

**April 2011**

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Trading in Australia Using a  
NZ Look Through Company

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In this LawBrief we briefly outline some key tax pointers for New Zealand operations trading in Australia, including the new look through company option.

If you have any comments on this LawBrief or suggestions for future topics please contact Keith Turner on (09) 309 6505 or email [keitht@nsatax.co.nz](mailto:keitht@nsatax.co.nz).

## Trading in Australia

Limited Liability is desirable when trading in a foreign country, yet in a Trans tasman operation the use of a subsidiary or branch operation will impact negatively in terms of the overall effective rate of tax on shareholder returns. The problem is double taxation and this arises in a cross border context because New Zealand does not recognise Australia's franking credits and likewise Australia does not recognise New Zealand's imputation credits. Franking/imputation credits represent credits for tax paid at the company level, and are attached to dividends as a credit for the shareholder.

Notwithstanding that foreign dividends derived by New Zealand companies are exempt income and no longer subject to foreign dividend withholding tax, and that there is an active income exemption for interests in controlled foreign companies (Australia has its own separate exemption), tax is paid at the corporate level in the foreign jurisdiction, and when those profits are distributed there are no imputation credits to attach to dividends so that withholding tax has to be deducted at 33%.

The effective tax rate on final distribution is 53% for a New Zealand subsidiary or branch operating in Australia. Typical methods for alleviating double tax are to extract monies pre tax by way of management fees (subject to transfer pricing rules), royalties (withholding tax) or interest (withholding tax and thin capitalisation rules apply).

For a lower effective tax rate the alternatives are to use a trust or limited liability partnership ("LLP"), or potentially a new look through company ("LTC"), which is available from 1 April 2011.

The effective tax rate for a New Zealand trust trading in Australia will be 45% which is the top Australian personal marginal tax rate, which they apply to trusts in Australia. The Australian tax paid at 45% will be available as a credit against New Zealand's trustee income tax rate of 33%, with any excess tax credit simply falling away. Limited liability can be achieved by using a corporate trustee.

However, trust structures may not be suitable for larger operations, where there are a diverse group of shareholders, or where shareholders will likely enter and exit the business.

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An LLP would provide the same effective tax rate as a trust if the limited partners are trusts. LLP's do potentially involve a greater set up cost (partnership deed) as well as further administration costs – e.g. another set of accounts. There are also restrictions on who can provide management services.

A New Zealand LTC is able to operate overseas as a branch and derive foreign income without affecting its LTC status. An LTC is, of course, easily established and as it is a fiscally transparent entity for tax purposes the double taxation issue with Australian franking credits does not arise. With New Zealand trusts or individuals as shareholders the effective tax rate is just 33%.

The branch of the LTC will be taxed as a corporate in Australia at 30%, and the shareholders claim that as a credit against their 33% New Zealand trustee income tax liability. With the benefit of limited liability, this structure offers advantages, whether operating alone or in partnership/ joint ventures with Australian entities.

It would be worth exploring whether this structure may alleviate Australian capital gains tax on the eventual sale of the business by a share sale. However, a sale of shares in an LTC constitutes a sale of the underlying assets for New Zealand tax purposes, and New Zealand income tax may arise.

The other issue to watch out for is that the LTC cannot be treated as a foreign company (e.g. where the mind and management is exercised in Australia), so some governance procedures need to be adopted.

You may be aware of the thin capitalisation rules – where a non resident debt funds a New Zealand subsidiary at such a level that IRD regards this as extracting excessive interest. If that applies, the New Zealand company's interest deduction will be reduced.

We now have the fat capitalisation rules, which apply in reverse, where a New Zealand resident shareholder "over" debt funds a foreign entity from New Zealand and equity finances, from offshore. Again the New Zealand company's interest deductions claimed here will potentially be subject to limitation.

**Seminars**

Attached are details of upcoming seminars. Readers may well be interested in the seminar on the tax implications of litigation.

**Disclaimer**

This newsletter is not intended to provide an exhaustive or comprehensive statement of tax law and it should not be relied on or used as the basis for any decision or legal action. Detailed professional advice should always be sought in order to verify the applicability of the relevant legislation to the specific case.