

# THE BRIGHT-LINE TEST

New Zealand tax laws mandate that you are to be taxed on any gains that you have made by selling a property if you have the intention to resell the property when purchasing it. The IRD had some difficulty in applying this rule, so introduced the bright-line test, that was meant to draw a 'bright line' to indicate when a person had bought and sold their property with the intention to sell the property. The bright-line test is to work alongside the original test, known as the intention test.

## WHAT IS THE BRIGHT-LINE TEST?

The bright-line test/rule, in brief, is a legal test that determines when someone is to pay tax on their residential property. Basically, the test tries to determine when someone has sold and bought a house with the intention to resell the property.

The bright-line test only applies to residential land, which essentially means land that is not used as business premises or as farmland. The rule says that if you have bought and sold your house in a two-year period, that you are to be taxed on this gain. Of course, there are exceptions to this rule.

You may be asking, what happens if the bright-line test applies to me? If the test applies you will be taxed on the gain via your income tax return for the year, and if you make a loss the loss will be 'ring fenced'. This essentially means that if you are to owe tax on another property sale in the future, you are not liable to pay for the amount you lost in the previous property sale.

## THE BRIGHT LINE CHECK LIST:

- Have you bought your house on or after 1 October 2015?
- Are you selling this property within two years of purchasing it?  
*If 'yes' to both of these things, the bright-line test applies, unless one of the following exceptions apply.*
- Did you Inherit the property?
- Is the property your main house?  
*(This is the house you have the most connection to/ spend at least 50% of your time at).*
- Did you receive the property because it was relationship property and you had a relationship break down?
- Was the property transferred to you under a will?

### Exceptions to the exception:

**Main Home:** The test will still apply if you rent out more than 50% your land, because the main purpose of your land is to rent. This test will also apply if you have more than one main home (you will not be required to pay tax on the house you have the most connection to e.g. social ties).

**Relationship Property:** The test will still apply if you sell the home within two years of its original purchase date.

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## WHEN DOES THE BRIGHT-LINE PERIOD START AND END?

### Starts:

The bright-line period starts when you purchase the property and the land has been officially registered with Land Information New Zealand.

### Ends:

The bright-line period ends when you sign the agreement to sell the property. But it is good to remember that there are different rules in some circumstances, and you should consult your lawyer to make sure that you know when the bright-line period ends in your circumstance.

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## WHAT IF I WAIT TWO YEARS, WILL I STILL HAVE TO PAY TAX ON THE GAIN?

Selling a property after two years means that the bright-line test will not apply to you, but the Intention test may still apply to you. As mentioned previously, the bright-line test was implemented because IRD were having difficulty to prove a persons' intention when they had purchased the house. In the case that IRD can prove that you had an intention to resell when you purchased the house, you will be taxed on that gain.



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