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WEEKLY COMMENT: FRIDAY 3 MAY 2024

1. The *Taxation (Annual Rates for 2023-24, Multinational Tax, and Remedial Matters) Act 2024* (the “Multinational Tax Amendment Act 2024”), with a date of assent of 28 March 2024, contains major amendments to the bright-line test rules and the related rollover relief rules, which apply to a person’s disposal of residential land if the “bright-line end date” as defined in the Multinational Tax Amendment Act 2024, is on or after 1 July 2024.

Bright-line test for disposals within 2 years

2. The Multinational Tax Amendment Act 2024 has reinstated a 2-year bright-line test for disposal of residential land. As noted above, the new rule applies to a disposal of residential land if the “bright-line end date” for the land is on or after 1 July 2024.
3. “Bright-line end date” is defined, for a person’s disposal of residential land, as meaning:
 - (a) The earliest of:
 - (i) The date the person enters into an agreement for the disposal;
 - (ii) The date on which the person makes a gift of the land;
 - (iii) The date on which the land is compulsorily acquired under any Act by the Crown, a local authority, or a public authority;
 - (iv) If there is a mortgage secured on the land, the date on which the land is disposed of by or for the mortgagee because the mortgagor defaulted; or
 - (b) If none of paragraphs (a)(i) to (a)(iv) apply, the date on which the estate or interest in the land is disposed of.
4. Under the new rule in s CB 6A(1), an amount that a person derives from disposing of residential land is income of the person if the person’s bright-line end date is within 2 years of their “bright-line start date”.
5. A person’s “bright-line start date” is defined in s CB 6A(2) as follows:
 - (a) General rule: The date on which the instrument to transfer the land to the person was registered under the Land Transfer Act 2017;
 - (b) For land outside New Zealand: The date on which the instrument to transfer the land to the person was registered under foreign laws of a similar nature to the Land Transfer Act 2017;

- (c) If an instrument to transfer land to the person was not registered before the person's bright-line end date: The date the person acquired an estate or interest in the land under s CB 15B (i.e. the date from which the person had an estate or interest in, or an option to acquire, the land, but if an option to acquire land is exercised, the date the option is exercised – see also Question We've Been Asked QB 17/02 Income tax – Date of acquisition of land, and start date for 2-year bright-line test - *Tax Information Bulletin* Vol. 29 No. 4, May 2017 (but the references to s CB 15B in the bright-line test discussion need to be updated to include the newly enacted rules);
 - (d) If the land was acquired from another person on completion of a land development or subdivision: The date the sale and purchase agreement for the developed or subdivided land was entered into;
 - (e) If the land results from the person subdividing their land: The person's bright-line start date for the undivided land;
 - (f) If the land is a freehold estate converted from a lease with a perpetual right of renewal: The date of the grant of the leasehold estate;
 - (g) If a joint tenancy is converted into a tenancy in common, or vice versa: To the extent the person's share or notional share in the land is unchanged, the person's bright-line start date for the land before the conversion;
 - (h) If there is a change of trustees: The transferee trustee's bright-line start date is the bright-line start date the transferor trustee had for the land.
6. A special rule applies if an owner of land has more land transferred to them, or transfers part of their land to another person: The instrument of transfer for the transferred land is treated as being for the transferred land only and not for the pre-existing land.
7. The bright-line test rules in s CB 6A do not apply to a person's disposal of residential land if:
- (a) Any of the general land taxation rules in sections CB 6 to CB 12 apply – the land taxation rules in these sections take precedence;
 - (b) The main home exclusion in s CB 16A applies; and
 - (c) If s FC 9 applies, which applies to inherited property as follows when residential land is transferred on a person's death:
 - (i) Section FC 9(1) applies to two types of transfers that may occur upon the death of a person: a transfer of a person's estate to an executor (covered by s FC 1(1)(a)), and a transfer of property on a distribution, by an executor, administrator, or trustee of a deceased person's estate, to a beneficiary who is beneficially entitled to receive the property under the will or the rules governing intestacy (covered by s FC 1(1)(b));
 - (ii) Section FC 9(2), as amended by the Multinational Tax Amendment Act 2024, provides that the bright-line test in s CB 6A does not apply to the transfer of residential land covered by the transfers referred to in s FC 9(1), including any intervening transfer to an executor or administrator;

- (iii) It is possible that the main home exclusion in s CB 16A could also apply – see paragraph 18 onwards below;
- (iv) The *Taxation (Annual Rates for 2021–22, GST, and Remedial Matters) Act 2022* (the “March 2022 Amendment Act”), which received the Royal assent on 30 March 2022 inserted the revised s CB 6A by introducing a s CB 6A(2B) which provided that the bright-line test in pre-existing s CB 6A did not apply to a subsequent disposal (before 1 July 2024), by an executor or administrator, or by a beneficiary, of residential land transferred to them on the death of a person, and the Platform Economy Amendment Act 2023 inserted a reference to s FC 9 in s CB 6A(2B), and Inland Revenue stated in the Platform Economy TIB on page 96 that the amendments clarify that the bright-line test does not apply if the executor or administrator of the estate or the ultimate beneficiary sells the land;
- (v) This clarification of an exemption for a subsequent sale by an executor or administrator, or by a beneficiary, has not been provided for in the revised s CB6A which applies from 1 July 2024, and it is not clear that a subsequent sale by such persons within the 2-year bright-line period will be exempt under the new rules;
- (vi) The amended s FC 9(2) refers to “the transfer of the residential land”, meaning the transfer to a beneficiary referred to in s FC 9(1), and not necessarily a subsequent transfer by the beneficiary;
- (vii) However, the extension, in s FC 9(4), of the bright-line test exemption to a recipient entitled to rollover relief who receives residential land from a beneficiary of the deceased person and subsequently disposes of it, is retained, which implies that a subsequent sale by a beneficiary should also be exempt from the bright-line test rules (see paragraph 16 below under the rollover rules).

Rollover rules from 1 July 2024

- 8. The new general rollover relief rules are contained in subpart FD and apply when residential land is transferred within the “bright-line period”, which is defined in s YA 1 as meaning the period beginning with the bright-line start date for the land and ending with the bright-line end date for the land.
- 9. Section FD 1(1) applies when residential land is transferred within the bright-line period:
 - (a) Between persons associated under any of sections YB 2 to YB 13 at the date of the transfer and for at least 2 years before that date; or
 - (b) To a trustee of a trust in which all beneficiaries, other than the transferor in their capacity as a beneficiary, are:
 - (i) Associated with the transferor at the date of transfer and for at least 2 years before that date (except for beneficiaries aged less than 2 years and persons who have become associated due to marriage or adoption, who must be associated with the transferor since birth, marriage or adoption, as applicable); or
 - (ii) Charitable organisations.

10. Rollover relief applies as follows:

- (a) The transfer is treated as a disposal by the transferor and an acquisition by the transferee for an amount equal to the cost of the residential land to the transferor;
- (b) The transferee's bright-line start date for the land is the transferor's bright-line start date;
- (c) For the purpose of determining whether the main home exclusion in s CB 16A applies, the transferor's use of the property is attributed to the transferee.

11. Inland Revenue notes in the Commentary to the Amendment Paper that to ensure that the new rollover provisions cannot be used to avoid the application of the bright-line test in situations where it was intended the test should apply, there is also a limitation on the number of times rollover relief can be applied to a property. Rollover relief can only be claimed for a property under the associated person provision once in any two-year period.

12. With effect from 1 July 2024, sections FC 9B and FC 9C are being repealed, meaning that the transferor will not be deemed to have received the greater of the cost of, or consideration received from the transfer of, the residential property transferred, and the transferee will not be deemed to have a cost base for the residential property equal to the greater of the cost to the transferor or the consideration given. For persons to whom the rollover relief rules apply, the property will be deemed to be transferred at cost regardless of the consideration actually given by the transferee to the transferor.

13. Rollover relief under s FD 1 does not apply to a transfer of residential land if s FD 1 has already been applied to a transfer of the residential land and 2 years have not passed from the date of the first transfer.

14. The pre-existing rollover relief provisions for Maori authority trusts and Treaty of Waitangi settlements, located in s CB 6AC and CB 6AE respectively, are being retained, but have been rewritten and relocated to sections FD 2 and FD 3, respectively.

15. Other pre-existing rollover relief rules are also being retained.

16. As noted in paragraph 7 above, effective from 1 July 2024 an amendment to s FC 9(4) provides that when residential land is transferred to an executor or administrator of a deceased estate, or distributed by them to a beneficiary, and the beneficiary disposes of the residential land to a person to whom rollover relief would apply under subpart FD, the bright-line test rules in s CB 6A will not apply to a subsequent disposal of the residential land by the recipient.

17. Specific rollover rules contained in sections FB 3A, FO 10, and FO 17 (which provide rollover relief for land transferred on settlement of relationship property or company amalgamation) are preserved by s CB 6A(6):

- (a) When residential land is transferred on a settlement of relationship property, s FB 3A provides that the transfer is treated as a disposal and acquisition for an amount that equals the total cost to the transferor at the date of the transfer;
- (b) When property belonging to an amalgamating company becomes the property of an amalgamated company on a resident's restricted amalgamation, s FO 10 provides that property that would be revenue account property merely because of the bright-line test

or the 10-year rule in sections CB 9 to CB 11 and s CB 14, is treated as having been acquired by the amalgamated company on the date it was acquired by the amalgamating company, at the total of the price paid and additional expenditure incurred by the amalgamating company;

- (c) When land belonging to an amalgamating company passes to an amalgamated company on a resident's restricted amalgamation, s FO 17 provides for a transfer at market value if a subsequent disposal by the amalgamated company could give rise to income, including under the bright-line test.

Main home exclusion from 1 July 2024

18. The main home exclusion in s CB 16A has been replaced. The replacement applies to a person's disposal of residential land if the bright-line end date for the land is on or after 1 July 2024.
19. The general rule in s CB 16A(1) is that the bright-line test in s CB 6A does not apply to a person who disposes of residential land, if the land has been used predominantly, for most of the time the person owned the land, for a dwelling that was the main home of:
 - (a) The person; or
 - (b) A beneficiary of a trust, if the person is a trustee of the trust and:
 - (i) A principal settlor of the trust does not have a main home; or
 - (ii) If a principal settlor of the trust does have a main home, it is that main home that the person is disposing of.
20. Under s CB 16A(2), the period in which the dwelling was constructed is ignored when determining whether the residential land has been used predominantly for a dwelling that was the main home as set out in s CB 16A(1).
21. Inland Revenue notes in the Commentary on the Amendment Paper that:
 - (a) The main home exclusion will apply if the land has been used predominantly (i.e. more than 50% of the land area), for most of the time the person owned the land (i.e. more than 50% of the period), for a dwelling that was the person's main home;
 - (b) The requirement that the land is used predominantly for the person's main home means that most of the area of the land (ie, more than 50%) must have been actually used for the home: the test is based on a person's actual use of the property and not the person's intended use of the property;
 - (c) The land also must be used for most of the time that the person owns the land as their main home, which requires the property to have been used more than 50% of the time as their main home for the period the person owns the land;
 - (d) The land does not need to have been used without interruption as their main home - for example, a main home can be rented out for short periods while the owner is on vacation or prior to settlement of the sale of the property, as long as the time is less than the private residential use;

- (e) The main home exclusion is modified so that the period when a dwelling is being constructed on the land is ignored in determining whether the land has been used predominantly as a main home for most of the period;
 - (f) The ordinary meaning of “construction” would apply, which would encompass work to build or erect the main home, including the design phase. In many cases, construction would be considered complete once the code compliance certificate has been issued under the Building Act 2004, however, the exact length of the construction period would depend on the facts and circumstances of each case;
 - (g) The main home exclusion would either apply or it would not apply - it would not apply on a proportionate basis, meaning that when the property is used less than 50% for the main home of the person, either by land area or time, then the main home exception will not apply.
22. Sections CB 16A(3) to (5) provide that the main home exclusion will not apply if the person disposing of the land (including 2 or more persons who occupy the residential land together, and also including a non-natural person that any person or persons occupying the land have significant control over) has:
- (a) Used the exclusion twice within the 2 years immediately preceding the bright-line end date for the residential land; or
 - (b) Engaged in a regular pattern of acquiring and disposing of residential land to which the main home exclusion would otherwise apply.



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