Inland Revenue
Te Tari Taake

Deadline for comment: 1 September 2020 . Reference ED0223

Operational Statement OS 20/0X

Non-resident employers' obligations to deduct PAYE, FBT and ESCT in cross-border employment situations

Introduction

Operational statements set out the Commissioner's view of the law in respect of the matter discussed and deal with the practical issues arising out of the administration on the Inland Revenue Acts.

This Statement clarifies the approach to take with regards to a non-resident employers' obligations to deduct PAYE, FBT and ESCT in certain cross-border employment situations.

All legislative references are to the Income Tax Act 2007 (the Act) unless specified otherwise.

Application

This statement provides general guidance to assist non-resident employers' in meeting their tax obligations regarding when to deduct PAYE, FBT and ESCT on cross-border situations. The Statement will apply from the date it is issued. However, the Commissioner will not be applying resources to examine positions taken by taxpayers prior to that date.

If you have any concerns about compliance with the tax obligations discussed in this statement, you should discuss the matter with a tax professional or Inland Revenue.

Summary

1. A non-resident employer has an obligation to withhold PAYE from a PAYE income payment made to an employee if:

    - The employer has made themselves subject to New Zealand tax law by having a sufficient presence in New Zealand; and
    - The services performed by the employee are properly attributable to the employer's presence in New Zealand.

2. A non-resident employer may have a Fringe Benefit Tax (FBT) or Employer Contribution Superannuation Tax (ESCT) liability for a benefit provided to, or a contribution made for an employee if:

    - The employer has made themselves subject to New Zealand tax law by having a sufficient presence in New Zealand; and
    - The services performed by the employee are properly attributable to the employer's presence in New Zealand.

3. There is no PAYE withholding obligation if a PAYE income payment is "non-residents' foreign sourced income" for the employee.

4. There is also no PAYE withholding obligation for a PAYE income payment made to a non-resident employee working in New Zealand if the domestic exemption in s CW 19 applies, or a Double Taxation Agreement (DTA) gives relief from source taxation such as where the employee is in New Zealand 183 days or less in a twelve-month period.

Discussion

5. This Statement provides guidance on whether employers have PAYE, FBT and ESCT obligations in various cross-border employment situations.

6. The different situations involve different combinations of; the residence of the employer, the residence of the employee, and the country in which the employment services are performed.

Non-resident employers

Territorial limitation - Presence

7. The PAYE rules[1] are intended to apply to New Zealand residents or matters over which New Zealand has jurisdiction. A non-resident may make themselves subject to New Zealand law (including the PAYE rules) by having a sufficient presence in New Zealand (*Alcan*[2] and *Clark*[3]). The nature and extent of the required presence may vary depending on the facts in each case.

8. If a non-resident employer has a trading presence in New Zealand, such as carrying on operations and employing a workforce for the purpose of trade, this would normally be sufficient for the employer to have a PAYE withholding obligation for employees they pay PAYE income payments to.

9. A sufficient presence for a non-resident employer would also include having a permanent establishment, a branch, contracts that are entered into in New Zealand and performing contracts in New Zealand with employees based here.

10. An address for service (in New Zealand) is also another indication that the non-resident employer has made themselves subject to New Zealand law.

11. A sufficient presence would <u>not</u> include a situation where an employee chooses (as a matter of personal preference) to undertake their employment activities in New Zealand where those activities had no necessary connection to New Zealand, and where this was the non-resident employers' <u>only</u> connection with New Zealand.

12. It is considered that merely having employees in New Zealand would not, of itself, constitute a presence of the employer sufficient to subject the employer to New Zealand's jurisdiction. Therefore, the degree to which an employee "represents" the employer in activities in New Zealand will be one of the things to take into account to decide whether the presence is sufficient to mean that the employer has submitted themselves to New Zealand's jurisdiction.

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1 Section RD 2 of the Income Tax Act 2007.

2 *Alcan New Zealand Ltd v CIR* (1993) 15 NZTC 10,125 (HC).

3 *Clark (Inspector of Taxes) v Oceanic Contractors Inc* [1983] 1 All ER 133 (HL).

13. It is also considered that having a parent, subsidiary or associate would not be enough in itself to have a presence in New Zealand without something more, such as any of the factors mentioned in paragraphs [8], [9] and [10].

Example one

Boston Architects (BA) is an architect firm based in the USA. BA employs George who lives in Wellington. George participates in virtual meetings and completes all of his work in Wellington but as BA does not have any New Zealand clients, all the work is sent back to the US electronically.

Would BA have an obligation to deduct PAYE?

No. There would be no obligation to deduct PAYE as George's employment activities have no necessary connection to New Zealand, and the only connection to New Zealand is that George lives there.

Example two

George's work is highly respected and quite specialised, as he only designs schools. When there is a project to build a new school in Wellington, George is engaged (through BA) to provide his expertise and advice.

Would BA have an obligation to deduct PAYE?

No. George's expertise and advice does not require him to be in New Zealand to give it. He is not carrying on operations or employing a workforce (on behalf on BA) in New Zealand to give this advice. Although there is a connection to New Zealand while undertaking his employment activities for this project, this is not enough to impose a PAYE obligation on BA.

Example three

George's work on the school went well. When a new school project comes up, George is engaged (through BA) and is put in charge of dealing with the client and running the project. While some work is also done in the US, 3 more staff are hired in Wellington to help George out. It is hoped that this might be the start of more New Zealand work for BA.

Would BA have an obligation to deduct PAYE?

Yes. In this situation there is a sufficient presence in New Zealand for BA to have an obligation to deduct PAYE. George (on behalf of BA) is carrying on operations for the purpose of its business, he is entering into and performing contracts in New Zealand (on behalf of BA), and additional staff have been employed in connection with the project being undertaken in Wellington.

Services performed

14. Where a non-resident employer has made themselves subject to New Zealand law by having a sufficient presence in New Zealand, the extent of the non-resident employer's obligations will be limited to matters that are properly attributable to their New Zealand presence.

15. This means that if, for example, a non-resident employer carries on a business in New Zealand and pays wages to an employee who performs services that are properly attributable to the New Zealand business, the employer will have an obligation to withhold PAYE from those wages.

16. Most of the time the PAYE withholding obligations will arise where the employee is based in New Zealand.

17. However, it is possible that a New Zealand resident employee could perform services overseas that are properly attributable to the non-resident employers' New Zealand presence.

18. For example, a New Zealand resident employee may be temporarily based overseas investigating the purchase of new equipment to be used in the employers' New Zealand operations. The services of the employee would be properly attributable to the New Zealand operations and, therefore, the non-resident employer would be required to withhold PAYE from PAYE income payments made to the employee.

Section CW 19 - Amounts derived during short-term visits

19. Under s CW 19, income that a non-resident person derives in a tax year from performing personal or professional services in New Zealand during a visit is exempt income if:

- The visit is for 92 or fewer days (counting the day of arrival and departure as whole days);
- The person is present in New Zealand for 92 days or fewer in total in each 12-month period that includes the period of the visit;
- The services are performed for or on behalf of a person (which could include an employer) who is not resident in New Zealand;
- The income is chargeable with income tax in the country in which the person is resident.

20. Exempt income is excluded from the definition of "salary or wages" and, therefore a "PAYE income payment[4]" is also exempt under this provision. No PAYE withholding obligation will arise for any payments described in s CW 19.

Relief given by a DTA

21. No PAYE withholding obligation will arise for PAYE income payments where a DTA provides the employee with relief from New Zealand taxation.

22. A DTA may have the effect of denying New Zealand any taxing rights for an amount of employment income derived by a non-resident employee for employment services performed in New Zealand. This may occur if the non-resident employee is in New Zealand for in total, 183 days or less in a twelve-month period, the remuneration is paid by a non-resident employer, and the remuneration is neither borne by nor deductible in determining the profits attributable to a permanent establishment which the employer has in New Zealand.

23. Please note, the example above assumes the wording of the DTA as described, although this wording may vary slightly within different DTA's with regards to the taxing rights for employment income.

[4] "PAYE income payment" is principally defined by reference to "salary or wages" which excludes an amount of exempt income (s RD 5(1)(c)(i)).

New Zealand resident employers

24. An issue with regards to payments by a New Zealand resident employer is whether there is an obligation to withhold PAYE where the PAYE income payment is paid to a non-resident employee for work performed overseas.

25. It is considered that a New Zealand resident employer does not have any obligation to withhold PAYE from a PAYE income payment that is "non-residents' foreign-sourced income"[5] for the employee. This is because:

- The Core Provisions indicate that the purpose of the Act is to tax assessable income. Income tax is generally not intended to apply to non-residents' foreign-sourced income; certainly not in the case of employment income.
- It would be inconsistent with the purpose of the Act to impose a PAYE withholding obligation on the employer in relation to such income.

Employer superannuation contribution tax (ESCT)

26. A non-resident employer who has made themselves subject to New Zealand's law by having a sufficient presence in New Zealand, and who pays PAYE income payments, may have a liability for ESCT. Like the situation for PAYE on a PAYE income payment, the employer's superannuation contribution would have to relate to employment services that are properly attributable to the employer's presence in New Zealand.

27. This means that, for a non-resident employer, an ESCT liability will normally only arise when the employee is performing services in New Zealand. However, a non-resident employer could have an ESCT liability for a contribution made for the benefit of an employee working overseas, if the services provided by the employee overseas are properly attributable to the employer's New Zealand presence.

28. A non-resident employer who has not made themselves subject to New Zealand's jurisdiction has no liability for ESCT. This is so whether or not the employee is a New Zealand resident and whether or not the employment services are performed in New Zealand or overseas.

Fringe benefit tax (FBT)

28. A non-resident employer who has made themselves subject to New Zealand's jurisdiction by having a sufficient presence in New Zealand, and who pays PAYE income payments, will have a liability for FBT (subject to the discussion below). Like the situation for PAYE on a PAYE income payment, for an FBT liability to arise the provision of a fringe benefit to an employee would have to be a benefit provided to an employee in connection with the employer's presence in New Zealand.

29. This means that, for a non-resident employer, an FBT liability will normally only arise where the employee is performing services in New Zealand. However, a non-resident employer could have an FBT liability for a benefit provided to an employee working overseas, if the services provided by the employee overseas are properly attributable to the employer's New Zealand operations.

30. An FBT liability will also depend on other factors, including whether the employee has received a PAYE income payment in the period. Additionally, s CX 26

[5] As defined in s BD 1(4).

provides that a benefit is not a fringe benefit to the extent to which it is received in a quarter or an income year in which they derive one or more PAYE income payments, all of which are not liable for income tax.

31. A non-resident employer who has not made themselves subject to New Zealand's jurisdiction has no liability for FBT.

This Operational Statement is signed on XX Month 2020