum annual hours spent by enterprise internally on tax	40,000	100,000
Average external cost	\$11,836	\$11,296
Maximum annual amount spent by enterprise externally on tax	\$550,000	\$500,000
Tax as a % of total compliance costs	30%	34%
% of respondents who obtained information from Inland Revenue	78%	72%
% of respondents who employed external tax advisers	79%	74%
% of respondents who directly accessed tax legislation	42%	34%
% of respondents who used other publications and advice	36%	30%

Key findings:

- Consistent with 2003, tax remained the most popular choice for the first compliance cost priority. 41.1% of respondents selected tax, compared with 35.5% in 2003.
- Unlike 2003, 2004 saw tax as the top compliance cost when all three priorities were added together (63.1% in 2004 compared with 60.8% in 2003).
- As in 2003, tax compliance costs per FTE were high for small enterprises but fell to relatively modest levels once an enterprise employed more than 50 FTEs.
- The average total tax compliance cost per FTE fell as the number of FTEs increased.
- The largest fall in tax compliance costs per FTE was recorded for the 0-5 FTE group.
- In 2004, tax compliance costs represent over half of total compliance costs for the 0-5 and 6-9 FTE groups, and almost half of total compliance costs for the 10-19 FTE group, compared to the average of 34% overall.
- There was a decline in advice obtained from external sources across all sizes of enterprise.

3.2 Results of the survey continue to show that tax is a key compliance cost issue for businesses. Although the survey shows that from 2003 to 2004 the overall trend for tax compliance costs was a minor decrease, it is disappointing to see that it has increased its position as the top compliance cost priority. The Government will need to take future steps to ensure tax as a compliance cost priority does not continue to trend upwards.

## **PART B – BUSINESS NEW ZEALAND’S VIEWS ON THE MAIN PROVISIONS OF THE BILL**

### **4. Changes to the Tax Depreciation Rules**

- 4.1 Business New Zealand submitted to the Inland Revenue Department (IRD) in regard to the ‘Repairs and Maintenance to the Tax Depreciation Rules’ issues paper in September 2004. In it, Business New Zealand agreed that it was timely for a review of the depreciation rules to take place, particularly whether the current rules were reflecting the reality of economic life in times of rapidly advancing technology and ‘24-7’ business operations. We pointed out that depreciation rules should not result in investment decisions being made primarily for tax purposes. As a matter of principle, the tax system should be neutral and should not seek to favour certain types of investments or activities over others.
- 4.2 We did note that ‘retaining the revenue’ is not a good starting point for any review of depreciation rules, as this unprincipled approach had been taken across a number of recent reviews of the tax system. This has seen positive proposals being counterbalanced by negative ones in order to claw back lost revenue from the former. Also, depreciation rules need to be relatively simple and user-friendly, so that they do not impose significant compliance costs on businesses.
- 4.3 Regarding the tax depreciation treatment of patents in the Bill, Business New Zealand supports the change regarding the alignment of depreciation treatment so that the first allowable depreciation deduction includes depreciation for the period from the date the patent application was lodged to the date the patent was granted.
- 4.4 The Bill has also listed four proposed changes to the special depreciation rate rules in the Income Tax Act (ITA) 1994. Business New Zealand supports all four proposed changes. We also do not oppose the amendment to add plant variety rights and the right to use plant variety rights to the list of depreciable intangible property.
- 4.5 Business New Zealand agrees with the proposed amendment to the ITA that would allow an extension on the deduction for losses on buildings when a building has been destroyed or rendered useless for the purpose of deriving gross income owing to an event that is considered to be outside the control of a taxpayer, such as earthquakes and floods which are deemed to be ‘qualifying events’.
- 4.6 However, we would like to see this extension also include the voluntary disposal or destruction of a building. There may be justifiable reasons for the voluntary destruction of a building, such as the building becoming unsafe or poorly constructed, yet is not torn down for financial reasons. This would mean that buildings are not treated any differently to other forms of depreciable property.

- 4.7 *Recommendation: That the deduction for losses on buildings include voluntary destruction or disposal.*

## **5. Legal Professional Privilege for Tax Advice**

- 5.1 Business New Zealand agrees that accountants should be able to provide candid and independent advice to their clients without the need to disclose that advice to IRD, which is a position lawyers currently have. Privileged communications involving tax advice documents under the proposed changes would be one way in which to level the playing field between the accounting and legal professions.
- 5.2 While we support the overall move towards legal professional privilege for tax advice, Business New Zealand considers the proposals outlined to be very cautious, and quite technical. In particular, the requirement for a statutory declaration for the tax advisor is somewhat of an onerous and largely unnecessary compliance cost.
- 5.3 Furthermore, we do not consider the playing field between lawyers who give tax advice and accountants who give tax advice to be completely evened up by the introduction of the amendments. For instance, the Bill excludes factual background matters from not being disclosed, although lawyers are not obligated when claiming privilege to disclose such facts. Any statutory privilege for tax advice needs to include both the factual background information and the opinions or advice provided by an accountant.
- 5.4 *Recommendation: That statutory privilege for tax advice provided by accountants also includes factual background matters.*

## **PART C – BUSINESS NEW ZEALAND’S VIEWS ON OTHER SELECTED POLICY MATTERS OF THE BILL**

### **6. Tax Exemption for Petroleum Exploration and Development**

- 6.1 Business New Zealand supports moves by the Government to exempt non-resident companies and offshore petroleum fields from taxes on income earned from drilling exploration or development wells and from undertaking seismic survey work relating to petroleum exploration in New Zealand for a period of six years.
- 6.2 We agree that the current tax exemption period of 183 days is simply too short for any significant exploration to take place, which involves a sizeable cost on explorers to move their equipment to and from New Zealand. The costly moves by the companies to keep within the 183 day rule while at the same time not raising tax revenue for the Government does mean that an inefficiency in the tax regime exists.
- 6.3 While supportive of the move, we also request two further changes. The first being that the exemption is automatically given, rather than having to be applied for. The second change is that the exemption should also extend towards other non-resident contractors providing services associated with drilling and surveying, such as well testing and logging, which can also carry a

significant cost. This would lead to a more equitable solution and less disruption in the day-to-day running of such exploration projects.

- 6.4 *Recommendation: While the Bill's proposal that tax exemptions of non-resident companies for drilling exploratory or seismic survey work relating to petroleum exploration in New Zealand should proceed, Business New Zealand also recommends that the exemption is automatically given rather than having to be applied for, and that the exemptions apply to all services associated with drilling and surveying by non-resident contractors (i.e. well testing and logging).*

## **7. Tax Deductions for Business Environmental Expenditure**

- 7.1 Business New Zealand supports the proposal to clarify and update the rules on the treatment of environmental expenditure, along with the categories and the rate at which an amortisation deduction is available to business taxpayers when no other deduction is available. We also agree that the elimination of the distinction between industrial and non-industrial waste is a sensible step.
- 7.2 Our only concern with the proposal involves the interest rate paid on deposits from a restoration account that taxpayers can set up with the IRD. Given the current level of interest rates on deposits provided by financial institutions, the 3% proposed by the IRD seems very low, even by conservative standards. Business New Zealand would want to see this rate increase so that it is at least more commercially aligned.
- 7.3 *Recommendation: While the Bill's proposal that the categories and rates for deductible environmental expenditure as outlined in the Bill should proceed, Business New Zealand also recommends that the interest rate of 3% on deposits into a restoration account should be revised upwards to make it more commercially aligned.*

## **8. Publication of Tax Offenders' Names**

- 8.1 Business New Zealand fully supports the proposal that the Commissioner of IRD not publish the names of serious tax offenders. We deem the current requirement to be excessively harsh on taxpayers, especially those who evade for small sums, or one-off offenders. Although the reason behind the initial publication of names was to deter tax offending, the inconclusive evidence that it has succeeded when it was introduced in 1994 means its continued use is not warranted.

## **9. GST Deregistration for Non-Residents**

- 9.1 Business New Zealand strongly opposes the IRD's proposal that the Commissioner for IRD is given the discretion to deregister non-residents who do not carry on a taxable activity in New Zealand to prevent the inappropriate refund of GST on their purchases in New Zealand.
- 9.2 We oppose the proposal due to two reasons. The first is that we do not believe the current situation is leading to a serious problem in the first place.



The amount of lost tax revenue would no doubt be comparability insignificant to the total tax take.

- 9.3 The second and more important reason is that it would put New Zealand at a comparative disadvantage compared with say Australia who continue to allow non-residents to claim back their input tax credits. In particular, traditional sources of tourism revenue from conferences held in New Zealand for instance could easily be lost for the benefit of obtaining minimal GST revenue. The total economic growth effects of a conference held in New Zealand that provides revenue for a multitude of New Zealand businesses (whether it be directly through the conference venue or indirectly through individual guest tourist spending) would surely outstrip any extra tax revenue gains for the Government.
- 9.4 *Recommendation: The Bill's proposal to deregister non-residents who do not carry on a taxable activity in New Zealand should not proceed.*