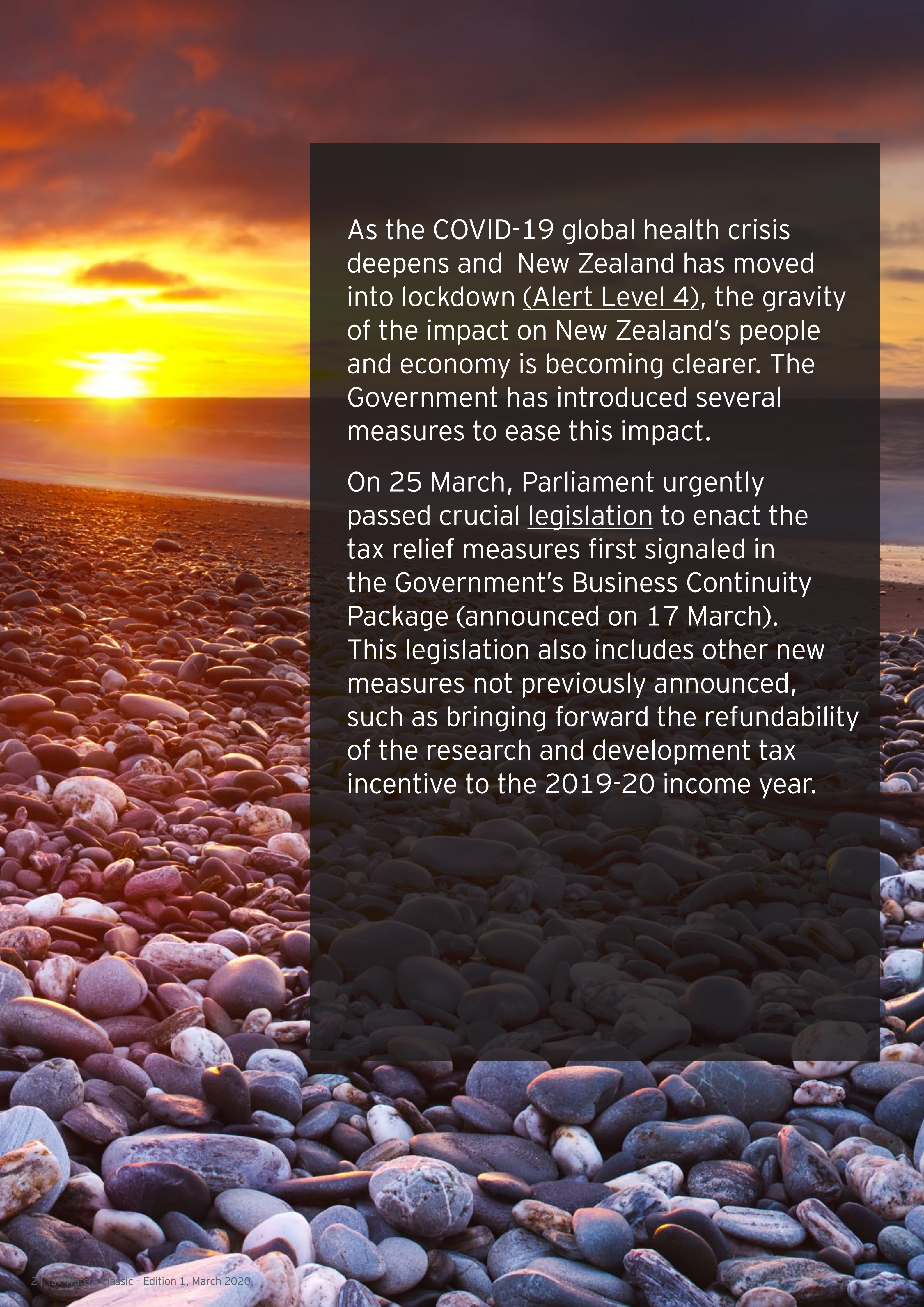
COVID-19 Special

Tax Watch: Classic Edition 1

March 2020

Building a better working world



As the COVID-19 global health crisis deepens and New Zealand has moved into lockdown (Alert Level 4), the gravity of the impact on New Zealand's people and economy is becoming clearer. The Government has introduced several measures to ease this impact.

On 25 March, Parliament urgently passed crucial legislation to enact the tax relief measures first signaled in the Government's Business Continuity Package (announced on 17 March). This legislation also includes other new measures not previously announced, such as bringing forward the refundability of the research and development tax incentive to the 2019-20 income year.

In this edition of Tax Watch, we provide an overview of key relief measures, including:

- Wage subsidies
- Specific tax-related measures, expansion of welfare support and other measures

We also include other matters that should be considered in relation to:

- Financial reporting impacts of building depreciation
- Customs and indirect tax
- Privacy law
- Corporate and contractual matters
- Estate and succession planning

The response to COVID-19 is evolving rapidly. Further assistance from the Government will be announced in the coming days and weeks and EY will keep you informed.

Next steps

While the world comes to grips with the full extent of the social, economic and trade disruptions, we recommend all businesses pause for breath and take stock before taking any action.

New Zealand's employment laws are unlikely to be amended in the short term. As such, it is important to consider existing employment obligations before making restructuring decisions.

Government authorities will also be feeling the pressure of lockdown as well as increased demand and uncertainty, and processing times are likely to reflect that. Considered action and patience will pay dividends in the long run.

We continue to interact with Government agencies, including Inland Revenue and Customs, on measures to help relieve the compliance burden on businesses and to otherwise help them, so they can focus on other key business requirements during this time.

Additional resources

The dedicated EY global COVID-19 website provides insights on responding to volatility and building enterprise resilience.

For any specific queries regarding COVID-19 please refer to the Ministry of Health's website, the Government's COVID-19 website or call Healthline on 0800 358 5453.

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Wage subsidy scheme

The wage subsidy scheme was introduced in the Government's Business Continuity Package (the Package). The scheme has since been expanded and refined, with the estimated cost lifting from $5.1 billion to $8-$12 billion.

The scheme represents a significant part of the Package and will assist many businesses. It's intended to help employers retain people in employment, even if there is no business activity during the lockdown.

Amount & application

Employers eligible for the subsidy will receive a flat rate of $585.80/week for employees working 20 hours or more per week ($350/week for employees working less than 20 hours per week). The subsidy is paid as a lump sum and covers 12 weeks per employee.

The subsidy was originally capped at $150,000 per business, limiting its value for larger employers. However, the evolving situation and move to lockdown has seen the Government remove this cap entirely.

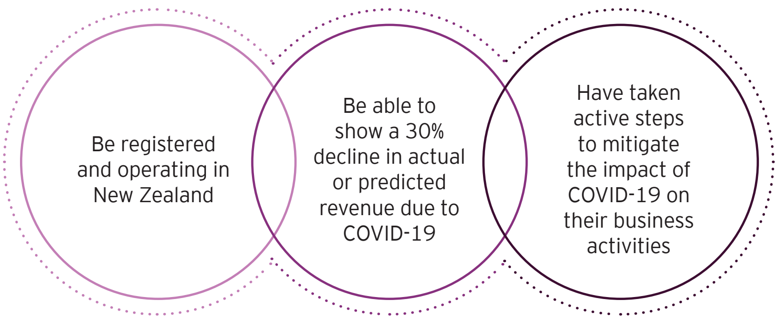
The subsidy is being administered by the Ministry of Social Development (MSD) – the application site is here.

Eligibility criteria

To qualify, businesses must:

- Be registered and operating in New Zealand with their employees legally working in New Zealand; and
- Be able to show a 30% decline in actual or predicted revenue due to COVID-19, over the period of a month, when compared with the same month last year (or a reasonably equivalent month for businesses less than a year old). The decline must occur between January-June 2020; and
- Have taken active steps to mitigate the impact of COVID-19 on their business activities (such as engaging with their bank, drawing on their cash reserves as appropriate, making an insurance claim, engaging with the Chamber of Commerce, industry association or the Regional Business Partner programme).

Sole traders and self-employed people may also be eligible for the subsidy, along with registered charities, non-governmental organisations, incorporated societies and post-settlement governance entities.



Obligations

In addition to meeting the eligibility criteria, employers must sign a declaration covering their obligations in relation to the subsidy.

These obligations include retaining the relevant employees and using best endeavors to pay them at least 80% of their pre-COVID income for the period of the subsidy. If that's not possible (for example when a business has no activity due to the shutdown and workers are not working any hours), employers must pass on at least the whole value of the subsidy to each affected worker. The only exception is if the employee's usual wages are less than the subsidy, in which case the employer must pay them their usual wages. Any difference is expected to be used for the wages of other affected staff.

The subsidy does not change employment law obligations and employees must be paid appropriately under their employment agreements for any hours worked during the lockdown.

Evidential requirements and audit process

Businesses should have documentation to support their declaration, including written consent from employees to share their information with MSD and proof of their consultations with banks and/or industry bodies.

Employers must notify MSD within 5 working days if anything changes that may affect their eligibility or entitlement to the subsidy. The subsidy must be repaid in certain situations, such as when an employer fails to meet any obligations about how the subsidy must be used or stops being eligible for the subsidy.

Cases of reported mis-use of the subsidy are being investigated and the Government is preparing an audit process to act as a backstop for the high-trust model. As a further integrity measure, a list of businesses receiving the subsidy will be made publicly available.

Income tax and GST treatment

Employers should process the payments as part of the employee's normal wages. All deductions (such as PAYE, KiwiSaver and child support) should be made as normal.

The employer is not liable for income tax or GST on the subsidies and will not be entitled to an income tax deduction for wages paid out of the subsidies.

Leave payments

Leave payments were previously available for employees required to self-isolate, or care for others in self-isolation. These additional payments were generally available in relation to all employees not able to work remotely and required to self-isolate.

However, the leave payment has now been folded into the wage subsidy scheme to prevent "double dipping" and is no longer available from 3pm on 27 March 2020. The leave payment scheme was designed at a time when only a few people were in isolation and is no longer fit for purpose under the Level 4 lockdown.

A sick leave scheme for essential workers is expected to be rolled out over the coming days.

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Tax and business cashflow measures, expansion of welfare support and other measures

Tax and business cashflow measures

The following tax relief measures have been enacted:

- Re-introduction of depreciation for non-residential buildings – Depreciation deductions at 2% diminishing value (1.5% straight line) will be reintroduced for new and existing industrial and commercial buildings from the 2020/21 income year. This change will immediately reduce provisional taxes payable. See below for information on related financial reporting impacts for taxpayers who recognise deferred tax in their financial statements.
- Provisional tax relief – The provisional tax threshold will increase from $2,500 of residual income tax (RIT) to $5,000 of RIT from the 2020/21 income year. This change will relieve approximately 95,000 taxpayers from the need to pay provisional tax. Affected taxpayers, who will now have longer to pay any amounts owing, will welcome this deferral.
- Use-of-money interest (UOMI) write off – New process to allow remission of UOMI charged on tax payments made by taxpayers "significantly adversely" impacted by COVID-19, will apply to debts arising on or after 14 February 2020. The new remission process will be in place for two years. Taxpayers must ask for relief and make payment as soon as practicable, although we expect Inland Revenue will take a pragmatic view of "as soon as practicable" given the circumstances. Taxpayers need to "ask" for the remission, meaning a written request is not necessarily required and a phone call to Inland Revenue or secure mail will suffice.
- Changes to the research and development tax incentive regime – Broad refundability for the R&D tax credit has been accelerated to the 2019/20 income year from the originally-planned 2020/21 income year. For reference, a business' refund would generally be capped at the amount of payroll-related taxes such as PAYE and FBT, paid in the same year. We are pleased to see the Government moved quickly on EY's proposal to bring forward R&D tax credit refundability. This change will help business R&D investment in the wake of COVID-19.
- Low value asset write-offs – The threshold that allows businesses to take upfront deductions for low-value assets has been lifted from $500 to $5,000 for assets purchased in the 12 months from 17 March 2020. The Bill also permanently increases the $500 threshold to $1,000 for assets purchased from 17 March 2021. This will reduce compliance costs for businesses and encourage the continuation of investment.
- Improved information sharing – Current information sharing settings have been relaxed to allow Inland Revenue to share information with other government departments to assist those agencies in their response to COVID-19.

Welfare support and other measures

Three main changes bolster welfare spending and support vulnerable individuals:

1
Main benefit increases from 1 April 2020.

2
Winter energy payment doubling for the 2020 period.

3
Removal of hours test for In Work Tax Credit from 1 July 2020.

Various other relief measures have either been enacted or announced, including:

- **Protection for tenants** – tenancies generally cannot be terminated, and rent cannot be increased, during the 3-month period starting from 25 March 2020.
- **Financial support package** for affected home owners and businesses, including:
  - **Business finance guarantee scheme** – seeking to underwrite business loans for SMEs.
  - **Mortgage payment relief** – A 6-month principal and interest payment holiday for mortgage holders and SME businesses.
- **Extension of visas** – certain temporary visas will be automatically extended until late September 2020.
- **Support for aviation** – A $600 million support package, including $330 million to help keep key air freight moving and ensure New Zealanders retain access to essential goods during lockdown.
- **Redeployment of forestry workers** – The Government has allocated $100 million to help redeploy affected workers, with the hard-hit region of Gisborne-Tairawhiti to be the first to receive assistance.

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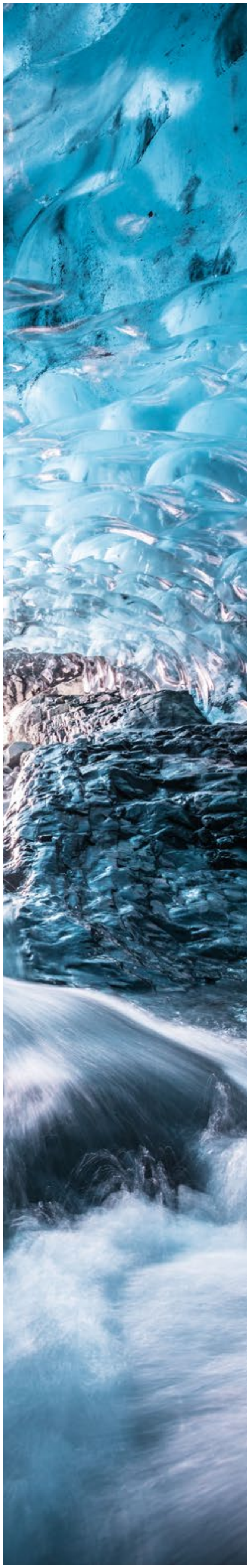

Reinstatement of tax depreciation on buildings – financial reporting impact

Tax depreciation on commercial and industrial buildings was removed from 1 April 2011. The reintroduction of 2% diminishing value (or 1.5% straight line) tax depreciation from the 2020/21 income year may have a significant impact on many entities preparing financial statements, in accordance with generally accepted accounting practice in New Zealand (NZ GAAP).

Under NZ IAS 12 Income Taxes, there are different consequences for businesses based on when a building was purchased. Generally:

- Buildings purchased before 2010 – prior to the 2010 depreciation removal, businesses held a carrying amount for accounting and had a related tax base for building assets. With the reintroduction of tax depreciation, businesses will likely now have a deferred tax asset at 28% of the reinstated tax base (2010-11 un-depreciated tax cost plus qualifying capital additions since then), requiring a net accounting adjustment.
- Buildings purchased after 2010 – given the relevant 0% tax depreciation rate on acquisition, the tax base of the asset was zero. With reintroduction of tax depreciation, the business will be able to claim the original cost of the building as the tax base plus qualifying capital additions made since then. However, NZ IAS 12 is not clear on how the adjustment should be recognised and businesses are likely to be required to make an accounting policy choice.

Broader impacts on other temporary tax differences (recognised tax losses and other temporary differences) could arise. Taxpayers in such situations need to consider the wider impact of the reinstatement of tax depreciation deductions on general deferred tax asset and liability recognition under NZ IAS 12.

The accounting impact of the reinstatement of tax depreciation deductions will need to be reported in financial statements prepared for reporting periods ending after 25 March 2020, such as March, June, September and December 2020 balance dates. For earlier balance dates, if deemed material, a non-adjusting subsequent event note disclosure may be required.

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Customs and indirect tax considerations

As global trade networks adapt to the daily changing impact of the border closures, importers and exporters should consider their options to relieve cashflow pressure from customs duties and indirect taxes.

It may be worth considering the following points:

- Putting in place deferred payment arrangements with Customs for imported goods or extending deferred payment arrangements – both of which can relieve cashflow for importers.
- Changing GST return filing frequency
- Expediting GST input tax credits and GST refunds
- Obtaining duty drawbacks (refunds) if possible for any goods that are returned overseas or destroyed due to being unused past expiry
- Using tariff concessions for imported goods. In this respect the Government is providing additional relief for critical goods (e.g., soap and testing kits). If you are concerned as to whether you are getting the benefit of concessions as an importer, you may want to consider using EY's Global Trade analytics to identify missed savings
- Seeking revised valuation rulings from customs authorities to reflect adjustments in transfer prices resulting from COVID-19 related disruptions globally.

If you are an exporter, assessing the customs relief measures that are being implementing in your export markets.

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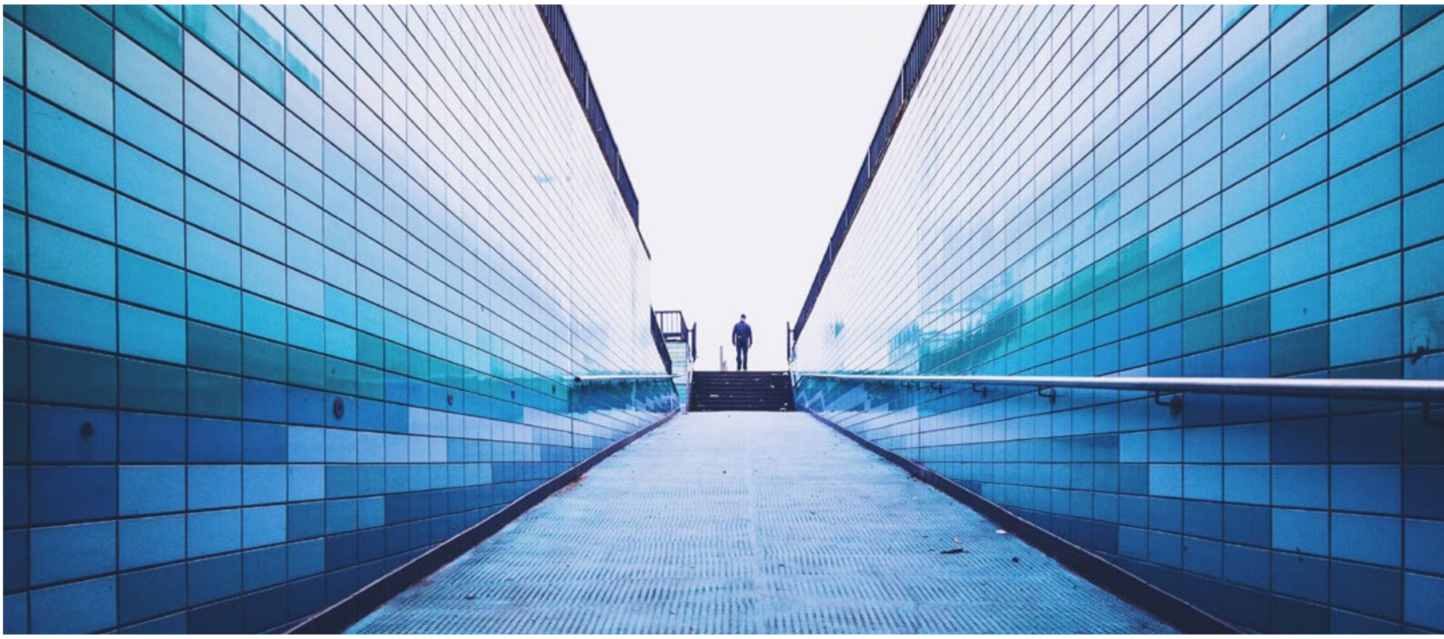

Privacy law considerations

Employers should take care to ensure they are not overlooking their privacy obligations to employees and others during COVID-19 challenges.

Under the Privacy Act 1993, there is a general obligation not to use or disclose personal information, unless an exception applies. One of those exceptions is if you believe the use or disclosure is necessary to prevent or lessen the risk of a serious threat to someone's safety, wellbeing or health. That exception **may** be available if an employee has COVID-19 and you need to protect the health of other staff. However, you should always take care to carefully assess the facts of each case to ensure you are not breaching the privacy of affected individuals.

If you don't need to identify the source of COVID-19 exposure, then you should avoid doing so.

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Corporate and contractual matters

With our borders closed to almost all travel and lockdown now in place, the pandemic's impact on businesses is already apparent.

It's worth considering issues such as:

- Suppliers and customers - What happens if your suppliers cannot meet your demands or if you cannot meet contractual obligations to your customers? Can your suppliers or customers use the pandemic to terminate their obligations to you? Do critical contracts require renegotiation?
- Corporate governance - Are you still able to hold board and shareholder meetings? Would remote meetings impact the company's tax residence? What duties do directors owe to shareholders and creditors if customers stop purchasing? What actions can directors take to reduce costs? How long can you continue to trade?
- Major transactions - What are the implications if you are a purchaser or a seller in a pending transaction? Does the pandemic change the due diligence that needs to be done on a business? Could it be deemed a material adverse event that allows a purchaser to cancel the transaction?

With developments occurring by the hour, it is difficult to predict with any certainty what may happen. A good starting point is to review the wording of your key contracts – asking do they address the consequences of the parties being unable to perform their obligations due to events beyond their reasonable control (often this will be in a clause headed force majeure)?

Planning ahead is key to ensuring your business is agile as it can be in these volatile times.

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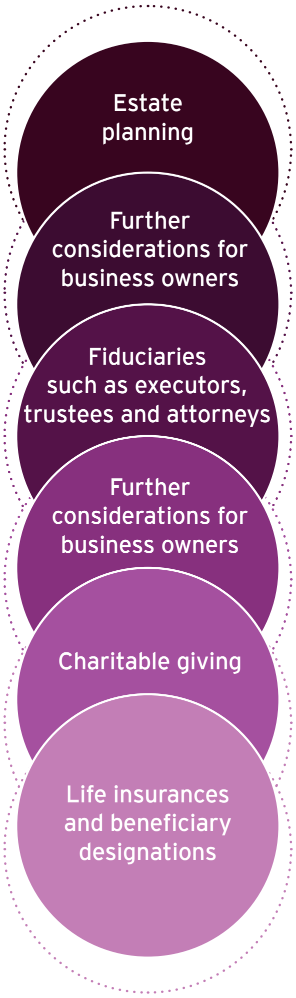
Estate and succession planning

COVID-19 presents some critical economic, social and health challenges – including risks to people's health, wealth, livelihoods and general quality of life.

These unprecedented times call for a review and assessment of:

- Estate planning – review any existing estate planning documents to ensure they are in order and up-to-date (wills, enduring powers of attorney and advance health care directives). If you don't have these documents in place, use this as an opportunity to ensure you and your loved ones are taken care of.
- Further considerations for business owners – consider who will take over your director and shareholder roles if anything were to happen to you, and ensure you make appropriate delegations both from a company law and private client perspective. It is essential to have an awareness of what roles you have and who the legal owners of the given property are - be it you personally, the company, or trustees of your family trust. This awareness is important because different laws dictate delegation of roles and management or succession of property.
- Fiduciaries such as executors, trustees and attorneys – if you are administering a deceased's estate, a trust fund or assets of a donor who appointed you as their attorney of significant size, you have a duty to manage these in the best interest of the beneficiaries or the donor. In an environment of uncertainty and financial downturn, these fiduciary duties shouldn't be overlooked.
- Charitable giving – if you want to donate funds to help fight COVID-19, consider whether your chosen charity is registered under the Charites Act 2005 and whether its purposes align with your intentions.
- Life insurances and beneficiary designations – consult with your life insurance brokers and review beneficiary nominations to ensure your life insurance policies and nominations are up-to-date and reflect current wishes.



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