

**EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY | HUKIHUKI HURANGA
- MŌ TE TĀKUPU ME TE MATAPAKI ANAKE**

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FACT SHEET | PUKA MEKA

Income Tax and GST- forestry activities registered in the Emissions Trading Scheme

Issued | Tukuna: Issue Date

IS ##/## FS #

This fact sheet accompanies IS **XX/XX** which considers the tax consequences for foresters who are registered in the Emissions Trading Scheme (ETS) and who receive, sell and surrender emissions units (NZUs). This fact sheet summarises the tax treatment of acquiring, selling and surrendering NZUs in a forestry context.

Summary of the tax treatment of NZUs

1. For GST purposes, all transfers of NZUs are zero-rated, so there is no amount of GST included on any purchases, receipts, surrenders and sales of NZUs.
2. For income tax purposes, NZUs are generally revenue account property. The general scheme for revenue account property is that any deduction for the cost of the property is carried forward and offset against any eventual proceeds on sale. For NZUs, this means there should not be a tax liability when the NZUs are received, held and surrendered for emission liabilities by a forester. Tax liabilities generally only arise when NZUs are sold. However, the different types of NZUs for tax purposes have different tax consequences.

Different types of NZUs for tax purposes

3. There are several types of NZUs for tax purposes in the forestry context:
 - Pre-1990 forest land NZUs were provided to eligible foresters with pre-1990 forest land under the forest land allocation plan.
 - Post-1989 forest land NZUs are earned by foresters who are ETS participants with eligible post-1989 forest land.
 - Permanent forestry sink Initiative (PFSI) NZUs were earned by foresters who had registered in the PFSI (which is now discontinued).
 - Replacement forest land NZUs are NZUs that a forester has bought to replace post-1989 forest land NZUs that had been sold. To qualify, the forester must not have previously acquired other NZUs to replace the sold post-1989 forest land NZUs.
 - Standard NZUs (eg, bought at auction or from the secondary market).
4. Both pre-1990 and post-1989 forest land NZUs must remain held continuously by the original recipient (or a party to a forestry rights agreement). They lose their tax status when they are transferred.

Tax treatment of NZUs

5. All NZUs are treated as revenue account property. There are two key points in time when there may be tax consequences for foresters:
 - on acquisition and at balance date; and
 - on surrender and sale.

Acquisition and balance date

6. In summary, there are no income tax liabilities that arise at the time of acquisition of NZUs or while NZUs remain on hand at the end of the year.
7. At the end of each income year, forest land NZUs (including replacement forest land NZUs) have a deemed value of zero, and standard NZUs that are purchased have a deemed value equivalent to their cost.
8. Deductions for the cost of any purchased NZUs can be claimed in the year of purchase only when the NZUs are replacement forest land NZUs. Deductions for standard NZUs purchased are delayed until the income year in which the NZUs are sold or surrendered for an emissions liability (as revenue account property).

Surrender and sale of NZUs

9. Disposals of NZUs may have tax consequences.
10. In very brief summary, sales of pre-1990 forest land NZUs (where the land was held on capital account) are excluded income and do not incur an income tax liability. Sales of all other NZUs will give rise to taxable income.
11. On surrender for emissions liabilities, the surrender is generally treated as a deemed sale that occurs for the value allocated to the NZUs at balance date. This means that there is no income tax liability arising at the time of surrender either because the surrender occurs for zero value or is deemed to occur for cost and is offset against an available deduction for that cost.
12. The tax consequences are summarised in Figure | Hoahoa 1.

Figure | Hoahoa 1: Tax treatment of different types of NZUs

| Type of NZUs | Acquisition and year end | Surrender | Sale |
|----------------------------------|----------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Pre-1990 forest land NZUs | On allocation, NZUs were exempt income . NZUs are valued at zero at the end of the income year. | No tax consequences on surrender, as NZUs valued at zero . | If the land is held on capital account, amount received from the sale of NZUs is excluded income . If the land is held on revenue account, amount received from the sale of NZUs is taxable . No deduction for cost is available against the amount |

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|---------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| | | | received as the NZUs are valued at zero. |
| Post-1989 forest land NZUs | No tax consequences in the year of receipt. NZUs are valued at zero at the end of the income year. | No tax consequences on surrender, as NZUs are valued at zero when surrendered for post-1989 forest land. | The amount received from a sale is taxable . No deduction for cost is available against the amount received as the NZUs are valued at zero. |
| Replacement forest land NZUs | Deduction available for the cost of NZUs in the income year in which purchased. NZUs are valued at zero at the end of the income year. | No tax consequences on surrender, as valued at zero when surrendered for post-1989 forest land. | Not relevant as to qualify as a replacement forest land NZUs these must be acquired for surrender. |
| Standard NZUs (purchased NZUs and includes forest land NZUs that lose their status due to transfer) | No deduction available for the cost of NZUs in the income year in which purchased. NZUs are valued at cost at the end of the income year. | Valued at zero when surrendered for post-1989 forest land. Deduction available for cost of NZUs at the time of surrender. | The amount received from a sale is taxable . Deduction available for cost of NZUs at the time of sale. |

Examples

13. The above concepts are illustrated in the following examples.

Example | Tauria 1: treatment of NZUs on harvest of post-1989 forest (stock change accounting)

Flo's Forestry Ltd owns an ETS registered standard post-1989 forest and uses stock change carbon accounting. The forest is 28 years old and is harvested in January 2024.

Flo's Forestry Ltd had received 10,000 NZUs for removal activities. The receipt of these NZUs is valued as being zero at the end of each income year up until the year of disposal.

Flo's Forestry Ltd was required to surrender 8,000 NZUs for emissions liabilities at the time of harvest. The 8,000 NZUs surrendered are deemed to be sold for zero. No

deductions are available in respect of the cost or surrender of the NZUs or for any emissions liabilities.

The remaining 2,000 NZUs were sold on the market. An NZU had a market value of \$64 at the time of sale.

Flo's Forestry Ltd will have an income tax liability for the year ended 31 March 2024 for the amounts received from the sale of 2,000 NZUs on the market, which was \$128,000. The full amount received is taxable because no deductions are available for the cost of the NZUs.

Example | Taura 2: replacement forest land NZUs deductible

Ray's Radiatas Ltd owns an ETS registered standard post-1989 forest and uses stock change carbon accounting. The forest is 18 years old as at February 2024 and is not due to be harvested for several years.

Ray's Radiatas Ltd had received 16,000 NZUs for carbon removal activities. The receipt of these NZUs is valued as being zero at the end of each income year up until the year of disposal.

Ray's Radiatas Ltd needed funds, so decided to sell half the NZUs on the market. An NZU had a market value of \$64 at the time of sale.

8,000 NZUs were sold for \$512,000 in March 2024. Ray's Radiatas Ltd will have an income tax liability for the year ended 31 March 2024 for this amount. The full amount received is taxable because no deductions are available for the cost of the NZUs.

Prior to harvest, Ray's Radiatas Ltd will need to acquire a sufficient amount of NZUs to fund its emissions liability. Those NZUs will be replacement forest land emissions units. In the income year of acquiring those units, a deduction is available for the cost of those units.

In the income year of surrender, the NZUs surrendered (whether they are post-1989 forest land emissions units or the replacement forest land emissions units) will be treated as being sold for an amount of zero and no income tax liability will arise.

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About this document | Mō tēnei tuhinga

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