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WEEKLY COMMENT: FRIDAY 3 JULY 2020

1. The *COVID-19 Response (Taxation and Social Assistance Urgent Measures) Act 2020* (the "first COVID-19 Tax Amending Act") received the Royal assent on 25 March 2020. The Act contains a number of tax changes including:

   (a) Repeal of the previous allowance for non-depreciable commercial buildings;

   (b) Depreciation deductions for non-residential buildings;

   (c) Increase in the low-value asset write-off threshold;

   (d) Removing the distinction between improvements on assets to which the 20% loading applied and assets to which it did not apply;

   (e) Use-of-money interest remission;

   (f) Increase in the provisional tax threshold; and

   (g) Research and development tax credits – broader access to refunds.

2. This week I will look at the fixed asset amendments and the use-of-money interest remission rules. Next week I will look at the increased access to R&D tax credit refunds.

Repeal of the allowance for certain commercial buildings

3. Section DB 65 of the *Income Tax Act 2007* has been repealed with effect from 1 April 2020. Section DB 65 provided a "de facto" depreciation deduction for fit out in a commercial building by treating 15% of the adjusted tax value of the building on 1 April 2011 (the date from which a 0% depreciation rate applied to buildings) as relating to fit out and allowing a depreciation deduction of 2% on that deemed fit out amount. This applied when fit out had not been separated out and separately depreciated.

4. With commercial buildings having become depreciable again from 1 April 2020 (see paragraph 5 onwards below) the allowance in s. DB 65 has been removed. If an allowance has been claimed under s. DB 65 on a commercial building, the adjusted tax value of that building on 1 April 2020 must be reduced by the cumulative allowances claimed between the 2011-12 and 2019-20 income years (see paragraph 13 below).

Depreciation deductions for non-residential buildings

5. Sections EE 31(2), and EE 31(3), which set the depreciation rate at 0% for a "building" acquired on or before 20 May 2010, or after 20 May 2010, respectively, will apply only to a "residential building" from the 2020-21 income year.

6. The term "residential building" is defined in s. YA 1 as:

   (a) Meaning a dwelling (defined in s. YA 1 as meaning any place used predominantly as a place of residence or abode, including any appurtenances belonging to or enjoyed with the place); and

   (b) Including a building intended to ordinarily provide accommodation for periods of less than 28 days at a time, if the building, together with other buildings on the same land, has less than 4 units for separate accommodation.

7. The term "non-residential building" is defined in s. YA 1 as meaning a building that is not a "residential building".

8. Taken together, the above amendments limit the application of the 0% depreciation for buildings to:

   (a) A dwelling; and

   (b) A building for providing short-term accommodation of less than 4 weeks at a time, if there are less than 4 units for separate accommodation on the same land.

9. Inland Revenue has stated in *Tax Information Bulletin* Vol. 32, No. 5, June 2020, ("the TIB Item") on page 3, that:

   "The definition of "dwelling" encompasses owner-occupied houses and apartments, and houses and apartments subject to residential tenancies.

   The second limb of the definition of residential building ensures there is certainty that the definition of "residential building" includes buildings such as a bach that the owner uses but also rents out on a short-term basis, and also buildings used exclusively for short-term accommodation provided by owners such as Airbnb properties. These may be within the definition of "dwelling", but this amendment puts beyond doubt that those buildings remain subject to the zero depreciation rate. The less-than four units provision excludes larger commercial premises such as motels from being treated as residential buildings."

10. An amendment to s. EE 35(2) will mean the prohibition on setting a special rate for a building will apply only to a "residential building" from the 2020-21 income year. Inland Revenue has noted in the TIB Item that this means that the ability to apply for and be granted a special depreciation rate from the Commissioner has been restored for non-residential buildings.

11. The depreciation rate that will apply to non-residential buildings will be 2% of diminishing value (DV) or 1.5% straight line (SL) based on an estimated useful life of 50 years. The Commissioner's Table of Depreciation Rates has been amended with effect from the 2020-21 income year onwards by s. 39 of the first COVID-19 Tax Amending Act.

12. The chosen depreciation rate is applied to the adjusted tax value (i.e. the opening tax book value) of a non-residential building at the beginning of the income year. The opening tax

book value is the "base value" less "deductions", calculated under sections EE 56 to EE 60. The definition of deductions in s. EE 60 has been amended so as to include the "total amount of previous deductions under section DB 65".

13. As explained in the TIB Item, for the 2020-21 year:

    (a) For buildings acquired after the end of the 2010–11 income year, the opening value for the 2020–21 income year is the:

        (i) Adjusted tax value at the end of the 2010–11 income year, less fit-out deductions taken under the section DB 65 transitional rule (if applicable); plus

        (ii) Non-deductible capital expenditure incurred on that building from the end of the 2010–11 income year to the start of the 2020–21 income year.

    (b) For buildings acquired after the end of the 2010–11 income year, the opening value for the 2020–21 income year is the:

    (i) Cost of the building; plus

    (ii) Non-deductible capital expenditure incurred on the building from the time it was acquired until the beginning of the 2020–21 income year.

14. The definition of "special excluded depreciable property" in s. EE 67, which essentially covered all buildings, and Schedule 39 which listed the exclusions from this definition (basically temporary structures), have been repealed, effective from the 2020-21 income year. The term has been replaced by "residential building" for which the depreciation rate remains 0%, under the amended s. EE 61(7B).

Increasing the low value asset threshold

15. Section EE 38 provides a deduction for an item of low value that would otherwise have to be depreciated, if the requirements of s. EE 38(1) are met, being that:

    (a) The cost of the item must not exceed the threshold value given by s. EE 38(2);

    (b) The item must be used or available for use in the income year;

    (c) The item cannot have been, and cannot become, part of any other depreciable property;

    (d) No deduction must be available for the item other than under s. EE 38; and

    (e) If the item is part of a group of items acquired at the same time from the same supplier, to which the same depreciation rate would apply, the total cost for all items in the group must not exceed the threshold value given by s. EE 38(2).

16. Section 8 of the first COVID-19 Tax Amending Act amended the threshold value in s. EE 38(2)(b) and inserted a new s. EE 38(2)(c) and EE 38(2)(d) as follows:

    (a) The $500 threshold in s. EE 38(2)(b) applies to items acquired on or after 19 May 2005 and before 17 March 2020;

    (b) A new temporary $5,000 threshold in s. EE 38(2)(c) applies to items acquired on or after 17 March 2020 and before 17 March 2021; and

(c) A new permanent threshold of $1,000 in s. EE 38(2)(d) apples to items acquired on or after 17 March 2021.

No distinction between improvements on assets with the 20% loading and other assets

17. Section EE 37 concerns depreciation of improvements to assets. In general, a person may:

    (a) Choose, under s. EE 37(4), to treat the item as a separate item of depreciable property; or

    (b) Choose, under s. EE 37(5) to treat the improvement as part of the depreciable property that was improved, by adding the improvement's adjusted tax value to the adjusted tax value of the depreciable property at the beginning of the year immediately following the year in which the improvement was made (assuming the improvement is immediately used or available for use).

18. There was an exception to this rule. If the 20% loading applied to the depreciable property that was improved because it was acquired on or before 20 May 2010, the improvement had to be treated as a separate item of depreciable property, under sections EE 37(3)(ab) and EE 37(3B).

19. This exception has been repealed, by s. 7 of the first COVID-19 Tax Act, with effect from the 2020-21 income year. Improvements made to property to which the 20% loading applies may be depreciated as part of the property that is improved, if the taxpayer chooses to do so.

Use of-money interest remission

20. Section 33 of the first COVID-19 Tax Act inserted a new s. 183ABAB into the *Tax Administration Act 1994*, which applies for a taxpayer if:

    (a) The taxpayer's ability to make a payment required by a tax law on or before the due date for the payment is significantly adversely affected by COVID-19; and

    (b) The due date for the payment is no earlier than 14 February 2020; and

    (c) The taxpayer is charged with use-of-money interest for failing to make the payment by the due date.

21. Section 183ABAB(2) provides that the taxpayer may ask the Commissioner to remit interest accrued after 14 February 2020 on the payment.

22. Section 183ABAB(3) provides that the Commissioner may remit the interest if:

    (a) The Commissioner is satisfied that the taxpayer:

        (i) Asked for the relief as soon as practicable; and

        (ii) Made the payment as soon as practicable; and

    (b) No more than 24 months have passed since 25 March 2020, the date on which s. 183ABAB came into force.

23. Sections 183ABAB(4) to (6) provide for an extension of the 24-month time frame if the ability of taxpayers to pay tax on time is likely to continue to be adversely affected by COVID-19.

24. Inland Revenue has stated in the TIB Item that:

    "The amendment allows Inland Revenue to remit interest on a late payment if the taxpayer's ability to make the payment on time was significantly adversely affected by the COVID-19 outbreak. …

    This includes both where a taxpayer has been physically unable to make a payment on time, for example, because they have been quarantined and do not have the ability to make the payment electronically while quarantined, and where a taxpayer's financial capability to make a payment on time has been adversely affected because of the economic impacts of COVID-19.

    For interest to be remitted the taxpayer must ask for it to be remitted and the Commissioner must be satisfied that the taxpayer has asked for the relief as soon as practicable and made the payment of tax as soon as practicable. The interest would not be remitted until the core tax debt has been paid."

25. At **ird.govt.nz/covid-19/manage-my-tax/penalties-and-interest** Inland Revenue has provided further guidance on how the remission of interest and penalties will be administered as follows:

    (a) It is the Commissioner's view that the customer has been significantly affected by COVID-19 financially where the customer's income or revenue has reduced because of COVID-19 and that because of that income or revenue reduction cannot pay their taxes in full and on time;

    (b) "As soon as practicable" will be determined on the facts of each case, however, the Commissioner considers the term will be satisfied so long as the customer applies for the relief at the earliest opportunity and agrees to, and completes, an arrangement that will see the outstanding tax paid at the earliest opportunity, or will be paid over the most reasonable period given the customer's specific circumstances;

    (c) Inland Revenue will not ask for that information in every case, but taxpayers should be able to provide, if asked at least three months banks statements and credit card statements, any management accounting information, and a list of aged creditors and debtors;

    (d) For businesses, Inland Revenue will be looking to understand the plan to sustain the business;

    (e) Relief will be available for both new debt due to COVID-19 (in the form of an instalment arrangement with or without a deferred payment start, partial write-offs and write-offs due to serious hardship) and existing debt for which an instalment arrangement can be renegotiated.

Increase in the provisional tax threshold

26. The threshold for paying provisional tax has been permanently increased from $2,500 to $5,000 from the 2020-21 income year onwards. Various amendments to provisions in subpart RC have been made to effect this.

27. For taxpayers with residual income tax of between $2,500 and $5,000, instead of paying provisional tax throughout the income year, they will now only have to pay by 7 February following the end of the income year.

Arun David, Director,
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