PrimeGlobal

An Association of Independent Accounting Firms

DOING BUSINESS IN NEW ZEALAND

COMPANY FORMATION IN NEW ZEALAND

MAIN FORMS OF COMPANY/BUSINESS IN NEW ZEALAND

New Zealand (NZ) has a number of business structures available to both residents and non-residents alike, the most commonly used being the limited liability company. Alternatives are the sole trader model, partnerships (both limited and unlimited) and trusts.

SPECIFIC TAX CONCERNS RELATED TO ESTABLISHING A COMPANY

The primary tax issue to consider when incorporating a NZ company, is the requirement for the entity to then pay income tax on worldwide income, although this exposure may be reduced to taxation on NZ sourced income only via the application of a double tax treaty agreement (DTA).

The standard income tax year in NZ ends on 31 March, although approval for off-March balance dates may be sought, particularly where there is a desire to align the NZ entities balance date with an offshore parents, for example.

A company must file an annual return of income to the Inland Revenue Department (IRD) by 7th July each year, unless the company utilises a registered tax agent, in which case the due date for filing may be extended to the 31st March of the following year.

The NZ company tax rate is presently a flat 28%. In this regard, NZ has a full imputation system, which essentially acts to reduce exposure to double taxation when shareholders receive dividends from the company. The imputation system usually only benefits NZ resident shareholders however, as most foreign jurisdictions do not recognise the imputation credit as a foreign tax credit claimable against any domestic taxes payable on the dividend received by their resident. Consequently care is required when establishing a presence in NZ, to ensure that the structure to be used provides the best return for any non-resident investors.

Most NZ companies are provisional tax taxpayers, which require the company to pay income tax in advance of the actual liability for the income year being determined. Payments are made on the 28th August, 15th January and 7th May, with any residual payment, referred to as terminal tax, due for payment on the following 7th April.

NZ has a non-resident withholding tax (NRWT) regime, which for a company usually creates an obligation to deduct a withholding tax from any dividends paid to non-resident shareholders. The standard NRWT rate on dividends is 33%, although that rate may be reduced by the provisions of an applicable DTA, including to a 0% rate where the company has fully imputed the dividend.

Losses incurred by a NZ company can usually be carried forward to the next income year or offset against profits of company's within the same tax group, which requires 66% common ownership. There are shareholder ownership continuity requirements with respect to tax losses and imputation credits, which if not met will result in the forfeiture of carried forward balances.

NZ has a value added consumption tax known as Goods and Services Tax (GST) which is imposed at the rate of 15% on supplies of goods and services consumed in New Zealand. A business must register for GST if it has annual taxable supplies (turnover) of NZ$60,000 or more. GST returns are required to be filed to the IRD either monthly, two monthly or six monthly (subject to defined criteria). Any GST payable is usually due on the 28th day of the month following the end of the relevant taxable period.

LEGAL ISSUES RELATED TO ESTABLISHING A COMPANY

The Registrar of Companies (commonly known as the NZ Companies Office) is responsible for overseeing and ensuring compliance with NZ company legislation by all companies (both domestic and foreign) registered as carrying on business in NZ.

To incorporate a NZ company, the desired company name must first be reserved (and approved by the Registrar) and the relevant incorporation documents must be completed and registered. A NZ company must have a NZ registered office and address for service, and the company must have at least one director who ordinarily resides in NZ or alternatively at least one Australian resident director who is also a director of an Australian company.

Once a NZ company has been incorporated, it has certain on-going filing obligations with the Registrar, which include the filing of an annual return. The annual return is essentially a confirmation that all current information surrounding the company held by the Registrar is up to date, although depending on the size or nature of the company's ownership, it may also require the filing of audited financial statements.

CULTURAL CONCERNS RELATED TO ESTABLISHING A COMPANY

New Zealand is a multi-ethnic country, comprising around 68% of people of European descent, 15% Maori (tangata whenua, the indigenous people), 10% Asian and 7% Pacific peoples. This ethnic diversity is projected to increase, with the Asian population in particular increasing to 14% over the next 15 years.

Business is generally conducted in English; however, some businesses which are substantially owned by Maori may use Maori in their day to day dealings with other Maori speakers. These businesses commonly produce their publications in both English and Maori. Government Departments also publish in both these official languages and other commonly used languages such as Mandarin, Hindi, or Samoan. Many recent immigrants, of course, still operate in their first language where they can.

There are generally no cultural concerns that need to be taken into account in terms of the establishment of a company in NZ itself. However naturally the reason a NZ presence is being established and the likely business to be undertaken in NZ by the company may have cultural implications for which specialist advice may need to be sought at some point in the future.

OTHER COUNTRY-SPECIFIC ISSUES RELATED TO ESTABLISHING A COMPANY

The Overseas Investment Office must consent to an acquisition by an "overseas person" of "sensitive land", "significant business assets" or fishing quota. "Sensitive land" includes non-urban land with areas greater than 5 hectares. "Significant business assets" includes 25% or more of a business where the consideration paid for the New Zealand part of the investment exceeds NZ$100 million.

PERMANENT ESTABLISHMENT IN NEW ZEALAND: BRANCH OR SUBSIDIARY?

DEFINITION OF A PERMANENT ESTABLISHMENT

Non-residents that are resident in a jurisdiction with which New Zealand has a double tax treaty agreement (DTA) are generally exempt from New Zealand income tax in respect of any business profits derived from New Zealand, provided there is no permanent establishment (PE) in NZ.

Article 5 of most of NZ's DTA's defines what is considered to be PE, and the concept generally relates to the foreign enterprise having a fixed place of business in NZ through which its business operations are wholly or partly carried on. The definition commonly includes, but is not limited to, a place of management, a branch, an office, or a factory.

The PE definition is often extended to include scenarios where the foreign enterprise is performing services in NZ through an individual who is present in NZ for more than 183 days or in respect to one project or a series of connected projects exceeding that timeframe.

Finally, often where a dependent agent of the foreign enterprise has an authority to substantially negotiate or conclude contracts in NZ, a PE will be deemed to exist in NZ.

Article 5 also lists several exclusions from the PE definition, including but not limited to:

- the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;
- the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;
- the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise;

For non-residents who reside in a jurisdiction with which NZ does not have a DTA, it is likely that the DTA PE definitions are still likely to be considered in the first instance, when determining whether or not a NZ PE exists.

DEFINITION AND MAIN DIFFERENCES BETWEEN A BRANCH AND A SUBSIDIARY

From a NZ perspective, a branch is often viewed as a foreign enterprise undertaking its operations in NZ through a PE. There is no legal separation between the foreign enterprise and its NZ branch operation. In other words, it is seen to be one single trading entity, undertaking its business activities in more than one jurisdiction.

A NZ subsidiary however is viewed as being a separate legal identity to its foreign parent company. Often the subsidiary will be a NZ company, specifically established to undertake the NZ business operations.

TAX AND ACCOUNTING OBLIGATIONS

Regardless of whether a branch or subsidiary structure is used, NZ income tax will be imposed on any income deemed to have been sourced from NZ, although such taxation may be restricted via the application of any relevant DTA provision.

Where a branch structure is used, the foreign enterprise will need to file a NZ income tax return annually in respect to any profit attributable to the NZ branch operation. Since the branch and the foreign enterprise are one of the same, there is limited ability under a branch structure to reduce the NZ profit through utilising various transfer pricing mechanisms, such as royalties fees for use of the enterprises intellectual property rights, interest charges on capital used to finance the NZ operation or management fees charged on a cost plus basis.

A subsidiary structure can utilise such transfer pricing strategies although robust transfer pricing documentation should be prepared in this regard, as the NZ IRD is clearly focused on mechanisms such as these being used by foreign enterprises to limit the level of NZ income taxes paid. The subsidiary must also file an annual NZ income tax return.

The profit of either structure is taxed at the company tax rate of 28%.

Under a branch scenario, the 28% is a final tax on the profit and what then happens to the tax paid profit in the foreign jurisdiction is of no interest to the NZ IRD.

Under a subsidiary structure however, any distribution of the tax paid profit during the lifetime (pre liquidation) of the company is considered to be a dividend. Where the shareholders are NZ residents, a resident withholding tax of 5% must be deducted from the dividend at the time of payment and paid to the IRD. Where the shareholders are non resident, non resident withholding tax at a rate between 0% and 33% must be deducted at the time of payment and paid to the IRD (rate dependent on number of factors).

Annual financial statements are, as a matter of course, prepared for NZ company's, although depending on whether the branch or subsidiary is "large" (as defined) will determine the exact nature of the financial statements that are required to be prepared, whether they are required to be audited and whether they are required to be filed with the NZ Companies Office. In addition, the nature and size of the trading entity will determine what level of NZ financial reporting standards must be applied in the preparation of any financial statements.

REGISTRATION FORMALITIES

An overseas company can set up a branch in New Zealand as long as it registers with the NZ Companies Office on the overseas company register within 10 working days of commencing business in New Zealand.

Incorporation of a NZ subsidiary company can be completed by following the process outlined on the NZ Companies Office website (https://www.business.govt.nz/companies/) for incorporating a company. This process involves initially seeking name approval for the NZ company, and once obtained, filing various incorporation documents such as director and shareholder consents. A NZ company must have a NZ registered office and address for service, and there must be at least one NZ resident director or alternatively one Australian resident director who is also a director of an Australian company.

Registration for various NZ taxes such as income tax and GST, can be completed via the IRD website (http://www.ird.govt.nz/).

STANDARD LEGAL OBLIGATIONS AND FORMALITIES FOR A BRANCH

An overseas company that operates a NZ branch must file separate audited financial statements, with the NZ Companies' Office, in respect of both the entity itself and the NZ branch operation, if it is a "large" overseas company. These must be filed within 5 months after balance date each year. Large is defined as having any two of the following: total assets of more than NZ$20million, revenue of more than NZ$10million per year or more than 50 employees.

HOW TO HIRE MY FIRST EMPLOYEE IN NEW ZEALAND

MAIN LEGAL STEPS TO FOLLOW TO HIRE A FIRST EMPLOYEE

Employers are required to register with the New Zealand Inland Revenue Department (IRD) and deduct pay as you earn (PAYE) tax for wages, salaries and taxable allowances paid to employees who are subject to New Zealand tax. Consequently, non-resident employers with employees working in New Zealand must register and deduct PAYE unless the employee is exempt from New Zealand tax in accordance with domestic law.

Employer registration can be completed online on the IRD website. PAYE must be paid to IRD monthly on the 20th of the following month.

An employment agreement should be signed by both parties prior to employment commencing. The employee must provide their employer with their IRD number. They must also tell their employer if they are in Kiwisaver. (see below for more details on the scheme.)

DESIGN AND CONTENTS OF AN EMPLOYMENT CONTRACT

A visa or work permit is required for a person to work in New Zealand unless they are a New Zealand citizen or holder of a New Zealand resident or permanent resident visa or an Australian citizen or Australian permanent resident or exempt from the requirement to hold a permit to be in New Zealand. Key employees of a business that wants to relocate its operations to New Zealand may be eligible for a work visa and, later, for residence under the Employees of Relocating Businesses Category. Employers in New Zealand who wish to recruit from overseas must provide evidence that there are no suitable New Zealand applicants for the job.

The Employment Relations Act (together with the Human Rights Act 1993) prohibits discrimination against employees on the grounds of sex, marital status, religious or ethical belief, colour, race, ethnic or national origin, disability, age, political opinion, employment status, family status, sexual orientation, and participation or involvement in the activities of a union as a union official or as a member. Where foreign language proficiency is required it is quite acceptable to advertise a job position where this is necessary.

In New Zealand the relationship between employer and employee should be documented by an employment agreement. Employment agreements may be individual (personal to the individual employee and employer) or collective (covering a group of employees and entered into between one or more unions and employers). Employers can specify in the employment agreement a "trial period" of up to 90 days and certain technical requirements must be complied with for the "trial period" to be effective. If an employee is dismissed during this trial period, he or she cannot bring a personal grievance or other legal proceedings in respect of the dismissal. However, employees on trial periods are still protected against discrimination, sexual and racial harassment, duress, or unjustified action by an employer.

The present adult minimum wage rate (before tax) for employees aged 16 or over is $15.25 per hour ($610 for a 40-hour week). There are some exceptions to this for young people in their first job or training. By law, employers must pay at least the minimum wage - even if an employee is paid by commission or by piece rate. The minimum wage applies to all workers aged 16 years or older, including home workers, casuals, and temporary and part-time workers.

There are no compulsory superannuation savings schemes in New Zealand, although the voluntary KiwiSaver superannuation regime requires a compulsory contribution from employers of 3% of the employee's gross salary or wage where the employee is a registered member of a KiwiSaver scheme. Upon starting with a new employer automatic enrollment in Kiwisaver will occur for an employee over the age of 18. They will then need to opt out if they do not wish to continue. Employer contributions are generally subject to employer superannuation contribution tax (ESCT) at the employee's marginal tax rate. These deductions must be paid to the IRD along with PAYE deductions.

There are 11 statutory public holidays in New Zealand. Under the Holidays Act 2003, employees are entitled to a minimum of four weeks annual leave after the first year of employment. Payment for annual leave is at the employee's average weekly earnings over the 12-month period before the leave is taken. Also after six month's service the employee is entitled to bereavement leave of three days on the death of an immediate family member and of one day in all other circumstances where the employer accepts that the employee has suffered bereavement.

For most employees, there is a minimum provision of five days paid sick leave after the first six months of continuous employment. An additional five days paid sick leave accrues from that point on, after each subsequent 12 month period. Employment agreements can provide for more generous sick leave provisions.

There is no statutory right to any redundancy payment under New Zealand law. Entitlement to any redundancy payment depends on the relevant employment agreement. It is common to expressly exclude any right to redundancy pay in employment agreements, although notice of termination for redundancy must be given.

Maternity leave of up to 18 weeks is available for employees with six months' continuous service. Paid parental leave (funded by the Government) provides payment for the 18 weeks leave upon the birth of a child or adoption of a child under the age of six.

Most non cash employee benefits such as an employer provided motor vehicle, low interest loans, and discounted goods and services are all taxable under the Fringe Benefits Tax system. FBT is based on the taxable value to the employee and tax is paid by the employer at either 49.25% or 43% of the value of the benefit.

CAN SOMEBODY DO BUSINESS FOR ME AND NOT BE AN EMPLOYEE?

It is relatively commonplace in NZ for parties to contract on a principal/contractor basis as opposed to an employer/employee basis. There are advantages for both parties in this respect, the principal relieved of numerous obligations an employer would otherwise have, and a contractor entitled to more freedom and the ability to claim various expenses for tax purposes that they would not have been able to do as an employee.

However, the IRD is constantly reviewing such relationships, their focus being a substance over form perspective, trying to identify situations where the relationship is in reality an employment one, even though the parties have attempted to label it as being something else.

If the IRD do establish an employment relationship, then the principal now employer may be exposed to penalties in respect of any PAYE not previously deducted from the contractor now employee payments. Therefore, due care should be exercised in this area.

HOW TO READ FINANCIAL STATEMENTS IN NEW ZEALAND

The Financial Reporting Act 1993 and the Companies Act 1993 govern the accounting and reporting requirements of Companies and other entities in New Zealand. The Companies Act 1993 requires that proper accounting records must be maintained in English.

Smaller companies may qualify as an exempt company if they are not subsidiaries, otherwise they are a "reporting entity". All reporting entities Financial Statements must comply with New Zealand equivalents to International Financial Reporting Standards (IFRS). Differential reporting is available to entities that do not have public accountability, provided there is no separation between the owners and the governing body, or the entity is not large. "Large" means two of: total income of NZ$20million; Total assets of NZ$10million; 50 employees.

Regardless of whether the entity is a reporting entity and required to comply with IFRS, or whether the entity is preparing special purpose financial statements, at the very least you can expect to see the following:

- Statement of Financial Performance (P & L, income statement);
- Balance Sheet (Statement of Financial Position);
- Statement of Movements in Equity;
- Notes to the accounts

A cash flow statement is only required for full reporting entities (IFRS).

Profit and Loss (P & L, income statement, statement of financial performance)
In the determination of profit, you can expect to see the following:

- All income and expenses derived/incurred during the year related to the normal running of the business and considered "revenue" in nature;
- Depreciation and amortisation on capital and intangible assets;
- Interest on loans
- Current tax expense

Statement of Movements in Equity
The equity at the beginning of the year, plus the current year net surplus and transactions with owners. The balance of equity at the end of the year flows through to the Balance Sheet.

Balance Sheet (statement of financial position)
The equity section will contain the final balance from the Statement of Movements in Equity usually broken down into share capital, retained earnings and reserves.

All assets and liabilities are listed and will be split between Current and Non-Current. Current reflects those assets and liabilities that are expected be collected or paid by company within the next 12 months. Non-current represents all assets and liabilities with a lifespan of greater than 12 months. If one figure is shown on the face of the balance sheet, it will be usual to see more detail in the notes to the accounts.