

Taxation Treatment of Non Resident Partnership Investors

Introduction

Tax law is inherently complex and often dependent on a taxpayer's personal circumstances. The position is further complicated when the taxpayer is a 'non resident'. These Notes are therefore intended as a guide only and reflect Forest Enterprises' understanding and interpretation of the applicable New Zealand tax laws and the professional advice we have obtained.

Although some general indications are provided as to the likely taxation treatment of non residents forestry transactions in their country of residence, you are encouraged to seek advice from your own taxation adviser to clarify the position specific to your circumstances and your country of residence.

Definition of a Non-Resident

A person is a non-resident for New Zealand taxation purposes if he or she:

- is away from New Zealand for more than 325 days in any 12 month period, or
- is in New Zealand for less than 183 days in any 12 month period, and

does not have an enduring relationship with New Zealand such as a permanent place of abode.

There are separate rules for determining whether a company or trust is a non-resident.

Partnerships and Taxation

Under New Zealand law, a partnership is not a separate legal or taxation entity therefore all taxation consequences rest with the individual Partners' both 'taxable losses' (in the years before harvest) and 'taxable profits' (during harvest).

Non Residents and the New Zealand Inland Revenue

Any non-resident who receives New Zealand derived 'income' must file a Non-Resident New Zealand Tax Return (IR3NR) with the New Zealand Inland Revenue Department (IRD). In this taxation context, 'income' is defined to capture both 'taxable profit' and 'taxable losses'. If a non-resident's only New Zealand income is from interest, dividends or royalties that have had Non-Resident Withholding Tax (NRWT) deducted at source at the correct rate, a Tax Return need not be filed.

A non-resident forestry Partner will therefore probably be required to file an IR3NR every year of their investment as in all years they should have tax losses (even if only from the rates, insurance, management fees etc), including during the harvest years (see below for details on the special taxation treatment of harvest income).

Tax Losses – New Zealand Tax Position

New Zealand tax law defines most expenditure incurred in the establishment, tending and management of a Radiata pine plantation forest as a deductible expense. During the years preceding harvest the partnership will therefore normally make a net loss. At the end of the accounting year, each Partner is allocated their pro rata share of this loss and must account for it individually with the IRD.

As noted earlier, a non-resident is required to file a return as the definition of income captures losses and the New Zealand IRD has the power to charge late filing fees. It is unlikely the IRD would take punitive action against a non-resident not filing a return if their only New Zealand taxable activity was a forestry loss (as there is no tax lost to the New Zealand IRD).

If a non-resident has New Zealand income other than interest, dividends or royalties, their share of the partnership loss can be deducted from this other income and consequently reduce the non-residents New Zealand tax liability.

The Partnership Tax Return filed annually by Forest Enterprises with the New Zealand IRD discloses the forestry tax loss allocated to individual Partners.



Tax Losses – Country of Residence Tax Position

As noted in the Introduction, the treatment of a non-resident's New Zealand forestry transactions in their country of residence is a matter each Partner should seek their own advice on. In general terms, we would expect New Zealand forestry losses to be either deductible in a Partner's country of residence or capitalised and carried forward for future deduction against the forestry income from harvest.

Harvest Income – New Zealand Tax Position

For New Zealand tax purposes, income from the harvesting of trees is classified as a royalty. Certain types of income, including royalties, require the deduction of NRWT when paid to non-residents.

A non-resident forestry partner therefore receives their share of the harvest proceeds net of the deduction of NRWT. NRWT on royalties is currently 15% of the 'income', unless New Zealand has a Double Tax Agreement (DTA) with the non-resident Partner's country of residence and that DTA includes income from the exploitation of trees within the definition of royalty. Currently all DTA's specifically exclude income from the exploitation of trees therefore the rate is 15%.

'Income' is taken to be the proceeds from the sale of the harvested trees (the logs) net of the direct harvest costs (all costs to the point of sale but excluding Forest Enterprises harvest management fee). The resulting 'income' is referred to by forestry people as the net stumpage.

At the end of each tax year, non-residents receive a IR67 Certificate from Forest Enterprises detailing the apportioned amount of the gross harvest revenue (royalty) for the year and the non-resident withholding tax deducted. Forest Enterprises files a copy of the IR67 Certificate with the New Zealand IRD.

At the end of the accounting year, each Partner is allocated their pro rata share of the Partnerships net profit from the harvest and the Partnership's Tax Return filed discloses each Partner's share plus any interest income.

As noted earlier, if a non-resident's only New Zealand income is from harvest revenue (and as this is treated as a royalty and therefore has NRWT deducted at source), there is no further New Zealand tax liability in respect of this income and provided the non-resident has not derived any other New Zealand 'income', a Tax Return is specifically not required.

Technically the non-resident is still required to file a return to account for the forestry loss and any interest income, however it is unlikely the IRD would take punitive action against a non-resident not filing a return in this circumstance (as there is no tax lost to the IRD).

As NRWT is a final tax, it is not refundable in whole or part. Any other New Zealand losses available to a non-resident (forestry losses carried forward, 'Cost of Bush', or losses from other sources) cannot be offset against their harvest income.

Harvest Income – Country of Residence Tax Position

As noted in the Introduction, the treatment of a non-resident's New Zealand forestry transactions in their country of residence is a matter each Partner should seek their own advice on.

In general, we would expect the New Zealand forestry income together with the current year losses (share of forestry costs) to be declared by the non-resident in their country of residence within their worldwide transactions.

The income declared by the non-resident Partner will be their pro rata share of the Partnership's profit for the year plus any interest income. The resulting taxable income will be subject to country of residence tax at the Partner's applicable tax rate. Provided a DTA exists with New Zealand, the amount of NRWT paid in New Zealand (as per the IR67) will then be deducted from this calculated liability and the balance will be the tax payable in the country of residence. The nature of DTA's is that the tax already paid overseas counts as a credit against any tax payable locally (in the country of residence).

If the resulting 'tax payable' is negative (i.e. more tax has been paid in New Zealand than the local tax payable), it is not usual for the overseas tax paid to be refundable as this would represent the local government repaying tax collected and retained by another country.

Interest Income – New Zealand Tax Position

Partnerships may or may not have tax deducted at source from interest income depending upon whether they have successfully applied for an exemption. At the end of the accounting year, each Partner is allocated their pro rata share of interest income earned (separate from the forestry losses/harvest revenue) together with any tax deducted at source and must account for the income (and tax deducted) individually with the New Zealand IRD.

As noted earlier, a non-resident forestry Partner is required to file a New Zealand Tax Return when they have tax losses or tax income. Interest income results in a second obligation for filing a Tax Return and an associated liability on the non-resident to pay NRWT on their interest income at the applicable rate (or receive a refund if the tax deducted at source exceeds the applicable NRWT rate). The Partnership Tax Return filed annually by Forest Enterprises with the IRD discloses by individual Partner their share of the interest income and tax deducted at source (in addition to the forestry tax loss/income).

Interest Income – Country of Residence Tax Position

As noted in the Introduction, the treatment of a non-resident's New Zealand forestry transactions in their country of residence is a matter each Partner should seek their own advice on.

In general, we would expect interest income (together with their share of the current year Partnership profit or loss) to be declared by the non-resident in their country of residence within their worldwide transactions.

The interest income will attract country of residence tax at the Partner's applicable tax rate. The New Zealand NRWT paid on this income, will be accounted for as a credit against any country of residence tax payable, provided a DTA exists with New Zealand.

Cost of Bush - New Zealand Tax Position

Under New Zealand Tax law, the amount paid for existing trees in a forestry partnership becomes what is called 'Cost of Bush'. The 'Cost of Bush' carries forward, in theory to be available for deduction against the harvest revenue as it is received. As noted earlier, harvest income paid to non-residents is treated as a royalty and has NRWT (a final tax) deducted. As a consequence, any 'Cost of Bush' deduction carried forward to harvest is not utilizable by a non-resident in New Zealand.

Cost of Bush – Country of Residence Tax Position

As noted in the Introduction, the treatment of a non-resident's New Zealand forestry transactions in their country of residence is a matter each Partner should seek their own advice on.

In general, we would expect that the 'Cost of Bush' amount would be recognized by the non-resident Partner in their country of residence within their worldwide transactions and be available either as an immediate deduction or as a loss carried forward for deduction against the harvest revenue when received.

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