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**QWBA0118 – Income Tax – Meaning of “excessive remuneration” and “excessive profits or losses” paid or allocated to relatives, partners, shareholders or directors**

1. The New Zealand Law Society (Law Society) appreciates the opportunity to comment on the *QWBA0118 – Income Tax – Meaning of “excessive remuneration” and “excessive profits or losses” paid or allocated to relatives, partners, shareholders or directors* Exposure Draft (ED).
2. The ED brings into one document the Commissioner’s position on application of the anti-avoidance provisions in the Income Tax Act 2007 to alter a taxpayer’s position under the following four scenarios:
  - (a) Excessive remuneration or income paid to a relative;
  - (b) Excessive profit or losses allocated to a partner in a partnership;
  - (c) Excessive remuneration paid to a shareholder or director; and
  - (d) Excessive allocation of income from a look through company to a relative aged under 20.
3. As to (a), when determining whether remuneration is excessive, the Commissioner reiterates the criteria she will consider from the 1996 TIB. Those are:
  - the nature of the services and the circumstances in which they will be or are performed;
  - the knowledge and skills required to carry out the services, including any particular qualifications;
  - the amount of payment that the person carrying on the duties would be paid by another independent employer for like services;
  - the locality where the duties are being performed; and
  - the amount the taxpayer would be prepared to pay an arm’s length employee undertaking similar duties.
4. Those criteria make it clear that in almost every case, the considerations of what is “excessive” remuneration turn on their own facts. Because of that, examples are helpful.
5. However, the examples in the ED are of limited practical help. The example relating to excessive remuneration paid to a relative confirms that the Commissioner would not challenge the

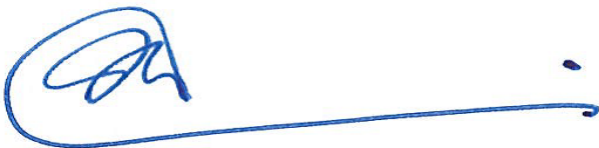
quantum of wages (\$20,000) paid to a taxpayer's 17 year old daughter if those wages are considered to be within the industry standard for similar work performed.

6. In contrast, the Commissioner would disallow a deduction for the same wage paid to the taxpayer's 5 year old son. That outcome is obvious and any other outcome would be illogical.
7. It would be more helpful for the Commissioner to include examples that are closer to the boundary. Such examples could include a 14 or 15 year old who undertakes casual work within his or her parent's business, such as filing or cleaning in the evening or weekends. The business could be conducted from home. In that scenario it begs the question, at what point do regular household chores become tasks that attract a deductible wage? It would be helpful for taxpayers if examples such as that one are included in the ED.
8. The Commissioner's positions in respect of the remaining three scenarios in (b) to (d) are consistent with the case law and her statutory obligations when considering the application of the anti-avoidance provisions. The examples given for each scenario are equally as unhelpful as the first one above. In each example, there is no question as to the way in which the Commissioner ought to apply the anti-avoidance provisions. The outcomes are obvious and the usefulness of the examples to taxpayers is limited.
9. The ED concludes with brief commentary on the similarity of the subject matter in this ED and the subject matter in the *Penny and Hooper* case. The Commissioner distinguishes the (a) to (d) scenarios from *Penny and Hooper* as being about excessive remuneration rather than the diversion of income. The Commissioner notes that her position on the later scenario is contained in the Interpretation Statement on Tax Avoidance released last year. Generally we are comfortable with the Commissioner's stated position of the law.
10. However, the Commissioner has an opportunity in this ED to provide real and useful examples of situations in which the application of the anti-avoidance provisions would be contentious. She ought to publish such examples and her position in respect of them to assist taxpayers to meet the standards she expects.

### Conclusion

11. This submission was prepared with the assistance of the Law Society's Tax Law Committee. If you wish to discuss this further please do not hesitate to contact the committee convenor Neil Russ, through the committee secretary Rhyn Visser (04 463 2962 or [rhyn.visser@lawsociety.org.nz](mailto:rhyn.visser@lawsociety.org.nz)).

Yours sincerely



Allister Davis  
**Vice-President**