Coversheet: Taxation of non-bank securitisation vehicles

Advising agencies	*Inland Revenue*
Decision sought	*The analysis and advice has been produced for the purpose of informing final decisions to proceed with policy changes to be taken by or on behalf of Cabinet*
Proposing Ministers	*Steven Joyce (Finance) and Hon Judith Collins (Revenue)*

Summary: Problem and Proposed Approach

Problem Definition

What problem or opportunity does this proposal seek to address? Why is Government intervention required?

Securitisations can have several commercial benefits, compared with other funding mechanisms, such as risk management, balance sheet improvement, credit enhancement, lower cost of funding, and access to a wider pool of lenders.

An important commercial objective of a securitisation is maintaining tax neutrality for the special purpose vehicle (SPV) used. There is a concern that the current tax rules may not allow for tax neutrality for the SPV to be achieved, and so may be discouraging securitisations.

The Government wants to ensure that tax settings are not discouraging some businesses from realising the commercial benefits of securitisations.

Proposed Approach

How will Government intervention work to bring about the desired change? How is this the best option?

There is currently a securitisation regime in the Income Tax Act 2007 which applies in respect of certain securitisations undertaken by financial institutions. The effect of the regime is that there are no tax consequences arising from the transactions between the financial institution and the SPV.

Extending that regime to cover businesses that are not financial institutions would ensure that securitisations that meet the criteria of the regime are tax neutral. This would remove a tax disincentive to undertaking securitisations, which is likely to produce growth given the commercial benefits securitisations provide.

Section B: Summary Impacts: Benefits and costs

Who are the main expected beneficiaries and what is the nature of the expected benefit?
The main expected beneficiaries of the proposal are New Zealand businesses with large books of trade credits or other receivables (Originators) that may wish to raise funding by using those receivables as security. The proposal should reduce compliance costs by removing the requirement for the SPV to return tax itself, and by removing the need for the Originator to calculate and return tax where the transferred receivables remain economically within the Originator's group. In terms of equity and fairness, taxing securitisations in accordance with their economic substance, would ensure that tax does not penalise (or incentivise) securitisations compared with other forms of fund raising. This would mean that the benefits of securitisations can be enjoyed more broadly.

Where do the costs fall?
The fiscal cost of the proposal for the Government is expected to be minor, as securitisations are typically structured to prevent tax arising where possible. There could be a fiscal cost from not recognising the transfer of assets to the SPV, although this would be the same as if the securitisation had not occurred. It is not expected that implementation of the proposal would raise any administrative issues for Inland Revenue. The proposal would reduce compliance costs for taxpayers, and would reduce tax costs to the extent that securitisations are not currently structured to prevent tax arising.

What are the likely risks and unintended impacts, how significant are they and how will they be minimised or mitigated?
A potential risk that was identified is that expanding the securitisation rules could open up the possibility of those rules being used to avoid tax on what is in substance a true sale to a third party. However, it is proposed that the expanded rules include a requirement that the securitised assets are treated as held by the Originator or another company in the group in its consolidated accounts under the International Financial Reporting Standards (IFRS). It is considered that this requirement should mitigate the risk that the new rules could be used to avoid tax on what is in substance a true sale to a third party.

Identify any significant incompatibility with the Government's 'Expectations for the design of regulatory systems'.
There is no incompatibility between this regulatory proposal and the Government's 'Expectations for the design of regulatory systems'.

Section C: Evidence certainty and quality assurance

Agency rating of evidence certainty?
We are reasonably confident in terms of the evidence on which the proposal is based, given that we have undertaken targeted consultation with interested and affected parties involved in New Zealand's securitisation market.

To be completed by quality assurers:

Quality Assurance Reviewing Agency:
Inland Revenue
Quality Assurance Assessment:
The Quality Assurance reviewer at Inland Revenue has reviewed the *Taxation of non-bank securitisation vehicles* Regulatory Impact Assessment prepared by Inland Revenue and associated supporting material and considers that the information and analysis summarised in the Regulatory Impact Assessment **meets** the Quality Assurance criteria.
Reviewer Comments and Recommendations:
The reviewer's comments on earlier versions of the Regulatory Impact Assessment have been incorporated into the final version.

Impact Statement: Taxation of non-bank securitisation vehicles

Section 1: General information

Purpose
Inland Revenue is solely responsible for the analysis and advice set out in this Regulatory Impact Assessment, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing final decisions to proceed with a policy change to be taken by or on behalf of Cabinet.

Key Limitations or Constraints on Analysis
It is understood that the current tax settings could be discouraging some businesses from realising the commercial benefits of securitisations. We cannot be sure of the scope of the problem, but have gleaned from consultation that the current tax settings are a disincentive to many taxpayer's undertaking securitisations. We also understand that currently securitisations are typically structured to prevent tax arising where possible. However, the extent to which tax is currently paid in respect of securitisation transactions is not known, so the potential revenue cost is not able to be quantified. That said, removing a tax barrier would be expected to result in more businesses being able to enjoy the commercial benefits of securitisations, and the tax neutrality of those transactions would be no different than if the securitisation had not occurred.
Responsible Manager (signature and date):
Peter Frawley Policy Manager Policy & Strategy Inland Revenue July 2017

Section 2: Problem definition and objectives

2.1 What is the context within which action is proposed?

A securitisation is a funding mechanism that involves issuing marketable securities that are backed by the expected cash flows from specific assets. New Zealand businesses with large books of trade credits or other receivables (Originators) may wish to raise funding by using those receivables as security. To do this, the Originator of the receivables transfers them to a special purpose vehicle (SPV), and the SPV then issues securities (typically debt instruments) to lenders. The SPV is structured to be bankruptcy remote from the Originator, so that the SPV's assets cannot be accessed by the Originator's creditors. In New Zealand (and internationally, in most cases) this means that the SPV is typically a trust.

A securitisation can have several commercial benefits compared with a regular loan, such as risk management, balance sheet improvement, credit enhancement, lower cost of funding, and access to a wider pool of lenders.

An important commercial objective of a securitisation is maintaining tax neutrality while ensuring the SPV is bankruptcy remote from the Originator. It is particularly important to ensure that the SPV itself is not exposed to a tax liability, as this can affect its credit rating.

2.2 What regulatory system, or systems, are already in place?

There is currently a securitisation regime in the Income Tax Act, but it applies only in respect of certain securitisations undertaken by financial institutions. Those rules were introduced as a result of the Reserve Bank of New Zealand's (the RBNZ's) response to the global financial crisis. Broadly, the RBNZ agreed to provide additional liquidity support for banks, provided the bank offered collateral securitised AAA rated residential mortgages as securities. As part of the security arrangements for this funding, the RBNZ required these mortgages be held by a bankruptcy remote special purpose vehicle (SPV).

In the absence of a specific regime, there would have been potential tax consequences arising from the use of SPVs, as required to access the RBNZ's liquidity support. The government determined that the tax rules should not impede the RBNZ measures assisting the stability of the financial system at that time. As a result, new provisions were introduced into the Act in 2009 to achieve tax neutrality.

Those provisions were extended in 2010, after the RBNZ introduced a new bank liquidity policy which included measures to require banks and certain finance companies to lengthen their funding to better match their lending terms. The provisions in the Act now apply to financial institutions generally (not just registered banks) and to covered bond programme SPVs (economically very similar to the residential mortgage-backed security SPVs).

The tax effect of the provisions is that the SPV is treated as transparent. The SPV's property, activities, status, intention and purpose are attributed instead to the financial institution. The financial institution is also treated as being party to any arrangement to which the SPV is a party, and the SPV is treated as not being that party to the arrangement.

Practically, this means that there are no tax consequences arising from the transactions between the financial institution and the SPV, while the SPV remains qualifying. Also, all transactions between the SPV and third parties are included in the financial institution's tax return.

The restriction of the current rules to securitisations by financial institutions is a consequence of the rules being introduced to facilitate financial institutions accessing the RBNZ's liquidity support during the global financial crisis. Wider application of the rules was not necessary for that purpose. However, there is no particular policy reason why the rules should not apply more broadly to corporate securitisations.

2.3 What is the policy problem or opportunity?

There is a concern that the current tax rules may not allow for tax neutrality for the SPV to be achieved, and so may be discouraging securitisations. The current rules can also trigger a tax liability on transfer of the receivables into the SPV. While potentially less serious than SPV taxation, this issue can create a large administrative burden, as all the receivables need to be valued for tax purposes. The concern in relation to the tax treatment of securitisations by businesses that are not financial institutions arises as a result of the application of the general trust rules and the financial arrangements rules.

Trusts can derive non-cash income, and there is an issue about whether this can be distributed as beneficiary income (in which case the beneficiary pays the tax on the income) or whether it must remain as trustee income (in which case the trustee pays the tax). In 2012, Inland Revenue published Interpretation Statement *IS 12/02 "Income Tax – whether income deemed to arise under tax law, but not trust law, can give rise to beneficiary income"*. The Interpretation Statement concluded that non-cash income can only be distributed to a beneficiary where there is a cash amount available for distribution. This can be an issue for SPVs, as securitisations are typically structured so the SPV has no cash income. This means that any non-cash income derived could result in a tax liability at the trust level.

There is also an issue arising because of the application of the financial arrangements rules, which require a "base price adjustment" to be carried out when any financial arrangement is transferred, which can trigger a tax liability. Although potentially less serious than SPV taxation, this issue can create a large compliance burden and result in compliance costs for taxpayers (the Originator and the SPV), as all the receivables need to be valued for tax purposes.

New Zealand has a small but active securitisation market, although there has been reduced activity following the global financial crisis. If the problem is not addressed, then the current tax settings may discourage some businesses from realising the commercial benefits of securitisations.

2.4 Are there any constraints on the scope for decision making?

There are no particular constraints on the scope for decision making.

2.5 What do stakeholders think?

As noted above, this issue was originally raised by the private sector, with the suggestion that the current securitisation regime in the Income Tax Act be extended to other corporate securitisations to remove the tax disincentive to undertaking securitisations.

Inland Revenue has undertaken targeted consultation on the proposal with interested parties. Given that the proposed amendments would only be relevant to those involved in New Zealand's securitisation market, officials considered that targeted consultation was sufficient. We consulted, by letter and subsequent discussions, with:

- Chartered Accountants Australia and New Zealand;
- the New Zealand Law Society (the NZLS);
- the Corporate Taxpayers Group;
- the Financial Services Council of New Zealand;
- the Financial Services Federation;
- Chapman Tripp on behalf of the Trustee Corporations Association and New Zealand Guardian Trust;
- EY;
- Bell Gully (who received the consultation proposed through the NZLS); and
- PwC.

Submitters were supportive of the proposal to extend the securitisation regime beyond financial institutions to other corporate securitisations. Submitters commented that widening the scope of the regime in this way would ensure a tax neutral outcome for securitisations undertaken by corporates that are not financial institutions. The issues raised at consultation are discussed in section 3 below.

Section 3: Options identification

3.1 What options are available to address the problem?

Option 1 (status quo)

Option 1 is to retain the status quo. Under the status quo, the tax settings may discourage some businesses from realising the commercial benefits of securitisations, as these arrangements can have higher tax costs and compliance costs than other funding arrangements.

Option 2 (extension of current rules)

Option 2 is to extend the current securitisation regime (in sections HR 9 to HR 10) beyond financial institutions to other corporate securitisations.

Option 3 (extension of current rules with requirement of recourse to the Originator)

Option 3 is to extend the current securitisation regime beyond financial institutions to other corporate securitisations, but with an additional requirement of the lenders having recourse to the Originator.

Arguably there is a potential risk that just extending the current rules (option two) could provide opportunities for the rules to be used to avoid tax on what is in substance a true sale to a third party.

Introducing an additional requirement (for non-financial institution securitisations) of recourse to the Originator is one possible way of reducing the risk of the provisions being used to avoid the tax consequences of a true sale to a third party. However, it would seem that this risk would be mitigated by the requirement in the current provisions that the financial arrangements (the receivables) held by the SPV are treated as held by the Originator in its consolidated accounts under IFRS.

Option 4 (extension of current rules with additional modifications)

Option 4 is to extend the current securitisation regime beyond financial institutions to other corporate securitisations, but with a number of modifications, as suggested by submitters during consultation (discussed further in section 5, below), namely:

- The regime could be extended in scope for financial institutions, beyond the types of securitisations currently covered (those involving residential mortgage-backed securities and covered bond programmes). The regime would apply more broadly for non-financial institutions, so it makes sense for financial institutions to also be able to benefit from the regime for other securitisations they may undertake.
- The regime could be extended to cover securitisations involving assets/receivables other than financial arrangements. For example, it is common for trade receivables and operating leases, which are excepted financial arrangements, to be securitised.
- The requirement for the securitised assets to be recognised in the Originator's consolidated IFRS financial statements could be amended so that recognition in the consolidated IFRS financial statements of a company in the same group would suffice.
- The regime should be elective, given that it removes a tax barrier. This would ensure that existing arrangements are not adversely affected if they have been structured to achieve a different result than what would arise under the regime.

3.2 What criteria, in addition to monetary costs and benefits, have been used to assess the likely impacts of the options under consideration?

The generic tax policy process (GTPP) includes a framework for assessing key policy elements and trade-offs of proposals. This framework is consistent with the Government's vision for the tax and social policy system, and is captured by the following criteria:

- *Efficiency and neutrality* – the tax system should bias economic decisions as little as possible;
- *Fairness and equity* – similar taxpayers in similar circumstances should be treated in a similar way;
- *Efficiency of compliance* – compliance costs for taxpayers should be minimised as far as possible;
- *Efficiency of administration* – administrative costs for Inland Revenue should be minimised as far as possible.

Efficiency and fairness are the most important criteria. It is generally worth trading-off increased compliance costs or administration costs for gains in these two criteria.

3.3 What other options have been ruled out of scope, or not considered, and why?

No other options have been ruled out of scope.

Section 4: Impact Analysis

Marginal impact: How does each of the options identified at section 3.1 compare with the counterfactual, under each of the criteria set out in section 3.2?

	Option 1 (status quo)	**Option 2 (extension of current rules)**	**Option 3 (extension of current rules with requirement of recourse to the Originator)**	**Option 4 (extension of current rules with additional modifications)**
Equity (fairness)	**0**	+ Taxes securitisations more fairly compared with other fund raising.	+ Taxes securitisations more fairly compared with other fund raising.	+ Taxes securitisations more fairly compared with other fund raising.
Economic (including efficiency)	**0**	+ Removes a tax disincentive to undertaking securitisations. More efficient, as removes need to recognise a transfer that does not have economic consequences.	+ Removes a tax disincentive to undertaking securitisations. However, narrows the scope of the rules, so reduces the potential efficiency and economic gains.	++ Removes a tax disincentive to undertaking securitisations. More efficient, as removes need to recognise a transfer that does not have economic consequences. Broadening of scope means the benefits of securitisations can be enjoyed more broadly.
Administrative	**0**	**0** No significant change in costs for Inland Revenue.	**0** No significant change in costs for Inland Revenue.	**0** No significant change in costs for Inland Revenue.
Compliance	**0**	++ Significantly reduces compliance costs for securitisers, as they will not have to have valuations of the receivables.	+ Significantly reduces compliance costs for securitisers, as they will not have to have valuations of the receivables. But narrowed scope means compliance savings will be enjoyed by fewer taxpayers.	++ Significantly reduces compliance costs for securitisers, as they will not have to have valuations of the receivables.. And by broadening scope, compliance savings will be enjoyed by more taxpayers.
Overall assessment	**0**	+	+	++

Key:

++ much better than doing nothing/the status quo
+ better than doing nothing/the status quo
0 about the same as doing nothing/the status quo
- worse than doing nothing/the status quo
- - much worse than doing nothing/the status quo

Section 5: Conclusions

5.1 What option, or combination of options, is likely best to address the problem, meet the policy objectives and deliver the highest net benefits?

We consider that option 4 is the best option to ensure that the commercial benefits of securitisations are achieved while maintaining the integrity of the tax rules. As noted, this option would extend the current securitisation regime beyond financial institutions to other corporate securitisations, but with a number of modifications (discussed below). The suggested modifications arose out of feedback received during consultation, so officials consider that these modifications would best ensure that the objectives of the proposal are met, while ensuring the regime does not provide tax incentives for securitisations, or facilitate tax avoidance.

Option 1, retaining the status quo, would mean that the tax settings would continue to discourage some businesses from realising the commercial benefits of securitisations, which can have higher tax costs and compliance costs than other funding arrangements. The Government wants to remove a tax disincentive to undertaking securitisations, given the commercial benefits they provide. The status quo is not supported.

Option 2 is to extend the current securitisation regime to non-financial institutions. The extended regime would apply to a broader class of securitisable assets than those currently covered for financial institutions, as the type of securitisations currently within the scope of the regime (residential mortgage-backed securities and covered bond programmes) are not typically undertaken by non-financial institutions. However, the current consolidation requirement may be too restrictive for securitisations other than those currently covered. The current consolidation requirement is that the securitised assets are treated as held by the Originator in its consolidated financial statements under IFRS. However, as discussed further below, submitters have commented that it is often the case in corporate securitisations that the securitised assets are de-recognised by the Originator but are recognised in the consolidated financial statements of another group company. Option 2 would be somewhat limited in terms of the securitisations it would apply to, which means the tax settings would continue to discourage some securitisations. As a consequence, option 2 is not supported.

Option 3 is to extend the current securitisation regime to non-financial institutions to a broader class of securitisable assets than those currently covered for financial institutions, but with the additional requirement of the lenders (the investors in the SPV) having recourse to the Originator. The possibility of an additional requirement of recourse to the Originator was suggested as an option in consultation to ensure that the provisions could not be used to avoid tax on what is in substance a true sale of financial assets to a third party. However, we consider that a requirement of recourse to the Originator is less preferable to other options for mitigating that risk. In particular, as discussed further below, the additional requirement of recourse to the Originator would be inconsistent with the commercial objective of ensuring that the SPV is bankruptcy remote from the Originator, and so would undermine the benefits of a securitisation. Submitters commented that from a practical point of view the Originator would not want to guarantee the SPV's obligations, and would just borrow itself if it were necessary for the investors to have recourse to the Originator. This would mean that from a practical point of view option 3 might be little utilised, which is contrary to the objective of removing a tax disincentive so that the benefits of securitisations can be enjoyed more broadly. Therefore option 3 is not supported.

The modifications to the proposed extended securitisations regime under the preferred option (option 4), and the reasons for them, are discussed below.

Extension to assets / receivables that are not financial arrangements

The current regime is limited to certain financial arrangements – New Zealand residential mortgages or loans secured by such mortgages.

Submitters noted that it is common for excepted financial arrangements such as trade receivables and operating leases to be securitised, and submitted that the regime should be extended to include the securitisation of such assets.

The intention of this proposed amendment is to extend the current securitisation regime so that New Zealand businesses with large books of trade credits or other receivables can securitise those assets in a tax neutral way. It was always intended that the amended securitisation regime (whether option 2, option 3 or option 4) should apply to a broader class of securitisable assets than those currently covered for financial institutions. These submissions are, therefore, consistent with the proposed amendments.

Extension to all securitisations by financial institutions

The current regime applies only to certain types of securitisations undertaken by financial institutions. Submitters have commented that if the regime is extended to non-financial institutions (who would typically not undertake the types of securitisations that are currently within the scope of the regime), then it should also be extended to other types of securitisations undertaken by financial institutions.

Officials agree with this submission, and consider that financial institutions should be able to use the regime for the same transactions as other corporates, in addition to the residential mortgage-back securities and covered bond programme transactions currently covered.

Amended consolidation requirement

The current rules require that the securitised assets are treated as held by the Originator in its consolidated financial statements under IFRS. Submitters have observed that this requirement is suitable for residential mortgage-backed securities and covered bond programmes, but might be too restrictive for other securitisations.

Submitters have commented that it is often the case in corporate securitisations that the securitised assets are de-recognised by the Originator but are recognised in the consolidated financial statements of another group company. It has been submitted that the consolidation requirement should be amended to accommodate such situations, and that if the group entity that recognises the securitised assets in its consolidated financial statements is separate from the Originator, the transfer of the receivables by the Originator should also be disregarded.

One submitter suggested that it should be sufficient for the consolidation requirement if the SPV[1] is included in the IFRS consolidated accounts of the Originator, or a group that includes the Originator, the Originator's parent company, or the beneficiary of the SPV.

Officials agree with the submitters who suggested that the consolidation requirement could be amended so that it is sufficient if the securitised assets are recognised in the consolidated financial statements of the Originator or another group company. This would mean the benefits of the regime can apply more broadly. In addition, officials consider that such an amended consolidation requirement would be sufficient to ensure that the provisions do not apply where there is a true sale to a third party.

Officials do not think it would be appropriate for it to be sufficient that the SPV or the securitised assets are included in the consolidated financial statements of the beneficiary of the SPV, if the beneficiary is not in the same group. It is considered that this could open up the possibility of the

[1] As opposed to the securitised assets.

provisions being used in a situation where there is in fact a true sale of the assets to a third party.

Requirement of recourse to the Originator

One of the proposed options, raised as a possibility as part of consultation, was for the extension of sections HR 9 to HR 10, with the additional requirement of the lenders (the investors in the SPV) having recourse to the Originator. This was suggested as a way of ensuring that the provisions could not be used to avoid tax on what is in substance a true sale of financial assets to a third party.

Submitters commented that the additional requirement of recourse to the Originator would be inconsistent with the commercial objective of ensuring that the SPV is bankruptcy remote from the Originator. Submitters commented that this would undermine the benefits of a securitisation, and from a practical point of view the Originator would not want to guarantee the SPV's obligations, and would just borrow itself if it were necessary for the investors to have recourse to the Originator.

Officials agree. However, as noted in section 4, officials consider that the risk that the regime could be used to avoid tax on what is in substance a true sale of the assets to a third party could be appropriately mitigated by the requirement that the receivables held by the SPV be treated as held by the Originator or another group company in its consolidated accounts under IFRS. As such, it is not considered necessary to include an additional requirement of recourse to the Originator.

Elective regime / application only to future securitisations

Submitters suggested that the proposed extended regime should be elective, or otherwise apply only to future securitisations, to ensure that existing arrangements are not adversely impacted if they have been structured to achieve a different result than that arising under the extended regime.

Officials agree with this submission. The regime is less burdensome than the current rules – ensuring tax neutrality for securitisations, so there is no issue with the regime being applied electively.

The current regime is not framed as being elective. However, there is no particular policy reason why it should not be, given that it removes a tax barrier. Officials therefore recommend that the regime be explicitly elective for financial institutions and other corporates alike.

Explicit tax neutrality

One submitter commented that the legislation, or associated commentary, should make it clear that transactions within the scope of the extended regime do not give rise to tax consequences (such as a disposal for tax purposes).

There was concern that the recent debt remission reforms indicate that loans made by the sole shareholder of a look-through company (LTC) to the LTC are not disregarded and that the shareholder would be required to account for the tax consequences of the loan essentially as both a deemed lender and borrower. It was suggested that this might indicate that the Originator in a securitisation would be treated as both disposing of and acquiring the securitised assets, given that section HR 9 shares similar statutory language to the transparency provisions in the LTC rules. It was also noted that there is uncertainty around the tax effects of a contribution of property to an LTC or partnership by a shareholder/partner. The submitter commented that general transparency principles would suggest that no disposal occurs, however alternative views had been put forward, and it was noted that this issue would be of particular importance in terms of the proposed expanded securitisation regime.

Officials will ensure that the legislation and associated commentary make it clear that the intention is for there to be no tax consequences for transactions within the scope of the regime.

5.2 Summary table of costs and benefits of the preferred approach

Affected parties *(identify)*	**Comment**: *nature of cost or benefit (eg ongoing, one-off), evidence and assumption (eg compliance rates), risks*	**Impact** *$m present value, for monetised impacts; high, medium or low for non-monetised impacts*	**Evidence certainty** *(High, medium or low)*
Additional costs of proposed approach, compared to taking no action			
Inland Revenue	Cost of legislative changes / process changes. This is a one-off cost.	Low	High
Wider government	Cost of legislative changes / process. This is a one-off cost.	Low	High
Total Monetised Cost	No monetised costs identified.		
Non-monetised costs	One-off cost of legislative amendment.	Low	High
Expected benefits of proposed approach, compared to taking no action			
Businesses wishing to undertake securitisations	Removes a tax disincentive to undertaking securitisations as a funding mechanism, so the commercial benefits of securitisations can be enjoyed by broadly. This is an ongoing benefit. Reduces compliance costs. This is an ongoing benefit.	Medium Medium	Medium Medium
Total Monetised Benefit	No monetised benefits identified.		
Non-monetised benefits	Removes tax disincentives and reduces compliance costs.	Medium	Medium

5.3 What other impacts is this approach likely to have?

As noted in Section 1, the extent to which tax is currently paid in respect of securitisation transactions is not known, so the potential revenue cost is not able to be quantified. However, we understand that currently securitisations are typically structured to prevent tax arising where possible, so any revenue cost is expected to be minimal. Further, removing a tax barrier would be expected to result in more businesses being able to enjoy the commercial benefits of securitisations, and the tax neutrality of those transactions would be no different than if the securitisation had not occurred.

In terms of the fiscal impacts of all of the options considered, as noted in Section 3, arguably there is a potential risk that expanding the regime could result in the rules being used to avoid tax on what is in substance a true sale to a third party. Introducing an additional requirement (for non-financial institution securitisations) of recourse to the Originator is one possible way of reducing the risk of the provisions being used to avoid the tax consequences of a true sale to a third party (Option 3). However, it would seem that this risk could be adequately mitigated by the requirement in the current provisions that the receivables held by the SPV are treated as held by the Originator in its consolidated accounts under IFRS (Option 2). Inland Revenue considers that the risk would be similarly mitigated by a requirement that the securitised assets are treated as held by the Originator <u>or another company in the group</u> in its consolidated accounts under IFRS (Option 4).

5.4 Is the preferred option compatible with the Government's 'Expectations for the design of regulatory systems'?

Yes.

Section 6: Implementation and operation

6.1 How will the new arrangements work in practice?
If approved, these proposals, which require legislative change, would be included in the next available taxation bill after the general election and would apply from the 2018/2019 income year. Given that the ability to use the regime for corporate securitisations would be optional, there is no need for any transitional arrangements. Taxpayers could simply file their returns on the basis of their decision to use the regime or not. We do not see any need for an election to use the regime to be specifically brought to Inland Revenue's attention. When introduced to Parliament, commentary would be released explaining the amendments, and further explanation of their effect would be contained in a Tax Information Bulletin, which would be released shortly after the bill receives Royal assent.

6.2 What are the implementation risks?
The proposals would have no system implications for Inland Revenue, and implementation would not incur additional administrative costs. No issues concerning implementation have been raised through consultation.

Section 7: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?
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.

7.2 When and how will the new arrangements be reviewed?
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. Inland Revenue's Policy & Strategy unit monitors the first year of operation of new legislation. If there is a need to make remedial amendments to the new rules these will be prioritised for inclusion on the Tax Policy Work Programme, and the proposal would go through the GTPP.