

## ROLLOVER RELIEF – BRIGHT LINE TEST CHANGE

Recently the government enacted changes in the Taxation (Annual Rates for 2022-23, Platform Economy and Remedial Matters) Act 2023 includes changes to the bright-line test. These changes provide rollover relief for transfers of residential property.

The effect of the relief will be that bright line test will not triggered on the transfer of the residential property and for the bright-line period to commence from the original purchase date.

Some similar changes have also been made to the application of the interest limitation rules, in order to continue to allow interest deductions to be claimed during the phase out of deductions between 1 October 2021 and 31 March 2025.

These changes largely apply with effect from 27 April 2021 (the effective date of the last change in the bright-line test length and the introduction of the interest limitation rules), although some apply from 1 April 2022.

The changes are intended to prevent taxpayers from being subject to the bright-line test and stung with a tax bill for transfers of residential property when there isn't a change in the economic ownership of the residential land. The changes also ensures that interest deductions are not forfeited when a property is transferred in similar circumstances.

When the bright-line test was initially introduced in 2015, rollover relief only applied for relationship property, inherited land and company amalgamations, so it was difficult to change ownership of residential property without the bright-line test applying. It was crucial to get the ownership structure correct before the residential property was acquired.

### ***When Rollover relief will apply***

For transfers of residential land on or after 1 April 2022, the changes extend the coverage of rollover relief for some transfers, provided certain conditions are met and there is no underlying change in economic ownership. Rollover relief is extended to the following structures:

- Family trusts
- Look-through companies
- Partnerships
- Transfers within wholly owned groups of companies
- Settlements under te Tiriti o Waitangi.

Rollover relief from the bright-line test (when applicable) means the original start date for the bright-line test is retained by the recipient of the residential property following the transfer. This is not an exemption to the bright-line test but merely a transfer of the original acquisition date from one entity to another in limited circumstances. If the recipient subsequently disposes of the residential property, the original acquisition date will be used to determine whether the bright-line test applies.



From an interest deductibility perspective, rollover relief ensures certain transfers do not preclude a person from applying the transitional phasing out of interest deductions. This is a reasonable approach, as prior to the rollover relief, a transfer would mean that interest deductions would be fully denied.

The extent of the rollover relief (when applicable) depends on the price paid for the residential property. In the event the bright-line test applies to an eventual sale of residential property, it is important to keep track of the original owner's acquisition cost, and the price paid on transfer (if any).

### ***Family trust transfers***

For transfers from family trusts (including Māori authority trusts) back to the settlor of the trust, rollover relief is generally available if the following conditions are met:

- The land is transferred on or after 1 April 2022;
- The transferee is a settlor of the trust and had originally transferred the land to the trustee or Māori trustee;
- If there is more than one transferee, the transferees acquire proportionally the same amount of land they originally transferred to the trust; and
- At the time the land is transferred from the trust to the transferee(s):
  - All transferees are beneficiaries of the trust;
  - At least one transferee is a principal settlor of the trust; and
  - The trust is a “rollover trust” or “Māori rollover trust”.

The definition of a “rollover trust” requires the following at the time of transfer:

- All principal settlors are beneficiaries of the trust;
- All principal settlors are close family associates; and
- All beneficiaries are close family beneficiaries.

The definition of a “Māori rollover trust” requires the following at the time of transfer:

- All beneficiaries of the trust are either members of the same iwi or hapū, or descendants of the same tīpuna; and
- The land being transferred is subject to Te Ture Whenua Māori Act 1993.

In summary, rollover relief now applies where a settlor or settlors receive land back from a rollover trust or Māori rollover trust if they previously sold the land to the trust or settled the land on the trust. The settlor no longer has to be the original settlor of the trust and can include other settlors, provided the conditions above have been met (see Resettlement of family trusts below).

### ***Principal settlor not original owner of the land***

Rollover relief will also apply when land is transferred to a settlor or group of settlors, provided all settlors receiving the land are “principal settlors” at both the time the land is originally acquired by the



trust and the time the land is transferred back to the settlors. Relief will not apply to transfers to settlors who are not principal settlors either at the time the land was acquired by the trust or the time the land is transferred back to the settlor. This ensures a beneficiary of the trust cannot become a principal settlor immediately before a transfer to them to avoid a bright-line test restart.

Relief in these circumstances will be quite limited and only applies in a situation where the transferee had not originally owned the land but was still a principal settlor of the trust. Unlike other rollover relief amendments which apply retrospectively, this update only applies for transfers on or after 1 April 2023.

### ***Transfers to self in different capacity and transfers involving multiple legal structures***

Rollover relief is generally provided when a person transfers residential land or disallowed residential property (“DRP”, which is property that is subject to the interest limitation rules) to themselves in different capacities. Common examples of these include:

- Transfers to a look-through company of which the person is the sole shareholder;
- Transfers from a rollover trust to a look-through company owned by the principal settlor of the trust; and
- Where the transferee is a settlor of the trust in their personal capacity and subsequent transfer back from the trust to them as a partner in a partnership.

Note the standard family trust transfer conditions (referred to above) must still be met for rollover relief to apply. However, this is a welcomed change as it avoids the need for two transactions to receive rollover relief.

### ***Resettlement of family trusts***

Rollover relief is now provided when residential land or DRP held by a rollover trust or a Māori rollover trust is resettled onto another related rollover trust or Māori rollover trust. Relief will apply if both trusts meet the definition of “rollover trusts” or “Māori rollover trust” and all beneficiaries are the same for each trust, or all natural person beneficiaries are either the same or close family associates of the principal settlor of the trust disposing of the land. Therefore, rollover relief is only available if both trusts meet the usual requirements for rollover relief referred to above.

As noted above, the general theme of rollover relief is that transfers that do not change the economic substance of land ownership will usually maintain the original acquisition date for the purpose of the bright-line test (i.e., rollover relief should apply).

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