

# New Zealand: pre-migration trusts

Henry Brandts-Giesen details some options offered by New Zealand trusts



#### ABOUT THE AUTHOR

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New Zealand (NZ) is a popular destination for individuals and families who for lifestyle, political, social, professional or other reasons wish to leave their country of domicile for a new life 'down under.' Increasing numbers of new arrivals from (in particular) Britain, Ireland, Southern Africa and Asia are arriving in NZ and many of these are unaware of the significant tax and succession planning advantages that may be available to them.

#### Jurisdictional advantages

NZ has grown in prominence over recent years for a variety of reasons. In particular its tax neutrality as regards 'foreign' trusts and limited partnerships has proved popular with high-net-worth individuals. NZ is a respected member jurisdiction of both the Organisation for Economic Cooperation and Development (OECD) and the Financial Action Task Force (FATF), with sound commercial, professional and judicial foundations.

In addition to the favourable tax regime available to non-residents, new migrants and returning expatriates, who have been absent from NZ for a continuous period of ten years or more, are also entitled to a 48 month tax exemption in respect of all offshore sourced income, even if that income is remitted into NZ during that time.

Furthermore, unlike in many countries from whence new migrants come, the NZ

Inland Revenue does not impose capital gains tax (except in limited circumstances), inheritance tax or estate duty, stamp duty or land development tax.

#### Pre-migration wealth structuring opportunities

In April 2006, the NZ government amended the *Income Tax Act 2004* to provide a four year exemption from income tax on foreign-sourced income earned by new migrants to NZ and returning New Zealanders who have been non-resident for tax purposes for ten years or longer. These persons are now known as 'transitional residents.' Tax may still be payable at source in the country in which income or capital gains arise, but the income can be freely remitted to NZ without fear of double taxation. With careful advice and planning in both the jurisdiction of origin and New Zealand, income and capital gains taxes might be deferred or reduced and some inheritance and estate taxes may be avoided altogether.

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These new rules provide transitional residents an exemption from income tax with regards income derived from any country other than NZ, in the form of dividends, interest, rents, and an exemption from the application of the foreign investment fund tax regime.

The exemption will endure for a period of 48 months commencing from the first day of the month in which the individual acquires a 'permanent place of abode' in NZ.

Examples of the exemption in operation:

1. Laurence, an accountant from London, visits NZ on 1 February 2008 for an interview with a 'Big 4' firm. He relocates to NZ permanently and acquires a permanent place of abode on 1 May 2008. He is subsequently deemed to be tax resident from 1 February 2008 under the 183 day rule. He has never been tax resident in NZ before. Laurence would qualify for the exemption. Although he is treated as tax resident from 1 February, he doesn't begin to satisfy the requirements for being resident until 1 May. His exemption would run from 1 February 2008 to 31 May 2012.
2. Schalk, a professional rugby player from Cape Town, arrives in NZ on 1 June 2006 to play for the Crusaders in the Super 14. He stays for three months (92 days). He comes back to NZ on 1 March 2007 and stays for another 3 months (92 days). By the time he leaves on 31 May 2007 he has been in NZ for more than 183 days in a 12 month period and is deemed to be tax resident from 1 June 2006. Schalk relocates to NZ and establishes a permanent place of abode here on 1 January 2008. He has never been tax resident in NZ before.

Schalk would qualify for the exemption. Although he is deemed to be tax resident from 1 June 2006, he does not begin to satisfy the residence requirements until after that date. His exemption would run from 1 June 2006. (Further investigation would be required to determine whether

he is then eligible to play for the All Blacks!)

3. Rachel, an investment banker from Auckland, leaves New Zealand and ceases to have a permanent place of abode here on 30 September 2006. She returns on holiday from time to time to visit friends. Each time, she is only present in NZ for a couple of weeks a year. Her last holiday here is from 1 to 14 August 2016. On 1 December 2016, Rachel decides to move back to NZ to live. She acquires a permanent place of abode on that date. She was last resident on 30 September 2006 - just over 10 years ago. On 19 May 2017, when she has been present for 184 days, she is deemed to be tax resident from 1 August 2016.

Rachel would qualify for the exemption. She began to satisfy the requirements of the Act for being a resident on 1 December 2016 when she reacquired a permanent place of abode in NZ. At that time she had not been resident in NZ in the preceding 10 years. Her exemption runs from 1 August 2016 to 31 December 2020.

### NZ foreign trusts

Crucially for succession planning and asset protection purposes, the exemption also applies to trusts where the settlor of the trust is a transitional resident. Individuals resident in certain jurisdictions have a unique opportunity prior to migration to gift assets into a trust without incurring the gift duties generally applicable to NZ resident settlors.

In order to achieve effective succession of wealth to the next generation (and provided the trust is established at a time where there are no known creditors likely to exercise rights of recovery) a highly effective asset holding vehicle for the inbound migrant is the NZ foreign trust.

A NZ foreign trust is a trust settled by a person who is not resident in NZ with

an NZ resident trustee from an approved organisation. The beneficiaries may, or may not, be resident in NZ. If these requirements are met and the income is derived from outside NZ then no tax is payable in NZ. The settlor must be non-resident in any one year of distribution in order for the trust to be tax neutral in NZ (any income arising in NZ would be subject to tax at 33 per cent).

If the settlor subsequently migrates to NZ and becomes a tax resident, the settlor has 12 months in which to nominate whether or not the trust is to become a complying trust (in other words, a normal domestic trust). If the settlor or trustee fails to nominate, the trust will automatically become a non-complying trust and will be subject to penal rates of tax on capital gain.

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Therefore, as previously discussed, a settlor, upon gaining residence in NZ for tax purposes, will qualify for a 48 month exemption on non-NZ sourced income. After that period, the settlor's status will change from transitional resident to tax resident. If, prior to migrating, the settlor had established an NZ foreign trust, then the settlor/trustee has a further 12 months to nominate whether or not the trust is to become a complying trust – therefore providing a further 12 month exemption from tax on non-NZ sourced income.

In addition to the five year exemption from tax on non-NZ source income, the trust will also allow the settlor to transfer wealth from one generation to the next without the concerns of gift duties, probate issues,

challenges to wills, or the concern of a spendthrift in the family.

### Potential pitfalls

However, it should be emphasised that there are potential pitfalls and it is essential that good advice be taken prior to arriving in NZ so that it is clear when the time period begins to run.

If the foreign trust is chosen as the most appropriate vehicle, the timing of the settlement becomes crucial. As Schalk from Cape Town discovered in example two above – there can be 'look, see, decide' trips made prior to the move to NZ by the settlor, which count towards residency.

If the trust is settled after one of those trips and the residency is deemed to have occurred prior to the settlement, the trust will not be a foreign trust. Therefore it will either be a complying trust, which is liable for income on all the assets worldwide from settlement, or it will be a non-complying trust, again liable for all worldwide income to the Inland Revenue, and at penal rates. The settlor must have the trust established as early as possible before the scouting expeditions to New Zealand. Alternatively, if some trips have been made already, the settlor will need to be advised as to the 183 day rule, so that the final journey to NZ falls six months after the trust is established and so that no visits have been made to NZ since the establishment of the trust, thereby avoiding the trap of losing the transitional status benefits.

In summary, a pre-migration trust can offer some significant advantages to individuals migrating to NZ, including a further 12 month extension to the 48 month exemption from tax on non-NZ sourced income. However, it is very important to carefully consider the timing of the trust establishment and transfer of the assets to the trust in order to ensure that the maximum tax benefits are enjoyed. ■