Regulatory Impact Statement

Black hole expenditure items: abandoned research and development, resource consents and company administration costs

Agency Disclosure Statement

This Regulatory Impact Statement has been prepared by Inland Revenue.

It provides an analysis of options to address the following areas where black hole expenditure may occur under current tax rules:

- abandoned research and development (R&D);
- certain fixed-life resource consents;
- unsuccessful resource consents where no application is lodged; and
- company administration costs.

These black hole expenditure items were predominantly brought to the attention of officials through correspondence from the private sector. The abandoned R&D black hole expenditure item was identified by officials during a recent review of tax settings related to innovation.

Black hole expenditure is capital expenditure that is not immediately deductible for tax purposes and also does not give rise to a depreciable asset for tax purposes, and therefore cannot be deducted as depreciation over time. Generally, taxpayers try to reduce their tax liability by deducting their expenditure, wherever possible, against their assessable income. If expenditure is incorrectly ascribed as non-deductible black hole expenditure, a number of problems can arise.

Black hole treatment of expenditure items for tax purposes can produce economic distortions. A taxpayer may choose to invest in an area where they can deduct or depreciate their expenditure instead of investing in a black hole expenditure item where they cannot. If investing in the black hole expenditure item would have been the most efficient choice in a world without tax, the taxpayer's investment decision has been distorted by tax settings.

Other issues that can arise include uncertainty for taxpayers about an item's correct tax treatment, an increase in compliance costs for taxpayers to obtain a deduction, inconsistencies in the tax treatment of similar expenditure items, and an incentive for taxpayers to re-characterise black hole expenditure items in order to access the deduction. It should be noted that due to the nature of such issues, it is not possible to accurately assess the exact scale of these problems.

It is proposed that some expenditure that is currently black hole in nature instead be made immediately deductible or depreciable, with some expenditure of a more capital nature to remain non-deductible. As the size of the problem cannot be quantified with any certainty, there is some uncertainty around the estimated fiscal costs, and the amounts of any expected fiscal gains are unknown.

The proposals have the following estimated fiscal implications:

	$m increase / (decrease)				
Vote Revenue Minister of Revenue	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**2016/17**
Tax Revenue	-	(0.360)	(1.560)	(2.010)	(2.460)

Estimated tax revenue costs is expected to continue to increase by $450,000 per annum to approximately $9 million per annum over time.

As these proposals were earmarked for potential announcement as part of Budget 2013, officials have not consulted on them with taxpayers, and the analysis undertaken has been subject to time constraints in order to meet Budget 2013 deadlines. However, these proposals are overwhelmingly taxpayer friendly and most were brought to officials' attention as a result of correspondence with the private sector. As the amendments will be included in a bill which will be considered by the Finance and Expenditure Committee, there will be an opportunity for submissions to be made by interested parties. Officials could also engage in direct consultation with submitters on the issues if agreed by the Select Committee. The analysis undertaken on this issue was carried out in conjunction with the Treasury, and they support the conclusions and recommendations made.

None of the policy options would impose additional costs on business, impair private property rights, restrict market competition, reduce the incentives for businesses to innovate and invest, or override fundamental common law principles.

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STATUS QUO AND PROBLEM DEFINITION

1. Black hole expenditure is capital expenditure that is not immediately deductible for tax purposes and also does not give rise to a depreciable asset for tax purposes, and therefore cannot be deducted as depreciation over time. A number of areas where black hole expenditure can occur under current tax rules have been brought to the attention of officials. A further area where black hole expenditure may occur was identified by officials during a recent review of tax settings related to innovation.

2. Black hole treatment of expenditure items for tax purposes can produce economic distortions. A taxpayer may choose to invest in an area where they can deduct or depreciate their expenditure instead of investing in a black hole expenditure item where they cannot. If investing in the black hole expenditure item would have been the most efficient choice in a world without tax, the taxpayer's investment decision has been distorted by tax settings.

3. Other issues that can arise include uncertainty for taxpayers about an item's correct tax treatment, an increase in compliance costs for taxpayers to obtain a deduction, inconsistencies in the tax treatment of similar expenditure items, and an incentive for taxpayers to re-characterise black hole expenditure items in order to access a tax deduction. It should be noted that due to the nature of such issues, it is not possible to accurately assess the exact scale of these problems.

4. The black hole expenditure items which are the subject of this Regulatory Impact Statement relate to:

- abandoned research and development (R&D);
- certain fixed-life resource consents;
- unsuccessful resource consents where no application is lodged; and
- company administration costs (dividend payments, listing fees and special shareholder meetings).

Abandoned research and development

5. Under current tax rules, a person is allowed an immediate deduction for expenditure they incur on research or development up until an asset is recognised for accounting purposes. Further development expenditure is capitalised. Development expenditure that has been capitalised can be depreciated only once there is a depreciable asset for tax purposes.[1] In the event that the project does not generate a depreciable asset for tax purposes, this capitalised expenditure will be rendered non-deductible either immediately or over a period of time.[2] This can act as a disincentive to undertake desired levels of R&D.

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[1] Note that the depreciable cost base of items of depreciable intangible property will not necessarily equate to the total capitalised expenditure the taxpayer will have incurred from the point of asset recognition.

[2] An immediate deduction is currently allowed under section DB 37 of the Income Tax Act 2007 for capitalised expenditure incurred in relation to a patent application that is refused or withdrawn.

Certain fixed-life resource consents

6. The Income Tax Act 2007 (ITA) lists items of intangible property that are depreciable – this includes certain fixed-life resource consents. In 1998, sections 15A (dumping of waste in coastal areas) and 15B (discharging hazardous substances from ships and offshore installations) were added to the Resource Management Act 1991 (RMA) to regulate dumping activities in the coastal marine area. Resource consents to do something which would otherwise contravene these sections of the RMA have a limited life of between five and thirty-five years. The ITA has not, however, been updated to include reference to these sections of the RMA. Therefore, capital expenditure incurred in obtaining a resource consent to do something which would otherwise contravene section 15A or 15B of the RMA is not currently depreciable. This is inconsistent with the tax treatment for expenditure on other fixed-life resource consents, which are depreciable.

Unsuccessful resource consents where no application is lodged

7. The ITA allows a deduction for expenditure incurred by a person who applies for the grant of a resource consent under the RMA and is refused the grant or withdraws the application. The wording of the relevant section requires that, for the expenditure to be deductible, the resource consent application process must be completed, even though the consent is no longer actually sought. This may result in some taxpayers incurring further expenditure to complete the application simply in order to obtain the tax deduction, which is an inefficient outcome.

Company administration costs: dividends, listing fees and shareholder meeting costs

8. Inland Revenue's view of the law in this area is currently in draft form. This has created some uncertainty in the private sector over the tax treatment of various company administration costs. The costs identified as of most concern are costs associated with the payment of dividends, listing fees and shareholder meeting costs. All of these items straddle the capital-revenue boundary, which creates the uncertainty. When considering the appropriate tax treatment of company administration costs, there is a trade-off between compliance costs and economic distortions; in general, the more accurate and consistent the item's tax treatment, the higher the associated compliance costs. As these expenditure items are usually relatively minor, minimising compliance costs is to be prioritised over minimising economic distortions.

OBJECTIVES

9. The objectives of the proposed changes are to:

(i) improve the efficiency of the tax system by ensuring that investment decisions are not distorted by tax considerations;

(ii) provide certainty about the tax treatment of particular expenditure items;

(iii) reduce compliance costs for taxpayers; and

(iv) improve the coherency, consistency and integrity of the overall tax system.

10. For the abandoned R&D and the resource consent expenditure items, minimising investment distortions has been prioritised over the other three objectives (however, they generally go hand in hand). On the other hand, for company administration costs, which are

usually relatively small, minimising compliance costs has been prioritised over minimising investment distortions where there is a conflict between objectives.

REGULATORY IMPACT ANALYSIS

Abandoned research and development

Status quo

11. Under the status quo, R&D expenditure that has been capitalised cannot be deducted where the project fails to produce a depreciable asset for tax purposes.

Option one (preferred option):

12. Option one is to allow an immediate deduction for failed capitalised R&D expenditure which would have been part of the cost of "depreciable intangible property" if the project had been successful.

Option two

13. Option two is to depreciate failed capitalised R&D expenditure, which would have been part of the cost of "depreciable intangible property" if the project had been successful, over the estimated useful life of the asset the R&D expenditure was aimed at creating.

Option three

14. Option three is to allow an immediate deduction for all capitalised R&D expenditure on failed projects that were aimed at creating an asset listed as depreciable for tax purposes on Schedule 14 of the ITA.

Option four

15. Option four is to depreciate all the capitalised R&D expenditure on failed projects over the estimated useful life of the asset on Schedule 14 of the ITA the R&D expenditure was aimed at creating.

Further information

16. Each of options one to four would also involve the introduction of appropriate claw-back rules (outlined below), which would apply in the event that a failed asset from an abandoned R&D project (which has had capitalised R&D expenditure deducted) becomes useful or is sold.

17. In the event that such a failed asset becomes useful, it is proposed that the capitalised R&D expenditure previously allowed as a deduction would be clawed back. The clawed-back amount would then be able to be depreciated over the estimated useful life of the asset.

18. In the event that such a failed asset is sold, it is proposed that the capitalised R&D expenditure previously allowed as a deduction (or the sale proceeds, if this amount is lower) would be clawed back. The exception to this would be where the sale of the failed asset would otherwise give rise to assessable income. In such instances, it is proposed that the entire sales proceeds would continue to be assessable income.

Summary

19. The impacts of the status quo and options one to four are summarised in the following table:[3]

[3] Neither the status quo nor any of options one to four have any social or environmental impacts.

Table 1: Abandoned research and development

Option	Meets objectives?	Impacts						Net impact
		Economic impact	Coherence / Consistency / Integrity	Certainty	Compliance costs	Fiscal impact	Risk	
Status quo	No	Disincentive to undertake the optimal level of R&D.	Not met, as a deduction for failed capitalised expenditure is usually allowed when it is written off.	Not met, as, if the R&D project fails, expenditure that would have been depreciable if it had succeeded may be neither deductible nor depreciable.	No impact.	No impact.	None.	The level of R&D undertaken may be sub-optimal.
One (preferred option)	Yes	Removes a disincentive to investment in R&D.	Improved, as a deduction is allowed for failed capitalised expenditure that would have been depreciable if it had been successful.	Improved, as businesses will know that if their R&D project fails they will be able to deduct the capitalised R&D expenditure they would have been able to depreciate if it had succeeded.	Reduced, as businesses will not need to incur unnecessary expenditure to access a deduction (where available).	Estimated fiscal cost of $1m per annum.	As this option restricts deductible expenditure to that which would have been part of "depreciable intangible property" if the project had been successful, and deductions are already allowed in the case of failed or withdrawn patent applications, this option may be perceived as being of limited benefit.	Overall, improves upon the status quo, as it reduces economic distortions and is consistent with the tax treatment for other items of failed capital expenditure.
Two	In part	Removes a disincentive to investment in R&D. Economically neutral between successful and unsuccessful projects.	Not met, as this is not the usual treatment of failed capitalised expenditure.	Improved, as businesses will know that if their R&D project fails they will be able to depreciate the capitalised R&D expenditure they would have been able to depreciate if it had succeeded.	Reduced, as businesses will not need to incur unnecessary expenditure to access a deduction (where available).	Estimated fiscal cost would eventually rise to a level similar to option one.	In addition to carrying the same risk as option one, the private sector could complain that this treatment is less favourable than solutions implemented for other black hole expenditure issues.	Reduces economic distortions, but is inconsistent with the tax treatment for other items of failed capital expenditure.

Three	No	Removes a disincentive to investment in R&D. Would give failed R&D projects a more favourable tax treatment than currently exists for successful ones.	Not met, inconsistent treatment between failed and successful projects.	Improved, businesses will know that if their R&D project fails they will be able to deduct all capitalised R&D expenditure.	Reduced, as businesses will not need to incur unnecessary expenditure to access a deduction (where available).	Estimated fiscal cost of $10m per annum.	Would create an asymmetric tax treatment with successful projects, which would distort investment decisions and potentially create tax avoidance risks.	Removes one economic distortion but creates a more serious one.
Four	No	Removes a disincentive to investment in R&D. Would give failed R&D projects a more favourable tax treatment than currently exists for successful ones.	Not met, inconsistent treatment between failed and successful projects. Also not the usual treatment of failed capitalised expenditure.	Improved, businesses will know that if their R&D project fails they will be able to depreciate all capitalised R&D expenditure.	Reduced, as businesses will not need to incur unnecessary expenditure to access a deduction (where available).	Estimated fiscal cost would eventually rise to a level similar to option three.	Would create an asymmetric tax treatment with successful projects, which would distort investment decisions and potentially create tax avoidance risks.	Removes one economic distortion but creates a more serious one. Also inconsistent with the tax treatment for other items of failed capital expenditure.

Certain fixed-life resource consents

Status quo

20. Under the status quo, expenditure incurred in applying for resource consents granted under the RMA to do something that otherwise would contravene section 15A (dumping of waste in coastal areas) or 15B (discharging hazardous substances from ships and offshore installations) cannot be depreciated. This creates investment distortions and is inconsistent with how other assets with a fixed life are depreciated, including other fixed-life resource consents.

Option one (preferred option):

21. Option one is to allow resource consents granted under the RMA to do something that otherwise would contravene section 15A or section 15B to be depreciable over the life of the consent.

22. All resource consents for the coastal marine area granted under the RMA to do something that otherwise would contravene section 15A or 15B of the RMA have a limited life of between five and thirty-five years. This option is consistent with our depreciation framework; fixed-life resource consents should be depreciated as their economic benefits are used up over their lifetime.

23. The impacts of the status quo and option one are summarised in the following table:

Table 2: Certain fixed-life resource consents

Option	Meets objectives?	Impacts							Net impact
		Economic impact	Coherence / Consistency / Integrity	Certainty	Fiscal impact	Compliance costs	Social / environmental impacts	Risk	
Status quo	No	No impact.	Not met, inconsistent with the tax treatment of other fixed-life resource consents.	Not met, likely to be further calls to change the tax treatment.	No impact, as no additional revenue or cost.	No impact, as existing tax treatment remains.	No impact, as existing tax treatment remains.	None.	Economic distortions and inconsistency with the tax treatment of other fixed-life resource consents would persist.
One (preferred option)	Yes	This option would minimise investment distortions and will improve the overall consistency of the tax system.	Improved, would be consistent with the tax treatment of other fixed-life resource consents.	Improved.	Estimated fiscal costs increase by $0.45m per annum from $0.11m in 2013/14 to approximately $9m per annum over time.	A very minor impact as taxpayers incur a small compliance cost to claim the depreciation deduction.	Moving to a more favourable tax treatment will likely, at the margin, increase the number of fixed-life resource consents applied for to carry out coastal dumping. However, the option does not alter the regulatory framework under the RMA for obtaining these consents.	There is some uncertainty about the fiscal cost of this option.	Minimises economic distortions and improves the consistency of the tax system.

Unsuccessful resource consents where no application is lodged

Status quo

24. Under the status quo, expenditure incurred in relation to an application for the grant of a resource consent under the RMA is deductible if the grant is refused or the application is withdrawn. Expenditure incurred in relation to an intended application for the grant of a resource consent, where an application is never lodged, is currently unable to be deducted nor depreciated.

Option one (preferred option):

25. Option one is to allow a deduction for expenditure incurred in relation to an intended resource consent application that is never lodged. The deduction would be allocated to the income year in which it is decided that the application will no longer be pursued.

Option two

26. Option two is to depreciate expenditure incurred in relation to an intended resource consent application that is never lodged over the life of the particular resource consent which would have been obtained if the application had been made and granted.

27. The impacts of the status quo and options one and two are summarised in the following table:

Table 3: Unsuccessful resource consents where no application is lodged

Option	Meets objectives?	Impacts						Net impact
		Economic impact	Coherence / Consistency / Integrity	Certainty	Fiscal impact	Compliance costs	Risk	
Status quo	No	No impact.	Not met, a deduction for failed expenditure is usually allowed when it is written off	Not met, there is likely to be issues with taxpayers trying to interpret the policy intent behind requiring an application to be completed to access the deduction.	No impact.	No impact, but already high because of additional costs incurred by taxpayer to complete the application to access the deduction.	None.	The current settings are inefficient and inconsistent compared with the tax treatment for other items of failed capital expenditure.
One (preferred option)	Yes	Improvement in efficiency, as taxpayers will no longer incur expenditure for no economic reason other than obtaining a tax deduction.	Improved, a deduction for failed expenditure is allowed when it is written off.	Improved.	No impact, as applicants are already likely deducting this expenditure by completing the application process.	Reduction in compliance costs, as businesses will no longer have to incur unnecessary expenditure in completing an application for a resource consent that is no longer sought.	None.	Improves upon the status quo, as allowing a deduction for expenditure is consistent with the tax treatment for other items of failed capital expenditure.
Two	In part	Improvement in efficiency, as taxpayers will no longer incur expenditure for no economic reason other than obtaining a tax deduction.	Not met, this is not the usual treatment of failed expenditure.	Improved.	No impact, as applicants are already likely deducting this expenditure by completing the application process.	Reduction in compliance costs, as businesses will no longer have to incur unnecessary expenditure in completing an application for a resource consent that is no longer sought.	None.	Depreciating expenditure over the life of the resource consent (had it been successful) is inconsistent with the tax treatment for other items of failed capital expenditure

Company administration costs: dividends, listing fees and shareholder meeting costs

28. There are no specific rules governing the tax treatment of these items, and Inland Revenue's view of the law in this area has only ever been released as a draft statement. In practice, there is some evidence to suggest that some taxpayers may not necessarily be deducting these expenses as set out in this draft statement. The analysis below will consider the status quo as Inland Revenue's latest view of the law.

Dividends

Status quo

29. Under the status quo, the capital-revenue test, which determines whether expenditure is revenue and therefore deductible, or capital and therefore not deductible (but possibly depreciable), should be applied to expenditure incurred during the dividend payment process. Inland Revenue's view of the law suggests that expenditure incurred on authorising dividends is deductible, but costs related to the allocation, payment, and disputes over the allocation of dividends are not.

Option one (preferred option):

30. Option one is to allow deductions for all costs associated with the payment of dividends. The payment of dividends is a regular ordinary business expense and despite some of the costs of the process being capital, it would be practical to allow deductions in order to minimise compliance costs and increase certainty for businesses.

31. The impacts of the status quo and option one are summarised in the following table:

Table 4: Dividends

Option	Meets objectives?	Impacts						Net impact
		Economic impact	Coherence / Consistency / Integrity	Certainty	Fiscal impact	Compliance costs	Risk	
Status quo	In part	Minimises investment distortions.	Met, consistent application of the capital-revenue test as usually applied to expenditure to determine deductibility.	No change.	No impact.	High compliance costs as taxpayers required to separate out expenditure incurred on authorising dividends from the other costs associated with the dividend payment process.	Enforcing and monitoring is difficult, with the cost often exceeding the benefit.	It is consistent but likely to maintain uncertainty and high compliance costs.
One (preferred option)	Mostly	Allowing deductions for a capital item incentivises additional spending on that item.	Reduced, allows a deduction for expenditure that is possibly capital.	Improved, would provide certainty of the law.	No significant impact, some evidence to suggest that some taxpayers may already be deducting this expenditure.	Reduced compliance costs as all expenditure associated with the payment of dividends would be deductible.	None.	Minimises compliance costs and increases certainty, but does reduce overall consistency.

Listing fees

Status quo

32. Under the status quo, the capital-revenue test should be applied to expenditure incurred on initial, subsequent and annual listing fees. The Inland Revenue draft statement suggested that all listing fees are capital expenditure and should not be deductible because they are used to raise and maintain equity.

Option one (preferred option):

33. Option one is to allow deductions for annual listing fees but not for the initial listing fee or subsequent listing fees arising from additional share issues. Annual listing fees are a regular expense with a short-term benefit, facts which favour allowing a deduction. Initial listing fees are incurred so a company can list on a stock exchange, and subsequent listing fees help with the acquisition of further equity. These benefits persist indefinitely, and are indicative of capital expenditure.

Option two

34. Option two would involve aligning the tax treatment of equity and debt raising costs. Debt and equity capital are partial substitutes for financing a business, which seems to imply that the respective tax treatments for debt and equity raising costs would need to be similar to prevent a bias towards one or the other. As debt raising costs are deductible, allowing a deduction for listing fees (initial, subsequent and annual) may reduce a bias towards debt financing. However, this needs to be balanced against the difference in the lives of equity (indefinite) and debt (limited).

35. The benefits arising from expenditure that raises equity persist indefinitely, whereas benefits from expenditure that raises debt are used up over the life of the loan. This would suggest that the different tax treatments for debt and equity raising costs are consistent with existing tax frameworks.

Summary

36. The impacts of the status quo and options one and two are summarised in the following table:

Table 5: Listing fees

Option	Meets objectives?	Impacts						Net impact
		Economic impact	Coherence / Consistency / Integrity	Certainty	Fiscal impact	Compliance costs	Risk	
Status quo	Mostly	Minimises investment distortions but may encourage financing with debt over equity.	Met, consistent application of the capital-revenue test as usually applied to expenditure to determine deductibility	Some uncertainty over the current tax treatment.	No impact.	No impact, compliance costs are not a problem here as no expenditure is to be apportioned.	Enforcing and monitoring is difficult, with the cost exceeding the benefit.	Preventing deductions for annual listing fees incentivises taxpayers to finance with debt over equity. Continued uncertainty of the tax treatment will remain.
One (preferred option)	Yes	Slight distortion favouring listing fees, but some evidence to suggest that some taxpayers are already deducting annual listing fees. This means there would be very little economic impact.	In part met, concessionary tax treatment of annual listing fees but the proposed treatment of initial and subsequent fees is consistent.	Met, would provide certainty of the law.	No impact, as applicants are already likely deducting this expenditure in line with the proposed policy.	No impact, compliance costs are not a problem here as no expenditure is to be apportioned.	None.	Provides certainty to businesses on the tax treatment of this item, minimises compliance costs. While it creates a slight economic distortion, this is not of concern.
Two	No	Allowing deductions for capital expenditure incentivises additional investment in that area.	Not met, this is a concessionary tax treatment for all listing fees.	Met, would provide certainty of the law.	Small unknown fiscal cost for allowing initial and subsequent listing fees to be deductible.	No impact.	None.	This is inconsistent with tax deductibility frameworks as it does not take into account the indefinite benefit taxpayers receive from publicly listing on a stock exchange.

Shareholder meeting costs

Status quo

37. Under the status quo, the capital-revenue test should be applied to expenditure incurred on annual shareholder meetings (AGMs) and special shareholder meetings. The Inland Revenue draft statement suggested that all AGM costs are deductible for tax purposes, whereas the deductibility of special shareholder meeting costs depends on the purpose of the meeting. For example, expenditure on a special meeting held to consider a major transaction is revenue and would be deductible, but considering a change to a company's constitution is capital and not deductible.

Option one (preferred option)

38. Option one is to confirm that AGM expenses are deductible, and make special shareholder meeting expenses non-deductible. AGMs are a requirement by law and are a regular business expense, but special shareholder meetings are often held to consider a material change in the business, and therefore are often capital expenditure.

Option two

39. The resolutions considered in a shareholder meeting are the most accurate determinants of deductibility. Option two involves requiring taxpayers to apportion shareholder meeting costs between the deductible (revenue) and non-deductible (capital) resolutions considered at each meeting.

Option three

40. Allow a deduction for all AGM and special shareholder meeting costs.

Summary

41. The impacts of the status quo and options one to three are summarised in the following table:

Table 6: Special shareholder meeting costs

Option	Meets objectives?	Impacts						Net impact
		Economic impact	Coherence / Consistency / Integrity	Certainty	Fiscal impact	Compliance costs	Risk	
Status quo	No	Incentivises taxpayers to consider capital resolutions at AGMs where they are deductible.	Met, consistent application of the capital-revenue test as usually applied to expenditure to determine deductibility.	Not met.	No impact.	High compliance costs as taxpayers have to break down expenditure into smaller categories than are currently accounted for.	Enforcing and monitoring is difficult, with the cost exceeding the benefit. It is often difficult to ascertain the major purpose of the meeting on occasions.	Does not provide certainty or reduce compliance costs for taxpayers while economic distortions persist.
One (preferred option)	Mostly	Incentive for taxpayers to consider capital resolutions at AGMs exaggerated further by disallowing deductions for all special shareholder meetings.	In part, tax treatment approximates the capital-revenue test, but is somewhat concessionary towards AGM costs and harsher towards special shareholder meeting costs.	Improved, would provide certainty of the law.	Small, unknown fiscal gain as some previously deductible shareholder meetings are no longer deductible.	Significant reduction in compliance costs. This option does not require taxpayers to break down expenditure into smaller categories.	None.	Satisfies prioritised objective of reducing compliance costs and provides certainty to taxpayers. However, economic distortions remain, and it is somewhat inconsistent with the overall tax system. Overall, net impact is positive.
Two	No	Least distortionary tax treatment.	Met, uses the most accurate determinant of deductibility (resolutions considered) instead of the current determinant, the meeting's purpose.	Not met, the complex design of this option would make it harder for taxpayers to apply the new tax treatment correctly.	Small, unknown fiscal gain, as some AGM and special shareholder meeting costs (where capital resolutions are considered) would no longer be deductible.	Significant increase in compliance costs with the introduction of apportionment rules.	May encourage taxpayers to artificially inflate the number of revenue resolutions to increase the deductible portion of the meeting cost.	Removes economic distortions to a degree but would increase compliance costs significantly and reduce certainty.
Three	In part	Most distortionary tax treatment.	Not met, concessionary tax treatment of both AGM and special shareholder meeting costs.	Improved, would provide certainty of the law.	Unknown fiscal cost as all shareholder meeting costs would be deductible.	Significant reduction in compliance costs. This option does not require taxpayers to break down expenditure into smaller categories.	Unknown fiscal risk, and allowing this concessionary tax treatment may lead to further calls for similar concessions to be made for other expenses.	Satisfies prioritised objective of reducing compliance costs and provides certainty. However, economic distortions are relatively large, the proposed tax treatment would be inconsistent, and there are identified risks.

CONSULTATION

42. Officials have not consulted with taxpayers on these issues because the proposals are earmarked for announcement in Budget 2013. However, it is expected that these proposals would be generally favourably received by taxpayers, as they are predominantly taxpayer friendly and have arisen partly from correspondence with the private sector.

43. As the amendments will be included in a bill which will be considered by the Finance and Expenditure Committee, there will be an opportunity for submissions to be made by interested parties. Officials could engage in direct consultation with submitters on the issues if agreed by the Committee.

44. The Treasury has been consulted and agrees with the proposals.

CONCLUSIONS AND RECOMMENDATIONS

Abandoned research and development

45. Officials recommend that an immediate deduction be allowed for failed capitalised R&D expenditure which would have been part of the cost of "depreciable intangible property" if the project had been successful (with appropriate claw-back rules which would apply in the event that a failed asset becomes useful or is sold). This reduces economic distortions, without creating an asymmetric treatment with successful R&D projects, which would result in more serious economic distortions. Also, an immediate deduction (rather than depreciation over time) is consistent with the tax treatment for other items of failed capital expenditure.

Certain fixed-life resource consents

46. Officials recommend that sections 15A and 15B of the RMA be added to Schedule 14 (depreciable intangible property) of the ITA. This will mean that expenditure on resource consents granted under the RMA to do something that otherwise would contravene these sections will be depreciable over the life of the resource consent. This policy change fits within Inland Revenue's depreciation framework; resource consents with a fixed-life should be depreciated as their economic benefits are used up over their lifetime to minimise economic distortions. It also improves the consistency of the tax system, as this change would grant these resource consents the same tax treatment as other fixed-life resource consents.

Unsuccessful resource consents where no application is lodged

47. Officials recommend that a deduction be allowed for expenditure relating to a failed resource consent application that has not been lodged. The status quo requires taxpayers to complete the application for a resource consent that is no longer sought, which is an unintended policy outcome that increases their compliance costs.

Company administration costs

Dividends

48. Officials recommend a deduction for costs associated with the payment of dividends. Requiring taxpayers to apply the capital-revenue test to this expenditure creates disproportionate compliance costs. Allowing a deduction will provide certainty about the item's tax treatment, and minimise compliance costs for taxpayers.

Listing fees

49. Officials recommend allowing deductions for annual listing fees but not for the initial listing fee (for listing on a stock exchange), or subsequent listing fees arising from additional share issues. Annual listing fees have short-term benefits that do not persist, whereas the benefits from initial and subsequent listing fees persist indefinitely. The proposed change also provides certainty to taxpayers over the tax treatment of these costs.

Shareholder meeting costs

50. Officials recommend allowing deductions for AGM expenditure but not for expenditure on special shareholder meetings. This will reduce compliance costs for taxpayers as it only requires them to allocate expenditure between the AGM and any other special shareholder meetings (if any), and not to apportion costs to capital and revenue items considered at the same meeting. It also provides certainty to taxpayers about the tax treatment of these costs.

IMPLEMENTATION

51. If approved, these proposals, which require legislative change, will be included in the next available taxation bill after Budget 2013 and will apply from the 2014/15 income year.

52. When introduced to Parliament, commentary will be released explaining the amendments, and further explanation of their effect will be contained in a Tax Information Bulletin, which would be released shortly after the bill receives Royal assent.

53. The proposals have no system implications for Inland Revenue but may incur some additional administrative costs. These are expected to be insignificant and would be met within existing baselines.

54. The proposals are not expected to result in any additional compliance costs for taxpayers. The intent of the proposed tax treatment of the company administration expense items is to reduce compliance costs.

MONITORING, EVALUATION AND REVIEW

55. In general, Inland Revenue's monitoring, evaluation and review of new legislation takes place under the Generic Tax Policy Process (GTPP). The GTPP is a multi-stage tax policy process that has been used to design tax policy in New Zealand since 1995. The final stage in the GTPP is the implementation and review stage, which involves post-implementation review of the legislation, and the identification of any remedial issues. Opportunities for external consultation are also built into this stage. In practice, any changes identified as

necessary for the new legislation to have its intended effect would generally be added to the Tax Policy Work Programme, and proposals would go through the GTPP.