

## **INCOME TAX TREATMENT OF TREATY OF WAITANGI SETTLEMENTS**

### **Introduction**

All legislative references are to the Income Tax Act 1994 unless otherwise stated.

The Crown has entered into settlements of claims in relation to historical breaches of the Treaty of Waitangi (“the Treaty”) with a number of Maori claimant groups and is in the process of negotiating settlements with other claimant groups. Generally the purpose of a Treaty settlement is to provide redress and compensation to Maori claimant groups for wrongs suffered as a result of historical breaches of the Treaty by the Crown.

A Treaty settlement generally includes:

- An agreed statement of the background to the claim, summarising the key facts about the history of the claim, an acknowledgement by the Crown of the wrongs done and an apology by the Crown for past injustices suffered by the claimant group and for breaches of the Treaty.
- Cultural redress which is intended to meet the cultural rather than economic interests of the claimant group. Cultural redress may be made by a variety of means including gifting back sites of special significance to the claimant group, the recognition of the claimants’ mana by changing place names, a Deed of Recognition acknowledging the claimants’ association with a particular area and requiring consultation with the claimant group on specified matters.
- Financial redress which may include cash, the return of land owned by the Crown and the right of first refusal to purchase specific Crown properties within a defined geographical area.

As part of the settlement the Maori claimant group generally agrees to give certain undertakings (for example, to support the passing of the settlement legislation by Parliament) and agrees that the Treaty settlement will be in full and final settlement of the claimant group’s Treaty grievances.

The Crown also provides funding for negotiations to claimant groups through the Office of Treaty Settlements (“the OTS”), which negotiates Treaty settlements on behalf of the Crown, to claimant groups who enter into direct negotiations with the Crown.

The purpose of this Interpretation Statement is to consider:

- Whether financial redress received by Maori claimant groups as compensation for historical breaches of the Treaty in settlement of claims lodged with the Waitangi Tribunal (whether as a result of the Crown’s acceptance of a recommendation of the Waitangi Tribunal or following direct negotiations with the Crown) are income; and
- Whether funding for settlement negotiations provided by the Crown through the OTS is income.

The Interpretation Statement does not address the income tax treatment of amounts subsequently derived from Treaty settlement payments, nor will it address other funding provided to claimant groups (such as funding provided by the Crown Forestry Rental Trust). This Interpretation Statement also does not deal with the question of whether any amount paid in addition to the financial redress agreed between the Crown and the claimants where there is a delay between settlement being reached and the financial redress being paid is income.

## Summary

- Financial redress under a Treaty settlement is not income under section CD 3. Treaty settlement negotiations are not businesses in themselves and, in the event that any claimant groups are carrying on a business, Treaty settlements are not amounts derived from such a business.
- Financial redress under a Treaty settlement is not income under ordinary concepts in terms of section CD 5.
- Under section CB 5(1)(n) compensation paid under the Crown Forestry Assets Act 1989 to the successful claimants (except compensation based on market stumpage) is exempt income under section CB 5(1)(n) to the extent that in the absence of that provision the payments would be income. Compensation under the Crown Forestry Assets Act 1989 paid to the successful claimants on the return of Crown forestry land is not income under sections CD 3, CD 5, CE 1(1)(a) or (e), CE 2 or CJ 1.
- Where the payment of the financial redress agreed under a Treaty settlement is delayed until settlement legislation is enacted, such redress is not gross income under section CE 1(1)(c).
- Claimant funding provided by the Crown through the OTS is not income under ordinary concepts (section CD 5), nor is it an amount derived from a business (section CD 3). Claimant funding is not a payment to which section DC 1 applies as claimant funding is not provided in respect of any business carried on by claimant groups.

## Background

In 1840 the Treaty was signed between the Crown and the Chiefs of the Confederation of United Tribes of New Zealand and a number of independent chiefs of New Zealand. Under the Treaty the Crown guaranteed to Maori “the full exclusive and undisturbed possession of their Lands and Estates Forests Fisheries and other properties which they may collectively or individually possess so long as it is their wish and desire to retain the same in their possession”.

The Crown has accepted that this obligation was breached in some instances and that land was acquired from Maori in ways that breached the principles of the Treaty. A publication by the OTS, *Healing the Past, Building a Future – a Guide to Treaty of Waitangi Claims and Negotiations with the Crown* (“the OTS publication”) says that:

Most historical Treaty claims involve one or more of the following types of land loss and alienation:

- purchases of Maori land by the Crown before 1865 (this includes pre-Treaty purchases later investigated and validated (“Old Land Claims”), Crown purchases and post-Treaty private purchases through the Crown’s waiver of its pre-emptive right),
- confiscation of Maori land by the Crown under the New Zealand Settlements Act 1863, and or
- transactions under the various Native Land Acts after 1865. (p. 41)

A great deal of historical research has been done in respect of the three types of land claim by the Waitangi Tribunal, the Crown Forestry Rental Trust and the Crown, as a result of which the Crown has a good understanding of the types of land-based historical claims in every area of the country and the amount of land that was lost to Maori: see pp. 41-42 OTS publication. The OTS publication says that the Crown expects that for most claims involving large natural groups the research already completed will provide a sufficient basis to begin negotiations. However, extra research may need to be undertaken if the Crown and claimant negotiators need to agree whether particular breaches of the Treaty and its principles occurred (for example, because the claimants want the Crown to apologise for a particular action but the Crown does not initially accept that there has been a breach). Further research may also be needed on specific issues arising from a claim (for example, where more than one group is making claims over the same area or a particular site) (see pp. 42-43). The OTS publication also says:

Because the Crown acknowledges that widespread breaches of the principles of the Treaty have occurred, it is now willing, if claimants wish to negotiate settlements of claims that include purchases before 1865, confiscation, and the operation and impact of the Native land laws after 1865. Claimants who want to negotiate to settle such claims do not need to go through Waitangi Tribunal Hearings or provide detailed research on each and every Crown action that they consider breached the principles of the Treaty. However, they do need to show the link between the Crown’s acts or omissions and the harm to their tupuna (ancestors).

...

Although the impact of land loss on Maori society was often similar regardless of the way land was lost, the culpability (extent to which a party is wrong or to blame) of the Crown does differ from case to case. The Crown believes that the seriousness of each type of breach is different and redress should reflect that, but this is a matter for discussion during negotiations. (p. 42)

The Crown has entered into settlements in respect of historical breaches of the Treaty with a number of Maori claimant groups and is in the process of negotiating other settlements. Historical breaches relate to the Crown’s actions or omissions up to 21 September 1992. The significance of that date is that it is the date on which Cabinet agreed on the general principles for settling Treaty claims.

### ***Settlement process***

The Waitangi Tribunal (“the Tribunal”) was established under the Treaty of Waitangi Act 1975. The purpose of the Treaty of Waitangi Act 1975 (“the TOWA”) is “to provide for the observance, and confirmation of the principles of the Treaty of Waitangi”. The Tribunal has exclusive authority to determine the meaning and effect of the Treaty as embodied in the Maori and English texts and to decide issues raised by differences between them: section 5(2) TOWA. The Tribunal’s main function is to inquire into and make recommendations to the Crown on claims submitted to the Tribunal by Maori: section 5 TOWA.

Any Maori may make a claim to the Tribunal: section 6 TOWA. The Tribunal has jurisdiction to consider the claim if the claim alleges a breach by the Crown of the principles of the Treaty that is alleged to affect the claimant prejudicially, either individually or by affecting a group of Maori of which the claimant is a member: section 6(1) TOWA. If the Tribunal finds that a claim is well-founded, it may recommend to the Crown that action be taken to compensate for or remove the prejudice or prevent other persons from being similarly prejudiced in the future: section 6(3) TOWA. The Tribunal can recommend both monetary compensation and the return of Crown land taken from Maori in breach of the principles of the Treaty and is required to identify the Maori or group of Maori to whom the land is to be returned: section 8(2) TOWA.

Claimant groups may have claims investigated by the Waitangi Tribunal or they may pursue negotiations with the Crown. Claims must be lodged with the Tribunal before the Crown will begin negotiating with a claimant group but once a claim is lodged, the claimants can immediately seek negotiations with the Crown. Alternatively, the claimants may choose to have their claims heard by the Tribunal before entering negotiations: OTS publication p. 38.

Some claimant groups have carried out direct negotiations with the OTS which is responsible for negotiating Treaty settlements on behalf of the Crown. The four steps of a direct negotiations process claim (as set out in the OTS publication) are as follows:

- *Preparing a claim for negotiation*
  - An agreement by the Crown and the claimants to negotiate, which involves the Crown accepting that there is a well-founded grievance and the claimant group satisfying the Crown's preference to negotiate with large natural groups that represent tribal interests (generally an iwi);
  - Conferral of the mandate of claimant group representatives by the claimant group and recognition of the mandate by the Crown;
  - The establishment of processes for consultation by claimant group negotiators with claimant group members on settlement issues and the development of a register of members.
- *Pre-negotiations*
  - The signing of Terms of Negotiation which set out the ground rules for negotiations;
  - Approval by the relevant Ministers of the funding to claimants as a contribution to the cost of negotiations;
  - The claimant group identifying the areas or sites and Crown assets in which they are interested in seeking redress and the types of redress which they consider are appropriate in relation to those sites or areas.
- *Negotiations*
  - The commencement of formal negotiations;

- After sufficient progress in negotiations, the Minister in Charge of Treaty of Waitangi Negotiations may send a letter to the mandated representatives outlining the parameters of the Crown offer and seeking Agreement in Principle from the claimant group to the Crown offer. Alternatively, the Crown and mandated representatives can seek a more formal agreement (a Heads of Agreement ) which outlines the Crown's settlement offer in more detail;
  - If the Agreement in Principle or the Heads of Agreement are signed by the Crown and mandated representatives a formal Deed of Settlement is prepared for initialling by the mandated representatives.
- *Ratification and implementation*
    - Consultation with and ratification by members of the claimant group;
    - Signing the Deed of Settlement;
    - Implementation of the settlement, which normally requires the passing of settlement legislation. The members of a claimant group must agree on a governance entity for holding and managing settlement assets. The Crown cannot transfer settlement assets until the claimant group has a governance entity that has been considered and ratified by members of the group (pp. 71-72 OTS publication).

### *Settlements*

A Treaty settlement generally includes:

- An agreed statement of the background to the claim, summarising the key facts about the history of the claim, an acknowledgement by the Crown of its responsibility for breaches of the Treaty and its principles and recognition of their impact on the claimant group and an apology by the Crown for past injustices suffered by the claimant group and for breaches of the Treaty. The OTS publication says that it is considered that the Crown's apology lays the foundation for settling historical claims of the claimant group and is a significant step towards rebuilding the relationship between the Crown and claimant group (p. 85);
- Cultural redress which is intended to meet the cultural rather than economic interests of the claimant group. The aim of cultural redress is to address historical grievances arising from the loss of ownership or guardianship of sites of spiritual or cultural significance, loss of access to traditional foods or resources and exclusion from decision-making on the environment or resources with cultural significance: see p. 96 OTS publication. Cultural redress may be made by a variety of means including gifting back sites of special significance to the claimant group, the recognition of the traditional place-names and the return of moveable taonga (artefacts). : see pp. 98-99 OTS publication;
- Financial redress which may include cash and the transfer of commercial assets owned by the Crown and the right of first refusal to purchase specific Crown properties within a defined geographical area.

As part of the settlement, claimant groups are required to give certain undertakings (such as an undertaking to support the passing of settlement legislation in Parliament) or agreements (such as agreement that the settlement will be in full and final settlement of the claimant group's Treaty grievance). The Crown's policy is that Treaty settlements are final. The settlement legislation prevents the courts, the Tribunal or any other judicial body or tribunal from re-opening the historical claims. See p. 32 OTS publication

### ***Crown Forestry settlements***

Crown forestry settlements are in a special category because of the settlement in respect of *New Zealand Maori Council v AG* [1989] 2 NZLR 142 (the *Crown Forestry Assets* case). The terms of the settlement were ultimately enacted in the Crown Forestry Assets Act 1989 ("the CFAA"). The case was one of a series of cases taken under section 9 of the State-Owned Enterprises Act 1986 ("the SOE Act"). Section 9 of the SOE Act provided that nothing in that Act shall permit the Crown to act in a manner which is inconsistent with the Treaty. In an earlier case (*NZ Maori Council v AG* [1987] 1 NZLR 641 ("the *Lands* case")) the Court of Appeal had held that the relationship between the Crown and Maori under the Treaty had created responsibilities analogous to a fiduciary relationship and that the Crown had an active duty to act to protect the Maori people in the use of their lands (pp. 663-664); therefore, in terms of section 9 of the SOE Act, the Crown was required to ensure that that Act was administered in a manner which ensured Maori land claims were safeguarded. As a consequence, a system of memorials on land transferred to SOEs had been developed under the Treaty of Waitangi (State Enterprises) Act 1988 (provisions which are now contained in the SOE Act). Land sold with memorials on the titles for the land could be compulsorily re-acquired by the Crown following a decision by the Tribunal: section 27B SOE Act. This system applied to any land transferred by the Crown to Forestcorp Ltd.

However, the Government of the day accepted a recommendation of a Forestry Working Group (established to report to the Ministers of Finance and State-Owned Enterprises as to the appropriate form in which the Crown's forestry assets should be sold) that, instead of transferring land to Forestcorp, Crown forestry land be retained and a right to manage the land and to cut the trees on it for a specified period be sold; it was considered that this procedure would enable the value of Crown forestry assets to be maximised while taking into account the existence of Treaty issues in respect of Crown forestry assets: see summary of facts in the *Crown Forests Assets* case. If this procedure was followed, the memorial system would not have applied to Crown forestry land, as the memorial system applied only when the land was transferred. In the *Crown Forests Assets* case the Maori Council sought leave from the Court of Appeal to take the matter back to court under the leave reserved to do so in the *Lands* case. The Court of Appeal held that the Maori Council's application was within the scope of the leave given and added the following observations (which indicated the court's likely approach in any substantive hearing):

It may be as well to add some observations, in the hope of helping resolution of the problem. In the judgments in 1987 this Court stressed the concept of partnership. We think it right to say that the good faith owed to each other by the parties to the Treaty must extend to consultation on truly major issues. That is really clear beyond argument. It seems that in relation to its new proposal the Government was in effect so advised by the Forestry Working Group in para 25 of their Report, already quoted. As yet the evidence before the Court does not indicate whether or not the Government accepted that recommendation. It is a matter which may be clarified if there has to be a further hearing of the case.

Partnership certainly does not mean that every asset or resource in which Maori have some justifiable claim to share must be divided equally. There may be national assets or resources which, even if Maori have some fair

claim other initiatives have still made the greater contribution. For example – and it is only an example – that might well be true of some pine forests. Moreover, the common interests may point to the sale of forestry rights, or some of them, to the best commercial advantage. But, as the Forestry Working Group recognised, it would be inconsistent with the principles of the Treaty to reach a decision as to whether there should be a general sale without consultation. (p. 152)

Therefore, the court considered that the Crown had an obligation under the Treaty to consult with Maori in relation to the Crown's proposals for the sale of the forests. The court also raised as a possibility that Maori may not have a right under the Treaty to an equal share of exotic forests.

Following the judgment a settlement was negotiated. The settlement agreement was enshrined in the CFAA. In his speech in the debate on the introduction of the Crown Forest Assets Bill (NZPD Vol 499, 1989: 11626) the Minister of State-Owned Enterprises outlined the features of the agreement between Maori and the Crown and what it was intended to achieve as follows:

The agreement acknowledges that the Crown will sell the existing exotic tree crop and forestry-related assets. Purchasers will be granted a right to use the land for a term that is “evergreen” – that is, it is extended automatically by a period of 1 year until notice of termination is given. The “evergreen” term – and the termination period, if triggered – will be of sufficient length to let any tree crop established by the purchaser reach maturity, and be harvested in accordance with accepted forestry practice.

Consideration for the sale will comprise an initial capital payment for the existing tree crop and related assets, and an annual market-based rental for the use of the land, which remains in the ownership of the Crown. Should the Waitangi Tribunal recommend against resumption of the land the Crown's ownership and related rights will be confirmed. **If, however, the Tribunal recommends the return of the land and part or all of the tree crop to Maori ownership, a number of options for compensation from the Crown will be open to Maori.** It is important that the purchaser of the cutting rights and associated assets will in no way be involved in the compensation payment to the successful claimant, nor would the purchaser require compensation from the Crown.

It is an important principle that the contract between the Crown and the purchaser remains unfettered. That principle will be met. In that way, any discount involved in the transaction for the perceived risk of successful land claims will be minimised, if not totally removed. From the time of the sale of the forest until a Waitangi Tribunal recommendation, land rental payments will be put into a fund administered by a trust known as the Rental Trust. Final beneficiaries of the trust will be the successful claimants, or, if the claim should be unsuccessful, the Crown.

...

The State forests were originally intended to be covered by the Treaty of Waitangi (State Enterprises) Act. The fact that they have not been covered by that Act is the result of an unusual set of circumstances resulting from the Government's decision not to transfer the Crown forestry assets to the Forestry Corporation. The Treaty implications of the forests are therefore unique. They are in no way a precedent for any other asset sale. The agreement is better for New Zealand – for the Government, for the taxpayers, for Maori, and for pakeha – than using the Treaty of Waitangi (State Enterprises) Act. It has been estimated that without such an agreement the value of sales of the Crown's forestry assets might have been discounted by as much as 20 percent because of purchasers' concerns about tenure. [emphasis added]

In the second reading debate (NZPD Vol 502, 1989: 12997) the Minister of Forestry said:

I come back to the part of the Bill in which the government has made provision to ensure that Maori interests are fairly dealt with. That provision comes about after agreement with those persons who negotiated on behalf of the Maori people and at the direction of the court. The effect of the provision is this: Crown licences will be tendered and Crown licences will be sold. If the Waitangi Tribunal should find subsequently that the land on which those forests stand ought to be returned to Maori people the Crown undertakes that the land will be transferred to those Maori people.

In the meantime all of the annual rentals will be placed in a rental trust – not touched by the Government – and, in the event that the Waitangi Tribunal finds in favour of the Maori people, the rental trusts and the moneys in them will be transferred to the Maori people. After the finding of the Waitangi Tribunal, all further rents will accrue to the new owners, the Maori people, but the rights of the purchaser of the forests – namely, of that person or company – are protected up to the stage at which their Crown licence ceases.

Under the CFAA (which reflects the terms of the agreement reached between Maori and the Crown), Crown forestry land is to remain in Crown ownership but the Crown may issue forestry licences and “Crown forestry assets” (being forests that comprise principally exotic trees growing or standing on Crown forest land) can be transferred to the holders of such licences: sections 11 and 14 CFAA. Each licence must contain a provision that if the licensed land is required to be returned to Maori, notice terminating the licence will be given at the end of 35 years from the 30 September after the end of the initial term (if notice is given during the initial fixed term) or at the end of 35 years from the 30 September next after the date of notice: section 17(4).

The Crown Forestry Rental Trust was established to hold all rents on forest land until Maori claims to forests had been determined by the Tribunal: section 34 CFAA. Under the terms of the Trust interest on the Trust’s funds was to be applied in assisting Maori claimants in the preparation, presentation and negotiation of their claims: see *Latimer v CIR* (2002) 20 NZTC 17,737.

If a claim is successful and the Tribunal’s recommendation is accepted by the Crown:

- the forestry land will be returned subject to the relevant forestry licence;
- rentals under the licence held by the Crown Forestry Rental Trust and future rental will be paid to the successful claimants; and
- the Crown must pay compensation to the claimants, in accordance with Schedule 1 to the CFAA: section 36 CFAA.

Clause 1 of the First Schedule provides that compensation is to be paid on to Maori to whom ownership of the land is transferred. Under clause 2 the amount of the compensation is to be:

- (a) Five percent of the specified amount calculated in accordance with clause 3 of this Schedule as compensation for the fact that the land is being returned subject to encumbrances; and
- (b) As further compensation, the remaining portion of the specified amount calculated in accordance with clause 3 of this Schedule or such lesser amount as the Tribunal may recommend.

Clause 3 provides that the person to whom compensation is payable (that is, the successful claimants) may nominate any of the following amounts as the “specified amount” referred to in clause 2:

- The market value of the trees that may be harvested under the Crown forestry licence as at the time the recommendation for the return of land to Maori ownership becomes final (clause 3(a)); or
- The market stumpage, determined in accordance with accepted forestry business practice, of wood harvested under the Crown forestry licence on the land to be returned to Maori



ownership from the date that the recommendation of the Tribunal for the return of the land to Maori ownership becomes final under the TOWA (clause 3(b)). “Stumpage” is defined in the New Zealand Institute of Forestry Professional Handbook (May 1999) as follows:

The value of the standing tree. Usually expressed as the value per cubic metre (or tonne) of the logs by quality in the tree. Generally derived from the sale value of the log at a sale point (eg. “at mill”, “at wharf gate” or “on skid”) by deduction of all the costs incurred in getting the tree off the stump to that point of sale.; or

- The net proceeds received by the Crown from the transfer of the Crown forestry assets to which the land to be returned relates, plus a return on those proceeds for the period between transfer and the return of the land to Maori ownership (clause 3(c)). Clause 5 provides that for the purpose of clause 3(c) the return on the proceeds received shall be such amount as is necessary to maintain the real value of those proceeds during either of the following periods:
  - If the claim was filed before the transfer occurred, a period of not more than 4 years from the date of transfer;
  - If the claim was filed after the date of transfer, the period from the date of transfer to the expiration of 4 years after the claim was filed and for any period after the relevant period, an amount equal to the return on one year New Zealand Government stock measured on a rolling annual basis plus an additional margin of 4 percent per annum.

### ***Funding for negotiations***

The Crown, through the OTS, will provide a contribution to the costs of direct negotiations. The amount of the funding depends on the features of the claimant group (how big the claimant group is, how scattered, whether consultation will require hui, tribal structures) and the complexity of the claim. Any claimant funding provided by the OTS is granted for the purposes of negotiations only and not for reimbursing research costs: p. 43 OTS publication.

Funding will not be provided to a claimant group unless the representatives of a claimant group have established that they have a mandate to represent the group but once mandating has been established, the Crown will consider reimbursement for mandating costs already incurred. Payments are then made by instalments of no more than \$50,000 at a time. Each payment will be linked to the progress of negotiations and reaching the most important milestones. The OTS requires that audited accounts be provided to the OTS once the milestones relating to the claimant funding have been achieved. Audited accounts must be provided at least every twelve months regardless of whether the milestones have been achieved. Invoices must be provided for every tranche up to \$50,000 before the tranche may be released.

Claimant funding does not represent an advance in respect of financial redress under a Treaty settlement. The funding provided will be over and above any money or other assets eventually given to the claimant group as redress for its historical Treaty claims. If a claimant group incurs costs over and above the amount of approved funding, in exceptional circumstances, the Crown may consider providing additional funding which is likely to be a payment “on account” of the final settlement. Once settlement has been reached, any approved claimant funding which have not been spent will be paid to the claimant group. Refer p. 56 OTS publication.

## Legislation

### Section CB 5(1)(n) provides:

To the extent that in the absence of this section the following amounts would be gross income, they are exempt income:

...

- (n) Payments made to any person as compensation under the First Schedule (except clause 3(b)) of the Crown Forest Assets Act 1989.

### Section CD 3 provides:

The gross income of any person includes any amount derived from any business.

The definition of “business” in section OB 1 reads as follows:

“Business”

- (a) Includes any profession, trade, manufacture, or undertaking carried on for pecuniary profit:
- (b) Is further defined in Schedule 6A for the purposes of that Schedule:

### Section CD 5 provides:

The gross income of any person includes any amount that is included in gross income under ordinary concepts.

### Section CE 1(1)(a), (c) and (e) provide:

The gross income of any person includes—

- (a) All interest, investment society dividends, and annuities:

Provided that where any securities have been acquired by purchase otherwise during the income year, the Commissioner may, where the Commissioner considers it equitable so to do, apportion between the transferor and the transferee any interest due or accruing due at the date of the transfer and not then paid:

...

- (c) Income derived under the accrual rules:

...

- (e) All rents, fines, premiums, or other revenues (including payment for or in respect of the goodwill of any business, or the benefit of any statutory licence or privilege) derived by the owner of land from any lease, licence, or easement affecting the land, or from the grant of any right of taking the profits of the land.

### Section CE 2 provides:

Subject to sections CJ 1 and FF 7, the gross income of any person includes any amount derived from the use or occupation of any land:

Sections CJ 1(1) and (2) provide:

- (1) The gross income of any person shall include any amount (including an amount deemed to have been realised under section FB 4 or section GD 1 or section GD 2) derived in any income year from—
  - (a) The extraction, removal, or sale or other disposition of any minerals, flax, or timber; or
  - (b) The sale or other disposition of any right to take timber,—  
whether by the owner of the land from or on which the minerals, flax, or timber are obtained or situated or by any other person.
- (2) A sale or disposition of land with standing timber on the land, except to the extent that the timber is—
  - (a) Timber comprised in ornamental or incidental trees; or
  - (b) Subject to a forestry right (as defined in section 2 of the Forestry Rights Registration Act 1983) registered under the Land Transfer Act 1952; or
  - (c) Subject to a profit à prendre granted before 1 January 1984,—  
  
shall be deemed to include a sale or other disposition of timber for the purposes of this section (whether or not the sale or other disposition includes other land or other assets or the land and timber are assets of a business), and in every such case—
    - (d) the part of the consideration attributable to the timber, including the amount determined under section FB 4, GD 1 or GD 2, is to be treated as the consideration paid for the timber; and
- (e) the amount of consideration under paragraph (d) is treated as—
  - (i) gross income of the person selling or otherwise disposing of the land; and
  - (ii) the cost of the timber to the person acquiring the land.

Section DC 1 provides:

- (1) This section shall apply in respect of—
  - (a) Any payment (in this section referred to as a “grant”) made to any taxpayer in any income year by the Development Finance Corporation of New Zealand or the New Zealand Film Commission or by any department or instrument of the Executive Government of New Zealand or any local authority, being a payment in the nature of a subsidy or grant in respect of any business carried on by that taxpayer other than a payment to which section CC 3 or section DL 3 (except section DL 3(6)), applies:
  - (b) Any expenditure in respect of which a grant is made.
- (2) Where, and to the extent that, in any income year, a grant is made to any taxpayer in respect of expenditure incurred by the taxpayer (not being expenditure of any of the kinds referred to in subsection (3)) that is allowed as a deduction under this Act, the amount of the deduction otherwise allowed, in respect of that expenditure shall be reduced by the amount of that grant, and the amount of that grant shall be deemed not to be gross income of that taxpayer.
- (3) Where, and to the extent that, a grant is made to any taxpayer in respect of expenditure incurred by that taxpayer in the acquisition, construction, installation, or extension of any asset (being an asset in respect of which a deduction for depreciation is allowed under this Act), the amount of that expenditure shall, for the purposes of determining the amount of any deduction allowed in respect of the depreciation of that asset, be deemed to be reduced by the amount of that grant, and the amount of that grant shall be deemed not to be gross income of the taxpayer.
- (4) Subject to section DC 3, this section shall not apply to the amount of any payment in the nature of an advance or loan.

- (5) For the purpose of giving effect to this section, the Commissioner may at any time amend any assessment, notwithstanding the time bar.

Section EB 1(1) provides:

- (1) For the purposes of this Act an amount shall be deemed to have been derived by a person although it has not been actually paid to or received by the person, or already become due or receivable, but has been credited in account, or reinvested, or accumulated, or capitalised, or carried to any reserve, sinking, or insurance fund, or otherwise dealt with in the person's interest or on the person's behalf.

Section EH 21(1) provides:

The accrual rules apply to a person who is a party to a financial arrangement and who is a New Zealand resident.

“Financial arrangement” is defined in section EH 22(1) as follows:

- (1) A financial arrangement is
- (a) a debt or debt instrument, including a debt that arises by law;
  - (b) an arrangement (that may include a debt or debt instrument or an excepted financial arrangement) under which a person receives money in consideration for a person providing money to any person
    - (i) at a future time, or
    - (ii) when an event occurs in the future or does not occur (whether or not the event occurs because notice is or is not given).

*Relevant provisions of the Crown Forests Assets Act 1989 (“the CFAA”) are set out below*

Section 11 of the CFAA provides:

- (1) The responsible Ministers may, on behalf of the Crown, transfer Crown forestry assets to any person for such consideration, and on such terms and conditions, as the responsible Ministers may agree with that person.
- (2) Crown forestry assets that are described in paragraph (a) of the definition of that term in section 2 of this Act may only be transferred to a person to whom it is proposed to grant a Crown forestry licence in respect of the land on which those assets are situated.
- (3) Nothing in subsection (2) of this section prevents the transfer of any Crown forestry assets referred to in that subsection in compliance with—
- (a) The terms of any contract that existed immediately before the commencement of this Act; or
  - (b) The terms of any contract that the responsible Ministers consider appropriate to enter into in accordance with current accepted business practice; ...

Section 13 of the CFAA provides:

Notwithstanding any Act or rule of law, Crown forestry assets growing or standing on, or fixed to, or under or over, any land may be transferred under section 11 of this Act, notwithstanding that neither the land nor any interest in the land is being transferred. For the purposes of that transfer, the assets and the land shall be regarded as separate assets each capable of separate ownership.

Section 17 of the CFAA provides:

- (1) For the purposes of this section termination period means the period of 35 years at the end of which a Crown forestry licence terminates in relation to the licensed land or any part of it.
- (2) Subject to this section, every Crown forestry licence that relates to Crown forest land that is situated in a district specified in the Schedule 3 to this Act, or on which a forest specified in that Schedule is located, shall comprise, as an initial fixed term, the term set out opposite that district or forest, as the case may be, in that Schedule, and shall then run from year to year by way of automatic extension.
- (3) Subject to this section, every other Crown forestry licence shall run from year to year by way of automatic extension.
- (4) Every Crown forestry licence shall provide that if a recommendation is made under section 8HB(1)(a) of the Treaty of Waitangi Act 1975 that becomes a final recommendation under that Act for the return of the licensed land, or any part of it, to Maori—
  - (a) The responsible Ministers shall give notice to the licensee that the recommendation has become a final recommendation:
  - (b) Notice shall be given to the licensee terminating the licence, or terminating the licence in so far as it relates to part of the licensed land, as the case may be,—
    - (i) If the notice is given during the initial fixed term, at the expiration of a period of 35 years commencing on the 30th day of September next after the end of that term; or
    - (ii) If the notice is given after the initial fixed term, or if the licence does not comprise an initial fixed term, at the expiration of a period of 35 years commencing on the 30th day of September next after the date on which the notice is given:
  - (c) In relation to the licensed land, or that part of it to which a notice of termination applies, as the case may be,—
    - (i) During the termination period the rights of the licensee under the licence in respect of that land shall be restricted to protecting, managing, harvesting, and processing the tree crops standing on that land at the commencement of that period; and
    - (ii) The licensee shall exercise those rights in accordance with accepted forestry business practice; and
    - (iii) The licensee shall, during the termination period, from time to time in accordance with the licence, give notice to the licensor of those parts of that land, including buildings and other fixed structures, roads, tracks, and access ways, that are no longer required by the licensee for exercising the licensee's rights under the licence during that period; and
    - (iv) The licensor shall take possession of any land referred to in subparagraph (iii) of this paragraph notified as being no longer required, and the licence shall cease to apply to that land except for provisions that relate to the rights and obligations of the parties during the balance of the termination period.
- (5) Every Crown forestry licence shall provide that if a recommendation is made under section 8HB(1)(b) or section 8HB(1)(c) or section 8HE of the Treaty of Waitangi Act 1975 that the licensed land, or part of it, not be liable to be returned to Maori ownership,—
  - (a) The licence shall, as regards the licensed land or any part of it to which the recommendation relates, be deemed to have been granted for an initial fixed term of 35 years whether or not the licence comprised an initial fixed term in accordance with subsection (2) of this section and whether or not the licence has been in force for the whole or part of that term:

- (b) Notice may be given to the licensee terminating the licence—
  - (i) If the notice is given during the initial fixed term, at the expiration of a period of 35 years commencing on the 30th day of September next after the end of that term; or
  - (ii) If the notice is given after the expiration of the initial fixed term, at the expiration of a period of 35 years commencing on the 30th day of September next after the date on which the notice is given:
- (c) Subject to the terms and conditions of the licence and to any enactment or rule of law, the licensee shall have the right, while the licence remains in force, to use the licensed land for any purpose whether or not it relates to the harvesting, planting, management or processing of trees on the licensed land.

Section 36 of the CFAA provides:

- (1) Where any interim recommendation of the Waitangi Tribunal under the Treaty of Waitangi Act 1975 becomes a final recommendation under that Act and is a recommendation for the return to Maori ownership of any licensed land, the Crown shall—
  - (a) Return the land to Maori ownership in accordance with the recommendation subject to the relevant Crown forestry licence; and
  - (b) Pay compensation in accordance with the Schedule 1 to this Act.
- (2) Except as otherwise provided in this Act or any relevant Crown forestry licence, the return of any land to Maori ownership shall not affect any Crown forestry licence or the rights of the licensee or any other person under the licence.
- (3) Any money required to be paid as compensation pursuant to this section may be paid without further appropriation than this section.

Schedule 1 of the CFAA reads as follows:

- 1. Compensation payable under section 36 of this Act shall be payable to the Maori to whom ownership of the land concerned is transferred.
- 2. That compensation shall comprise—
  - (a) Five percent of the specified amount calculated in accordance with clause 3 of this Schedule as compensation for the fact that the land is being returned subject to encumbrances; and
  - (b) As further compensation, the remaining portion of the specified amount calculated in accordance with clause 3 of this Schedule or such lesser amount as the Tribunal may recommend.
- 3. For the purposes of clause 2 of this Schedule, the specified amount shall be whichever of the following is nominated by the person to whom the compensation is payable—
  - (a) The market value of the trees, being trees which the licensee is entitled to harvest under the Crown forestry licence, on the land to be returned assessed as at the time that the recommendation made by the Tribunal for the return of the land to Maori ownership becomes final under the Treaty of Waitangi Act 1975. The value is to be determined on the basis of a willing buyer and willing seller and on the projected harvesting pattern that a prudent forest owner would be expected to follow; or
  - (b) The market stumpage, determined in accordance with accepted forestry business practice, of wood harvested under the Crown forestry licence on the land to be returned to Maori ownership from the date that the recommendation of the Tribunal for the return of the land to Maori ownership becomes final under the Treaty of Waitangi Act 1975. If notice of

termination of the Crown forestry licence as provided for under section 17(4) of this Act is not given at, or prior to, the date that the recommendation becomes final, the specified amount shall be limited to the value of wood harvested as if notice of termination had been given on that date; or

- (c) The net proceeds received by the Crown from the transfer of the Crown forestry assets to which the land to be returned relates, plus a return on those proceeds for the period between transfer and the return of the land to Maori ownership.
4. For the purposes of clause 3(c) of this Schedule, if the land to be returned is included within an area that was offered for sale as a single lot, the transfer proceeds in relation to each hectare of land returned to Maori ownership shall be not less than an amount equal to the average price per hectare of the forest lot specified in the selling process; except that—
- (a) Where a bid is accepted for a number of lots as one parcel, the average price shall be based on the price for the total parcel; and
  - (b) Where the lot concerned had an average age of less than 5 years, the average price applied shall be the average price of all lots transferred within the same Crown Forestry Management Limited administrative district existing at the time of transfer.
5. For the purposes of clause 3(c) of this Schedule, the return on the proceeds received by the Crown shall be—
- (a) Such amount as is necessary to maintain the real value of those proceeds during either—
    - (i) In the case where the claim was filed before the transfer occurred, a period of not more than 4 years from the date of transfer of the Crown forestry assets; or
    - (ii) In the case where the claim was filed after the date of transfer of the Crown forestry assets, the period from the date of transfer of the Crown forestry assets to the date of expiration of 4 years after the claim was filed; and
  - (b) In respect of any period after the period described in subparagraph (i) or subparagraph (ii) of paragraph (a) of this clause (as extended under clause 6 of this Schedule), equivalent to the return on one year New Zealand Government stock measured on a rolling annual basis, plus an additional margin of 4 percent per annum.
- For the purposes of this clause, a claim shall be deemed to be filed on such date as is certified by the Registrar of the Tribunal.
6. The period of 4 years referred to in clause 5 of this Schedule may be extended by the Tribunal where the Tribunal is satisfied—
- (a) That a claimant with adequate resources has wilfully delayed proceedings in respect of a claim; or
  - (b) The Crown is prevented, by reasons beyond its control, from carrying out any relevant obligation under the agreement made on the 20th day of July 1989 between the Crown, the New Zealand Maori Council, and the Federation of Maori Authorities Incorporated.
7. All payments under this Schedule, other than payments for the purposes of clause 3(b) of this Schedule, shall be made within 2 months after the date of the Tribunal's recommendation, or such later date as the Tribunal may direct, or the parties may agree.
8. All payments for the purposes of clause 3(b) of this Schedule shall be calculated at 3 monthly intervals and shall be paid within one month of the relevant 3 monthly period.

9. Payments under this Schedule, other than payments made for the purposes of clause 3(c) of this Schedule on which interest is payable in accordance with clause 5(b) of this Schedule, shall not bear interest.

“Crown forestry assets” is defined in the CFAA as follows:

Crown forestry assets means—

- (a) Every forest that comprises principally exotic trees growing or standing on Crown forest land; and
- (b) All improvements on, or associated with, Crown forest land and, without limiting the generality of the foregoing, includes:
  - (i) All buildings and other structures affixed to that land; and
  - (ii) All roads, tracks, accessways, firebreaks, bridges, culverts, irrigation works, erosion works, water-races, drainage works, water storage, and all works and services related to the prevention, detection, or fighting of fire; and
- (c) All plant, equipment, vehicles, tools, logs, consumable supplies, raw materials, forest produce and stores used or associated with the management of other Crown forestry assets; and
- (d) The forest stand records of the Crown; and
- (e) All rights (whether vested or contingent) under leases, licences, agreements for sale and purchase, profits à prendre, easements (including easements in gross), rights to take standing timber and growing crops, and any other form of right to occupy or use land other than Crown forest land; and
- (f) All patents, trademarks, copyright, and other intellectual property rights (whether protected by registration or other formal process, or not) and all planning and other statutory consents used in connection with the management of Crown forestry assets or Crown forest land; and
- (g) Shares or other securities in companies holding Crown forestry assets and shares or other securities held by the Crown for forestry purposes; and
- (h) All contracts entered into by the Crown in respect of Crown forestry assets referred to in the preceding paragraphs of this definition or the use of Crown forest land—

but does not include contracts that are not capable of assignment by the Crown and the leases or licences specified in the Schedule 2 to this Act:

## **Analysis**

### ***Whether amount derived from any business – section CD 3***

A business “includes “any profession, trade, manufacture, or undertaking carried on for pecuniary profit”. For there to be a business there must be a genuine intention to make a profit. In order to determine whether the activity is carried on with the intention of making a profit, the taxpayer’s subjective evidence of intention is relevant but must be tested against objective evidence. It is, therefore, necessary to consider both the nature of the taxpayer’s activities and the intention of the taxpayer in engaging in those activities. Factors that may be relevant in considering whether a taxpayer is carrying on a business include: the nature of the activity, the period during which the activity is engaged in, the scale of operations and the volume of transactions, the commitment of time, money and effort, the pattern of activity and the financial results. The fundamental concept of a business is that it is an activity that is



carried on in an organised, systematic and coherent manner that is directed at the end result of obtaining a profit. See *Grieve v CIR* (1984) 6 NZTC 61,682.

Not every receipt by a taxpayer who carries on a business is income under section CD 3. Section CD 3 applies to amounts derived “from any business”. The amount in question must be income and it will be income if it is derived from the current operations of the business, ie, it is “an ordinary incident of the business” or derived “in the ordinary course of the business”. In *CIR v City Motor Service Ltd* [1969] NZLR 1010 Turner J said:

... in my opinion in the words “from the business” of the company something more is meant than merely “as a result of the fact that the company was carrying on this business”. I think that *from the business* must mean *from the current operations of the business.*”

...remembering that Income Tax is always a tax on Income I conclude without difficulty that the words “from any business” in an Income Tax Act must mean “from the current operations of any business” and no more. They are not, in my opinion, apt to include accretions to the capital assets of the taxpayer which although they may result from the fact of his carrying on business, yet do not arise from the actual operations of that business. (p. 1017)

...

But income tax being “always a tax on income”, the crucial question in New Zealand must therefore in result be the same as that in Australia. Is the receipt income or capital? If it is gains or profits from a business, then the question reduces itself to whether these were derived from the *current* operations of the business, and therefore income, or whether no more than can be contended, as regard their connection with the business, than that without the existence of the business they would not have accrued. If no more than this last can be proved, the gains cannot be assessable income, and simply because they are not derived from the current operations of the business. (pp. 1017-1019)

In order to determine whether amounts are income from a business it is necessary to consider the nature of the business and the relationship of the transactions under which the amounts are received to the business. In *AA Finance Ltd v CIR* (1994) 16 NZTC 11,383 Richardson J said:

Whether gains produced in a business are revenue or capital depends on the nature of the business and the relationship of the transactions producing the gain to the conduct of the business. The classic statement in that regard is that of the Lord Justice Clerk in *California Copper Syndicate Ltd (Limited and Reduced) v Harris (Surveyor of Taxes)* (1904 5 TC 159 at p 166 that:

“... enhanced values obtained from realisation or conversion of securities may be so assessable, where what is done is not merely a realisation or conversion of investment, but an act done in what is truly the carrying on, or carrying out, of a business.”

Liability to tax does not depend on showing that the taxpayer is carrying on a separate business of dealing in investments. A transaction may be part of the ordinary business of the taxpayer or, short of that, an ordinary incident of the business activity of the taxpayer although not its main activity. A gain made in the ordinary course of carrying on the business is thus stamped with an income character. (p. 11,391)

*Whether the pursuit of a Treaty settlement is a business in itself*

A claimant group is normally a tribal-based group. A Treaty settlement is negotiated and entered into by representatives of that group on behalf of the members of the group and must be ratified by the members before it is binding on the claimant group. Financial redress negotiated under a Treaty settlement is transferred to and managed by the claimant group’s

governance entity. Before the Crown transfers financial redress, the Crown must be satisfied that the claimant group's governance entity is fully accountable to the members.

Under the Treaty the Crown guaranteed to Maori property rights existing as at the date of the Treaty. The breach of that obligation forms the basis for Treaty claims for financial redress. The purpose of the financial redress is to compensate the claimants for the economic losses resulting from the Crown's breaches of the Treaty. The OTS publication says:

Financial and commercial redress also recognise that where claims for the loss of land and/or resources are established, the Crown's breaches of the principles of the Treaty will usually have held back the full economic development of the claimant group concerned. The Crown does not provide full compensation based on a calculation of total losses to the claimant group... but it does contribute to re-establishing an economic base as a platform for future development. (p. 87)

In determining the quantum of redress that is offered, the Crown takes into account the amount of land lost to the claimant group through the Crown's Treaty breaches, the relative seriousness of the breaches involved, the benchmarks set by existing settlements for similar grievances. Secondary factors are the size of the claimant group today, whether there are any overlapping claims and any other special factors: refer OTS publication p. 89.

A purpose of a Treaty claim is to obtain compensation for economic losses resulting from the Crown's breaches of its obligations under the Treaty. Those obligations include a guarantee of property rights held by Maori as at the date of the Treaty: see *NZ Maori Council v AG* [1989] 2 NZLR 142; *NZ Maori Council v AG* [1994] 1 NZLR 513. Essentially the loss for which compensation is received is a loss of a capital nature.

A Treaty settlement also generally has a dimension beyond the compensation for economic losses. The other elements of a settlement are the Crown's apology and acknowledgement, and cultural redress. The Crown's acknowledgement and apology and cultural redress (which normally form part of the settlement reached) are intended to recognise non-economic losses of the claimant group.

Normally Treaty settlement deeds include a statement setting out the historical events giving rise to grievances, an acknowledgement by the Crown of acceptance of responsibility for the breaches and an apology by the Crown for its acts or omissions. The Crown's apology and acknowledgement are considered to be an important contribution to the settlement of Treaty grievances. The OTS publication states that it is recognised that excessive land loss had a harmful effect on Maori social development and has been accompanied by the loss of access to forests, waterways, food resources and places of spiritual and cultural value: p. 18.

"Cultural redress" is intended to address concerns raised by claimant groups in negotiations regarding issues of cultural, rather than economic, significance to the claimant groups. Cultural redress includes provision for consultation on the management, control or ownership of sites, areas or customary resources on Crown-owned land with which the claimant group has traditional and cultural associations and recognition of traditional place names. The OTS publication says that issues of cultural significance have often been raised by claimant groups in negotiations with the Crown.

Under the test in *Grieve* both the taxpayer's intention, and the nature and scale of the activity carried on by the taxpayer, are relevant in determining whether the taxpayer is carrying on a business. A Treaty settlement is a one-off event as the Crown seeks a comprehensive

settlement of all claims of a claimant group and the Crown's policy is that all settlements are to be final. A Treaty claim does not involve regular and recurrent transactions by claimant groups but the pursuit of a Treaty claim is carried on in an organised, systematic and coherent manner, generally over a period of years, with a view to obtaining a significant amount under a Treaty settlement. However, the Commissioner considers that the making of a Treaty claim is not for that reason a business. A Treaty claim is carried on with the intention of recovering compensation for past wrongs, in the form of economic redress, cultural redress and also an acknowledgement and apology from the Crown for its breaches of the Treaty, rather than with the intention of profit. A Treaty claim is not a purely commercial activity. The acknowledgement and apology and the cultural redress are regarded as important aspects of settlements. A Treaty claim is undertaken in order to recover compensation for a past loss rather than to make a profit.

*Whether financial redress under a Treaty settlement is an amount derived from another business*

The governance entities which receive Treaty settlement assets on behalf of claimant groups may either be existing entities or entities established for the purpose of receiving Treaty settlements. Some governance entities may carry on activities outside the Treaty claim and such activities may be businesses.

It is also possible that individual members of the claimant group, on whose behalf the settlement assets are received, may be carrying on a business and the individual members of a claimant group may be deemed by section EB 1 to have derived the settlement payment, on the basis that settlement payments have been dealt with in their interest or on their behalf by the entity which has received the settlement. (However, in some cases the settlement legislation has expressly provided that the settlement is for the benefit of the claimant group and not for the benefit of any individual, particular marae or particular hapu, except to the extent determined otherwise after the settlement by the governance entity: see section 467 Ngai Tahu Claims Settlement Act 1998; section 17 Pouakani Claims Settlement Act 2000.)

The Commissioner considers that even if the claimant group or individual members of the group were carrying on a business, a Treaty settlement is not an amount derived from any business carried on by such persons. A Treaty claim does not involve regular or recurrent transactions. The Crown's policy is that settlements are to be final settlement of all historical claims of the claimant group. A Treaty settlement is not a transaction that is entered into as part of the ordinary operations of any business carried on by a claimant group. The Treaty itself is not an ordinary commercial contract and is regarded as having constitutional significance: see *NZ Maori Council v AG* [1994] 1 NZLR 513.

The majority of claims involve land claims. The basis for financial redress under a Treaty settlement is that land or other resources have been lost to the claimant groups as a result of the Crown's Treaty breaches. The OTS publication indicates that financial redress under Treaty settlements recognises that Treaty breaches resulting in loss of land or other resources have had a detrimental effect on the overall economic position of claimant groups. The OTS publication says that:

Commercial and financial redress recognises that where claims for the loss of land and/or resources are established, the Crown's breaches of the principles of the Treaty will usually have held back the full economic development of the claimant group concerned. ...

It is impossible to put a precise value on the economic losses resulting from most Treaty breaches. This is because so much time has passed, and because the effects of various causes on the economic status of the claimant group today is such a complex matter. European settlement has also brought benefits to Maori that cannot be easily expressed in money terms. However, many commentators estimate that the losses to Maori amount to tens of billions of dollars. (p.87-89)

Financial redress under a Treaty settlement is paid to compensate for the loss of land or other resources held at the time that the Treaty was signed. Evidence was given by the Maori applicants in “the Lands case” and accepted by the court that land has a special significance in Maori culture. Richardson J commented:

The uncontested evidence in this case... amply justifies and supports conclusions of historians as to the crucial importance of land in Maori culture. The New Zealand Maori Council in its paper *Kaupapa – Te Wahanga Tuatahi* expresses it in this way:

“It [Maori land] provides us with a sense of identity, belonging and continuity. It is proof of our continued existence not only as a people, but as the tangatawhenua of this country. It is proof of our tribal and kin group ties. Maori land represents turangawaewae.

It is proof of our link with ancestors of our past, and with the generations yet to come. It is an assurance that we shall forever exist as a people, for as long as the land shall last.” (p. 674)

Given that evidence, the Commissioner considers that it is unlikely that land in respect of which compensation is paid under Treaty settlements would be treated as an asset of a revenue nature.

Compensation payments take the character of that which they replaced: *London and Thames Haven Oil Wharves Ltd v Attwooll* [1967] 2 All ER 124 and *Burmah Steamship Co Ltd v CIR* (1930) 16 TC 67. In *Burmah Steamship*, where a ship owner had received damages for breach of contract by a late delivery of a ship (which was, therefore, unavailable for trading operations), the damages were held to be business income as the damages were compensation for loss of trading receipts. Lord Clyde said:

In the present case there can be no doubt that, when the Appellant entered into the contract with the repairers, the consequences of a failure by the latter to deliver punctually, which were in the contemplation of both parties at the time, were that the Appellant would be deprived of the opportunity of putting the vessel to immediate profitable use in his business. It was in respect of this deprivation that the damages were recovered. The contemplated “hole” in the Appellant's profits was unfortunately made, and in my opinion the damages recovered must go, as a matter of sound commercial accounting, to fill that “hole”, and therefore constitute a proper item of profit in the Appellant's profit and loss account. (p. 136)

The *London & Thames Haven Oil Wharves Ltd* case concerned an insurance payment made to the owner of a wharf damaged by one of its shipping company clients. Part of the insurance payments related to consequential damage for loss of the use of the wharf (that is, the loss of profits from destruction of trading stock). Diplock LJ held that that part of the insurance payment was income from the taxpayer's business. He said:

Where, pursuant to a legal right, a trader receives from another person compensation for the trader's failure to receive a sum of money which, if it had been received, would have been credited to the amount of profits (if any) arising in any year from the trade carried on by him at the time when the compensation is so received, the compensation is to be treated for income tax purposes in the same way as that sum of money would have been treated if it had been received instead of the compensation. The rule is applicable whatever the source of the legal right of the trade to recover the compensation. It may arise from a primary obligation under a contract, such as a contract of insurance; from a secondary obligation arising out of non-performance of a contract, such as a right to damages, either liquidated, as under the demurrage clause in a charterparty, or unliquidated; from an

obligation to pay damages for tort, as in the present case; from a statutory obligation; or in any other way in which legal obligations arise. (p. 134)

The principle set out in those cases was applied in *Case S104* (1996) 17 NZTC 7,662 and in *Case T47* (1998) 18 NZTC 8,319. In those cases taxpayers who had been prevented from logging a native forest by a Government regulation had received a settlement payment from the Government. In both cases the TRA considered that the payment was income from the partnership's business, being compensation for loss of the profit that they would have derived from logging the forest.

However, in *The Glenboig Union Fireclay Co Ltd v IR Commissioners* (1922) 12 TC 427, where a taxpayer in the business of manufacturing fire clay goods and selling raw clay had received a payment for ceasing to work fire clay fields over which it had mining rights, it was held that the compensation payment was a receipt of a capital nature being an amount received for sterilisation of a capital asset. The fact that the amount of the compensation was determined having regard to profits that would have been earned from the fire clay left unworked was not relevant. The issue was whether the compensation was paid to compensate for a loss of a revenue or of a capital nature. Lord Clyde said:

In truth the sum of money is the sum paid to prevent the [taxpayer] obtaining the full benefit of the capital value of that part of the mines which they are prevented from working by the Railway Company. It appears to me to make no difference whether it be regarded as a sale of the asset out and out, or whether it be treated merely as a means of preventing the acquisition of profit that would otherwise be gained. In either case the capital asset of the Company to that extent has been sterilised and destroyed, and it is in respect of that action that the sum of £15,316 was paid. It is unsound to consider the fact that the measure, adopted for the purpose of seeing what the total amount should be, was based on considering what are the profits that would have been earned. That, no doubt, is a perfectly exact and accurate way of determining the compensation ... But there is no relation between the measure that is used for the purpose of calculating a particular result and the quality of the figure that is arrived at by means of the application of that test. I am unable to regard this sum of money as anything but capital money ... (pp. 463-464)

Compensation paid to replace amounts that would have been receipts of a revenue nature from a business carried on by a claimant group would prima facie be income. The Commissioner considers that financial redress under Treaty settlements is paid to compensate for a loss of a capital nature, being assets held by Maori at the time the Treaty was signed. Therefore, financial redress under Treaty settlements is not income on that basis..

### *Conclusion*

The Commissioner considers that the pursuit of a Treaty settlement in respect of historical breaches of the Treaty is not a business in itself and that even if a claimant group carries on another activity which constitutes a business, financial redress under Treaty settlements is not an amount derived from a business carried on by the claimant group or by members of the claimant group.

### ***Whether financial redress under Treaty settlements is income under ordinary concepts – section CD 5***

Amounts which are income under ordinary concepts are gross income: section CD 5.

Whether or not a particular payment is income under ordinary concepts depends upon its quality in the hands of the recipient. There is no necessary connection between the character

of a payment in relation to the payer and its character as a receipt by the payee: *Scott v C of T* (1966) 117 CLR 514; *The Federal Coke Company Ltd v FCT* 77 ATC 4255; *Reid v CIR* (1985) 7 NZTC 5,176.

Periodicity, regularity or recurrence of payments may indicate that the payments are income, but this factor is not conclusive. It is necessary to consider the relationship between the payer and payee and the purpose for which the payment is made. In *Reid v CIR* (1985) 7 NZTC 5,176 Richardson J commented as follows:

There may be difficulty in marginal cases in determining what are the ordinary concepts and usages of mankind in this regard and to assist in that determination there has been much discussion in the cases of criteria which bear on the characterisation of receipts as income in particular classes of case. The major determinant in many cases is the periodic nature of a payment (*FC of T v Dixon* (1952) 86 CLR 540; and *Asher v London Film Productions* [1944] 1 All ER 77). If it has that quality of regularity or recurrence then the payments become part of the receipts upon which the recipient may depend for his living expenses, just as in the case of a salary or wage earner, annuitant or welfare beneficiary. But that in itself is not enough and consideration must be given to the relationship between payer and payee and to the purpose of the payment, in order to determine the quality of the payment in the hands of the payee. (p. 5,183)

The approach in *Hallstroms Pty Ltd v FCT* (1946) 72 CLR 634 was described by Richardson J as exemplifying the governing approach in New Zealand for determining whether a receipt of an expense is of a capital or revenue nature: see *CIR v Thomas Borthwick & Sons (Australasia) Ltd* (1992) 14 NZTC 9,101, 9,103. In *CIR v Wattie* (1998) 18 NZTC 13,991 Lord Nolan confirmed that similar principles apply to both expenditure and receipts and that the *Hallstroms* approach is to be adopted in determining whether a receipt is capital or revenue:

It is well settled that in considering whether a particular item of receipt or expenditure is of a capital or revenue nature the approach to be adopted should be that described by Dixon J in *Hallstroms Pty Ltd v FCT* (1946) 72 CLR 634 and p 648 where he said that the answer to the question:-

“...depends on what the expenditure is calculated to effect from a practical and business point of view, rather than upon the juristic classification of the legal rights, if any, secured, employed or exhausted in the process.”

Dixon J was speaking in terms of expenditure but it is familiar law that within the context of the same business, similar principles will apply to payments and to receipts. This appears from the general discussion of the earlier cases by Lord Macmillan in *Van Den Berghs Ltd v Clark* [1935] AC 431 at pp 438 to 41, and from the *Borthwick* case itself, which was concerned with the character of a receipt. (p. 13,997)

In determining whether a receipt is capital or revenue, the issue is the consideration provided for the payment. Where the recipient does not provide consideration for the payment it is appropriate to consider the purpose of the payment. In *The Federal Coke Company Ltd v FCT* 77 ATC 4255 Brennan J said:

When a recipient of moneys provides consideration for the payment, the consideration will ordinarily supply the touchstone for ascertaining whether the receipt is on revenue account or not. The character of an asset which is sold for a price, or the character of a cause of action discharged by a payment will ordinarily determine, unless it be a sham transaction, the character of the receipt of the price or payment. The consideration establishes the matter in respect of which the moneys are received. The character of the receipt may then be determined by the character, in the recipient's hands, of the matter in respect of which the moneys are received. Thus, when moneys are received in consideration of surrendering a benefit to which the recipient is entitled under a contract, it is relevant to enquire whether or not that benefit was a capital asset in his hands. To adapt the words of Lord Macmillan in *Van den Berghs Ltd. V. Clark* (1935) A.C. at p. 443, and of Williams J. in *Bennett v. F.C. of T.* (1947) 75 C.L.R. 480 at p. 485, the enquiry is whether the congeries of the rights which the recipient enjoyed under the contract and which for a price he surrendered was a capital asset.

When a recipient gives no consideration for a receipt, it is not possible to identify the matter in respect of which the moneys are received by reference to rights which the recipient surrenders. Nevertheless, an enquiry into the “how and why” of the receipt may reveal the matter in respect of which the payment is received. If there be a consensus between the payer and the payee, their common understanding may identify the relevant matter. The intention or understanding of the payer alone is insufficient for “it would plainly be unsound to allow a determination of the character of a receipt in the hands of the recipient to be affected by a consideration of the uncommunicated reasoning which led the payer to agree to pay it” (*McLaurin v. F.C. of T.* (1961) 104 C.L.R. 381 at p. 391). (p. 4,273)

Therefore, the character of the asset sold for the payment or the character of the cause of action discharged by the payment will ordinarily determine the character of the payment.

Treaty settlements do not involve a gain from property, nor do they involve the provision of services. Treaty settlements are one-off events. Although it is possible that Treaty settlement payments could be made in instalments, regularity or recurrence of itself does not indicate that the payments are income. It is also necessary to consider the relationship between the payer and payee and the purpose of the payment in order to determine whether the payments are income: see *Reid v CIR* (1985) 7 NZTC 5,176. Treaty settlements may include the giving of undertakings by the claimants (such as an agreement that the settlement is full and final settlement of claims under the Treaty). However, the settlements are not paid *for* such undertakings. The undertakings are part of the procedure by which a Treaty claim is settled. Financial redress under a Treaty settlement is paid in order to provide compensation for historical breaches of a Treaty between the Crown and the ancestors of the members of claimant groups.

Where compensation is paid for the deprivation of an asset of a capital nature, the compensation will also be a receipt of a capital nature: see *Burmah Steamship Co Ltd v IRC* (1930) 16 TC 67. In *Burmah Steamship* Lord Clyde said:

It is true that the measure by which the amount of damages or compensation is ascertainable is no criterion of the capital or revenue character of the sum recovered for the purpose of adjusting an Income Tax account of profits and gains (*Glenboig Union Fireclay Coy. v Inland Revenue*, 1921 S.C. 400, 1922 S.C. (H.L.) 112). But, as the case just referred to shows, it is very relevant to enquire whether the thing in respect of which the taxpayer has recovered damages or compensation is deprivation of one of the capital assets of his trading enterprise, or — short of that — a mere restriction of his trading opportunities.

The purpose of the financial redress made under a Treaty settlement is to compensate the claimants for a loss caused by breaches of the Treaty. Such a loss is a loss of a capital nature, being assets held by Maori at the time the Treaty was signed.

### *Conclusion*

Given the above, the Commissioner considers that financial redress provided to settle historical Treaty grievances is not income under ordinary concepts in terms of section CD 5.

### ***Crown forestry land settlements***

- Generally compensation payments made to settle historical Treaty grievances (including compensation payments made on the return of Crown forestry land to Maori ownership) are not income under section CD 3 or section CD 5.

- In some circumstances Treaty settlement payments in respect of Crown forestry land are also exempt under section CB 5(1)(n). The circumstances in which Crown forestry settlement payments are exempt under section CB 5(1)(n) are discussed in detail below.
- Although the Commissioner considers that section CD 3 and section CD 5 would not apply to Treaty settlements in respect of Crown forestry land, a number of other provisions could apply to such Crown forestry settlement payments as are not exempt under section CB 5(1)(n). These provisions (which are discussed below) are: sections CE 1(1)(a) and (e), CE 2 and CJ 1.

***Exemption under section CB 5(1)(n) in respect of compensation payments made under the CFAA***

The consequences when Crown forestry land is returned to Maori ownership under a Treaty settlement are set out in the CFAA.

The Crown has sold forests on Crown forestry land and has granted licences in respect of Crown forestry land to the licensees. If Crown forestry land is returned to Maori ownership, it will be returned subject to a licence, which will terminate at the end of the notice period (35 years from the applicable date): see section 13(5) CFAA. Forests on the land are not returned to the successful claimants, the forests having previously been transferred to the licensees. During the termination period the licensees will continue to have the right to harvest trees growing on the land at the time the land is returned. The land will be resumed progressively by the claimants as trees growing on the land at the time of its return are harvested.

On the return of Crown forestry land to Maori ownership, the Crown must pay compensation to the Maori to whom ownership of the land is transferred in accordance with the First Schedule to the CFAA: section 36 CFAA; clause 1 First Schedule. There are two aspects to the compensation paid under the CFAA:

- First, in every case where Crown forestry land is returned to Maori an amount equal to five percent of the “specified amount” (however the specified amount is calculated) must be paid in order to compensate for the fact that the land is returned “subject to encumbrances” (that is, subject to the right of licensees to continue to harvest trees standing on the land until the end of the termination period): clause 2(b) First Schedule CFAA.
- Secondly, the Crown is required to pay further compensation, being the balance of the specified amount or such lesser amount as the Tribunal may recommend: clause 2(b) First Schedule CFAA. Section 8HB of the TOWA (which empowers the Tribunal to hear claims in relation to land licensed under the CFAA) does not indicate what matters the Tribunal is to take into account in determining the further compensation to be paid. However, the function of the Tribunal is to inquire into and make recommendations to the Crown on claims alleging a breach by the Crown of the principles of the Treaty. In *NZ Maori Council v AG* [1994] 1 NZLR 513 the Privy Council commented on the meaning of “principles of the Treaty” as follows:

In their Lordships’ opinion the “principles” are the underlying mutual obligations and responsibilities which the Treaty places on the parties. They reflect the intent of the Treaty as a whole and include, but are not confined to, the express terms of the Treaty.... With the passage of time, the “principles” which underlie the Treaty have become much more important than its precise terms.



Foremost amongst those “principles” are the obligations which the Crown undertook of protecting and preserving Maori property, including the Maori language as part of taonga, in return for being recognised as the legitimate government of the whole nation by Maori. The Treaty refers to this obligation in the English text as amounting to a guarantee by the Crown. This emphasises the solemn nature of the Crown’s obligation. It does not however mean that the obligation is absolute and unqualified. This would be inconsistent with the Crown’s other responsibilities as the government of New Zealand and the relationship between Maori and the Crown. (p. 517)

Therefore, on the return of Crown forestry land the successful claimants will receive at least 5 percent of the “specified amount” calculated in accordance with clause 3 and could receive as further compensation, an amount up to the balance of the “specified amount”, unless the Tribunal determines that a lesser amount should be paid. Each of the amounts referred to in clause 3 are measures of the value of the forests on the land returned. Under clause 3 of the First Schedule the “specified amount” is whichever of the following amounts is nominated by the successful claimants:

- The market value of trees on land returned as at the time of the recommendation to return the land becomes final (clause 3(a) of the First Schedule CFAA);
- The market stumpage harvested under the licence from trees on the land returned from the date that the recommendation to return the land becomes final; (clause 3(b) of the First Schedule CFAA).
- The net proceeds received by the Crown from the sale of the forests on the land to be returned “plus a return on those proceeds for the period between the transfer and the return of the land to Maori ownership” (clause 3(c) of the First Schedule CFAA).

The Income Tax Act 1976 was amended with effect from 25 October 1989 by the addition of section 61(62) (now section CB 5(1)(n)). Under section CB 5(1)(n) to the extent that in the absence of that provision, the payments would be gross income, payments of compensation under the First Schedule (except clause 3(b)) of the CFAA are exempt income. Therefore, compensation paid under the CFAA would be exempt income under section CB 5(1)(n), unless it is calculated under clause 3(b), that is, by reference to the market stumpage.

*Whether compensation payable under the CFAA would be gross income in the absence of section CB 5(1)(n)*

Section CB 5(1)(n) exempts compensation payments under the CFAA “to the extent that in the absence of that section” they would be gross income. The Commissioner considers that compensation payments made under the CFAA to claimant groups on the return of Crown forestry land to Maori ownership would not (in the absence of section CB 5(1)(n)) be gross income under sections CD 3, CE 1(1)(e), CE 2, CJ 1, CE 1(1)(a) or CD 5. These provisions are discussed below.

(a) *Amounts derived from a business – section CD 3*

For the reasons outlined previously, the pursuit of a Treaty settlement in respect of Crown forestry land is not a business in itself and if the successful claimants carry on another activity which constitutes a business, compensation payments under the CFAA are not amounts derived from such a business.

(b) *Payments for use of land – section CE 1(1)(e)*

Section CE 1(1)(e), which refers to amounts derived by the owner of land from a lease, licence or easement in respect of land or from the grant of a right of taking profits of the land, does not apply to the compensation payments for the following reasons:

- The payments are not received by the claimants as owners of the land, nor are they received from a licence or for the grant of cutting rights in respect of timber on the land. The payments would be received on the transfer of ownership of Crown forestry land to the successful claimants. Under the terms of the Crown Forestry Rental Trust on the return of any licensed land to Maori ownership, the successful claimants are entitled to receive the rental received by the trustees in respect of that land from the commencement of the licence until resumption and to receive future rental direct from the licensee: clause 11.1 of the Deed of Trust. Therefore, past and future rental payments are distinct from and are payable to the successful claimants in addition to the compensation paid under the First Schedule of the CFAA.
- The payments are not received for the grant of a right to take profits of the land. Any grant of cutting rights made in respect of Crown forestry assets is made by the Crown and not by the successful claimants.
- The Crown does not act on behalf of the successful claimants in granting the licences and selling the forests. In the *Crown Forests Assets* case the court considered that the Crown had an obligation under the Treaty to consult with Maori (as the other party to the Treaty) about the proposed sale of the forests. The consultation led to the agreement which specified how Crown forestry land and Crown forestry assets were to be dealt with pending resolution of claims under the Treaty and the consequences once a claim was resolved. The Maori Council and the Federation of Maori Authorities consented to the creation of the licences and the sale of the forests but until a recommendation of the Tribunal that the land be returned to the successful claimants is accepted by the Crown, the claimants have no rights in respect of the land other than inchoate rights under the Treaty.

(c) *Amounts derived from the use or occupation of any land – section CE 2*

Section CE 2 refers to amounts derived from the use or occupation of land. In *Smith v CIR* [1969] NZLR 565 it was held that section 91(a) of the Land and Income Tax Act 1954 (which included in the definition of income “all profits or gains derived from the use or occupation of land”) did not apply to a profit derived from the assignment of a right to cut timber. Although that right was an interest in land, the court considered that neither the original grantee nor the assignees acquired any property in the land. The court considered that section 91(a) was limited to the gain derived from the use or occupation of the land in the sense of a tangible, physical thing. Haslam J said:

Mr Carroll also rested part of his argument upon the submission that the term “land” embraced all estates or interests therein, and referred to the definition of the phrase “owner of land” in s. 2 of the Act, which applies “unless the context otherwise requires”. The word “land” itself is defined, with an even stronger qualification about inconsistency in the context, in s. 4 of the Acts Interpretation Act 1924 as including “. . . messuages, tenements, hereditaments . . .”. While the right created by the grant under review would fall within the relevant

passage in either statutory definition, I think that in the context of s. 91 the term “land” should be read in its primary connotation. I read the section as designed to clarify and extend the incidence of taxation in relation to profits and gains derived from the use and occupation of land. If this word be considered in its setting in s. 91 (1) (a), then emphasis is given to the financial yield derived by virtue of use or occupation by the taxpayer.... I conclude therefore that in s. 91 this word bears its everyday sense of a solid part of the earth's surface, and does not include estate or interest in realty. (p. 568-569)

The Commissioner considers that section CE 2 applies to amounts derived from agricultural use of the land. The Commissioner considers that section CE 2 does not apply to compensation payments made under the CFAA. Clause 2 of the First Schedule to the CFAA recognises that the land is returned subject to rights of the licensees which effectively prevent the claimants from having full use of the land while the licensees retain the right to cut trees situated on the land. The compensation is, in part, compensation for the fact that the land is returned subject to the use or occupation by the licensees. However, for section CE 2 to apply, the amounts must be derived from the actual physical use of the land by the successful claimants rather than as a consequence of the successful claimants having an interest in the land.

Section CE 2 is expressed to be “subject to” section CJ 1. Therefore, section CJ 1 prevails over section CE 2 where the receipts in question are amounts derived from the sale of timber: refer *C & J Clark Ltd v IRC* [1971] 1 WLR 905.

(d) *Amounts derived from the sale of timber or right to take timber – section CJ 1*

The Commissioner considers that the compensation payments are not income under section CJ 1(1) or (2) for the following reasons:

- Under section CJ 1(1) amounts deemed to have been derived under section FB 4, GD 1 or GD 2 from the sale or disposition of timber or the right to take timber are income. Sections FB 4, GD 1 and GD 2 would apply where the timber is trading stock. Even if these provisions were relevant, a claimant group to which Crown forestry land is returned would not derive any amounts from the sale of timber or the right to take timber. The grant of the licence and the sale of forests are made by the Crown and not by the claimants. When forestry land is returned to Maori claimants, the forests standing on that land are not returned to them. The forests have been transferred outright to licensees and in terms of section 13 of the CFAA, for the purposes of the transfer, the forestry assets and the land are regarded as separate assets each capable of separate ownership. On the return of the land to Maori ownership the rights of the licensee are preserved. Timber harvested from Crown forestry land that is subject to a licence is sold by the licensee, not by the claimants.
- In terms of section CJ 1(2) the sale or disposition of standing timber is gross income except:
  - Timber that is comprised in ornamental or incidental trees; or
  - Timber that is subject to a forestry right;
  - Timber that is subject to a profit à prendre granted before 1 January 1984.

The compensation is not paid for the sale of standing timber as the forests are not owned by the successful claimants. The forests are sold by the Crown to the licensees before the return of the land to Maori.

(e) *Interest – section CE 1(1)(a)*

The “specified amount” under clause 3(c) of the First Schedule includes a return on the net proceeds received by the Crown from the transfer of Crown forestry assets to which land to be returned to Maori ownership relates.

Under the common law, interest is the consideration for the use of a sum of money owed to or belonging to another person: *Re Euro Hotel (Belgravia) Ltd* [1975] 3 All ER 1075.

The true character of the payment is not determined by its description in the agreement or the legislation. In *Riches v Westminster Bank Ltd* [1947] AC 390 Viscount Simon commented:

The real question, for the purpose of deciding whether the Income Tax Acts apply, is whether the added sum is capital or income, not whether the sum is damages or interest. (p. 396)

Viscount Simon went on to say:

I come then to the second stage and ask what is the character of interest allowed under section 28 of the [Civil Procedure] Act of 1833. Here the argument is that, call it interest or what you will, it is damages and, if it is damages, then it is not interest in the proper sense’ or ‘interest proper’, expressions heard many times by your Lordships. This argument appears to me fallacious. It assumes an incompatibility between the ideas of interest and damages for which I see no justification. It confuses the character of the sum paid with the authority under which it is paid. Its essential character may be the same, whether it is paid under the compulsion of a contract, a statute or a judgment of the court. In the first case it may be called ‘interest’ and in the second and third cases “damages in the nature of interest” or even “damages”. But the real question is still what is its intrinsic character, and in the consideration of this question a description due to the authority under which it is paid may well mislead. (p. 406)

A distinction has been drawn in case law between an amount paid to compensate for a loss of a capital nature that is calculated by reference to interest (which remains a receipt of capital) and an amount paid to compensate for a delay in payment of compensation once the amount of the compensation has been determined (which is income under ordinary concepts). The application of this principle is illustrated by *Simpson v Executors of Bonner Maurice as Executor of Edward Kay* (1949) 14 TC 580. The *Bonner Maurice* case concerned a UK resident and national who, at the outbreak of the First World War, owned German stocks and shares which were deposited with banks in Germany. The dividends and interest were collected by the banks. During the war money could not be sent from Germany to the UK so that the dividends and interest accumulated in the banks. In 1917 some of the dividends and interest were paid to an official called the Treuhander. After the end of the war the money was returned to the representatives of the original owner under the Treaty of Versailles. They also received payments under a provision of the Treaty of Versailles which provided that nationals of the Allied and Associated Powers should be entitled to “compensation in respect of damage or injury inflicted upon their property, rights or interests” in Germany. That compensation was calculated on the basis of interest at 5 percent over the amount handed over to the Treuhander. Rowlatt J held that the compensation was not income:

The Treuhander did not receive this money subject to any liability to hold it as interest. No doubt the German law recognised it as remaining the property of [the British national], but not so as to bear interest. The Treaty did not give [the British national] any right to interest, nor did it declare the Treuhander a trustee so as to found any consequential claim for interest; it did not empower the tribunal to give interest as such, or to make any declaration as to the character of the purpose for which the Treuhander had held the money. The Treaty gave compensation, and the tribunal which assessed the principal sum has assessed it on the basis of interest. I think this sum first came into existence by the award, and no previous history or anterior character can be attributed to

it. It is exactly like damages for detention of a chattel, and unless it can be said that damages for detention of a chattel can be called rent or hire for the chattel during the period of detention, I do not think this compensation can be called interest. (pp. 592-593)

In *Raja's Commercial College v Gian Singh & Co Ltd* [1977] AC 312, the Privy Council explained the *Bonner Maurice* case. Lord Fraser, who gave the judgment of the Privy Council, commenting on the above passage from the judgment in that case, said at p. 322:

The last sentence of that passage is no doubt quite accurate in relation to chattels which, if not detained, would have been used by the owner for his own purposes but it is not applicable to chattels which the owner would have let out on hire, for example a motor-car belonging to a car rental firm or a TV set owned by a rental company. In the Court of Appeal Lord Hanworth MR said that the compensation was for preventing the British national from exercising the power of disposition over his property and he went on to say, at p. 602:

“The way to estimate that compensation or damages – the sensible way no doubt – would be by calculating a sum in terms of what interest it would have earned. That has been done, but the sum that was paid has not been turned into interest so as to attach income tax to it. It remains compensation and, for these reasons, it appears to me that it is not a sum which attracts or attaches income tax to it.

Refer also *Public Trustee v CIR* [1960] NZLR 365; *Marshall v Commissioner of Taxes* [1953] NZLR 335; *Whitaker v FCT* 98 ATC 4823.

The Commissioner considers that the situation in the *Bonner Maurice* case is analogous in that compensation under clause 3(c) is compensation for a loss of a capital nature which is calculated by reference to interest. The entitlement of the successful claimants to the amount would come into existence if their claim was successful but they have no previous entitlement to the payment of an amount representing a return on the net proceeds received by the Crown from the transfer of the Crown forestry assets to which the land returned relates.

The statutory definition of “interest” refers to a payment made “in respect of or in relation to money lent” except repayment of the principal sum: section OB 1. At its widest, “money lent” includes an “amount paid to, or for the benefit of, or dealt with in the interest of or on behalf of, any other person in consideration for an agreement or a promise to pay by the other person, where that amount is exceeded by the amount payable to the person in accordance with the agreement or the promise”: para (d), definition of “money lent” in section OB 1. The Commissioner considers that a Treaty settlement in respect of Crown forestry land does not involve the successful claimants paying an amount to the Crown in consideration for an agreement by the Crown to pay a greater amount.

Therefore, the Commissioner considers that where compensation payments are determined under clause 3(c) and an imputed return is added to the net proceeds of sale in order to calculate the specified amount under clause 3(c), compensation payments would not (in the absence of section CB 5(1)(n)) be interest.

(f) *Income under ordinary concepts – section CD 5*

Whether a payment is of a capital or revenue nature depends on what the payment is calculated to effect from a practical and business point of view: *Hallstroms Pty Ltd v FCT* (1946) 72 CLR 634. The character of the asset transferred for the payment or the character of the cause of action discharged by the payment will ordinarily determine the character of the payment: *The Federal Coke Company Ltd v FCT* 77 AT 4255.

The stated purpose of the compensation paid under clause 2(a) of the First Schedule (that is, an amount equal to 5 percent of the “specified amount”) is that it compensates for the fact that the land is returned subject to the rights of the licensee to continue to harvest trees on the land. A payment which represents compensation for the loss in value of land, that is a capital asset, or for interference with the ability of the claimants to use the land, is a payment of a capital nature: *Barrett v FCT* 15 ATD 149 and *Nullaga Pastoral Co Pty Ltd v FCT* 78 ATC 4329.

The Commissioner considers that payments of compensation under clause 2(a) of the First Schedule to the CFAA are not income as they are paid in order to compensate for the fact that the claimants do not immediately have full use of the land. The payments do not constitute consideration for a right to take something from the land, this right having previously been granted by the Crown to the licensee.

The successful claimants may also receive further compensation of an amount up to the balance of the specified amount. Settlements in respect of Crown forestry land and Crown forestry assets are settlements of claims for compensation in relation to historical breaches by the Crown of its obligation under the Treaty protect the Maori people in the use of their lands and other assets held at the time that the Treaty was signed. The CFAA applies only to forests which are principally exotic forests standing on Crown forestry land. In the *Crown Forests Assets* case the Court of Appeal referred to the possibility that the principles of the Treaty may not entitle Maori to share equally in the ownership of exotic forests. The settlement (which is reflected in the CFAA) appears to acknowledge that possibility as, in terms of clause 2(b) of the First Schedule of the CFAA, the successful claimants would receive less than 100 percent of the value of the forests (the specified amount), if the Tribunal so determines.

The Commissioner considers that compensation under the First Schedule to the CFAA (however it is calculated) relates to capital assets of the claimants. The Commissioner, therefore, considers that the compensation payments are not income under ordinary concepts.

### *Conclusion*

The issue of whether compensation under Crown forestry settlements is interest has been considered because it is not clear why compensation in relation to Crown forestry land settlements was exempt income in some cases but not others. Whether compensation under the CFAA is exempt income depends on the method used to calculate the amount of the compensation. One of those methods appeared to include an amount based on the time value of money: clause 3(c) Schedule to the CFAA. Compensation payments under the CFAA (except compensation calculated under clause 3(b), that is, compensation calculated by reference to market stumpage) are exempt income under section CB 5(1)(n). The question of whether compensation under the CFAA would be income in the absence of section CB 5(1)(n) has been considered in an attempt to ascertain the policy underlying the exemption.

Section CB 5(1)(n) applies to the extent that in the absence of that provision Crown forestry compensation payments would be gross income. Section CB 5(1)(n) does not, however, provide that such payments are income. The CFAA and section CB 5(1)(n) reflect the terms of the settlement between the Crown and the Maori Council. It appears that the predecessor of section CB 5(1)(n) was enacted in order to confirm what the parties to the settlement considered was the existing position. The Commissioner considers that the better view is that the exclusion was not intended to alter the existing position, which was that compensation

payments (however calculated) would not have been gross income under the predecessors of sections CD 3, CD 5, CE 1(1)(a) or (e), CE 2 or CJ 1. Compensation in relation to Crown forestry settlements would not be gross income under sections CD 3, CD 5, CE 1(1)(a) or (e), CE 2 or CJ 1 in the absence of section CB 5(1)(n).

***Whether financial redress under Treaty settlements is income under the accrual rules***

In most cases settlement legislation is required in order to ensure the finality of a Treaty settlement, to provide for Statutory Instruments, to remove statutory memorials from land titles in the claim area and to vest land in the claimant group, if normal administrative land transfer processes would not be appropriate. Therefore, there may be a delay between the settlement being agreed and payment being made. Settlements may be conditional upon the passing of settlement legislation.

For the accrual rules to apply there must be a financial arrangement. Paragraph (a) of the definition of “financial arrangement” in section EH 22(1) refers to a debt or debt instrument. The Commissioner considers that where a settlement is conditional on the passing of legislation to give effect to the settlement, the settlement does not give rise to a debt or debt instrument in terms of paragraph (a) of the definition of “financial arrangement”, as the obligation to make payment will not be unconditional. To be a debt or debt instrument, there must be an unconditional obligation to make payment: *Case Q2* (1993) 15 NZTC 5,005. In *Case Q2* Judge Willy said:

The 1987 report of the Consultative Committee, Exhibit 3, contained an information release from the Office of the Minister of Finance relevant to this matter. In explaining the definition of “financial arrangement” the Minister says:

“The definition includes within the umbrella term financial arrangement or debt instrument. The term debt instrument has been used as it describes most financing arrangements involving the provision of credit in money or monies worth. The term debt instrument is intended to apply to every conceivable type of the [sic] provision of credit including all forms of Government commercial paper, Government stock, Treasury Bills, Kiwi Bonds and so on. And whether or not secondary market operators reconstruct split or hybridise such instruments. It is intended to include everything that is not equity and to avoid artificial distinctions based on technical legal rather than economic or substantial differences.”

It should be noted at this point that in law a “debt” is usually defined as a sum of money payable in respect of a liquidated money demand recoverable by action; *Rawley v Rawley* [1886] 1 QBD 460 or as it was put in *Ogdens Limited v Weinberg* (1906) 95 TLR 567 by Lord Davey.

“The word debt no doubt means something recoverable by an action for debt and nothing can be recovered in an action for debt except what is ascertained or can be ascertained. A claim for an amount which is uncertain and cannot be adjusted in an account cannot I think be justly called a debt.”

In *Words and Phrases Legally Defined*, 3rd Edition, it is said that the legal definition of a debt is “a sum of money due by certain and expressed agreement”. (p. 5014)

This aspect of the judgment was not discussed in the appeal of the case (*CIR v Dewavrin Segard (NZ) Ltd* (1994) 16 NZTC 11,048).

For there to be a financial arrangement in terms of paragraph (b) of the definition, there must be:

- An arrangement;
- Under which [the Crown] receives money;
- In consideration for the Crown providing money to the claimant group at a future time.

The definition of “money” in section OB 1 includes “money’s worth” whether or not it is convertible into money. In *McElwee v CIR* (1997) 18 NZTC 13,288 the High Court held that although a benefit need not be convertible into money to be “money’s worth” for the purposes of the accruals provisions, it must be able to be valued. Therefore, the court held that a guarantee for no consideration was not a financial arrangement. The High Court accepted the following comments by Glazebrook & Oliver in *The New Zealand Accrual Regime – a practical guide* (1989) at p 51:

The second operating principle of accrual income and expenditure calculations is that all benefits received and provided under a financial arrangement which are included in accrual calculations must be convertible into monetary equivalents. This principle is not explicit in the legislation but can be inferred from the fact that the accrual rules operate on what are essentially cash flow calculations. If a benefit is not given a monetary equivalent, it cannot be included in the accrual calculation. This is not to say that a benefit must in practice be convertible into money.... What is required is that the benefit be able to be assigned a monetary value.

The Commissioner considers that a Treaty settlement is not a financial arrangement under paragraph (b) of the definition of that expression as the payment made by the Crown is not “in consideration for” a benefit received by the Crown. Treaty settlement payments are made to compensate the claimants for past economic losses suffered as a result of the Crown’s breaches of the Treaty rather than in return for anything provided to the Crown under a Treaty settlement. Undertakings or agreements given by the claimants under a Treaty settlement are merely part of the process by which settlement is effected.

### *Conclusion*

The Commissioner considers that a Treaty settlement where payment is delayed until the passing of settlement legislation is not a financial arrangement. Where a Treaty settlement is conditional upon the passing of settlement legislation, the settlement is not a “debt or debt instrument”. A Treaty settlement is also not a “financial arrangement” in terms of paragraph (b) of the definition of that term.

### *Claimant funding*

The first stage in a direct negotiation with the Crown is that representatives of the claimant group must establish that they have a mandate to represent the members of the group and the Crown must accept that there is a well-founded grievance. Once that stage has been reached, the claimant group may apply to the Crown for reimbursement of the costs incurred in seeking a mandate (locating, registering and informing members of the claim). The claimant group can also apply for further funding for the cost of negotiating the Terms of Negotiation and for the costs of negotiating the final Deed of Settlement. The OTS publication says that the Crown will not necessarily provide full funding for negotiations. In assessing the amount of the Crown’s contribution the OTS will take into account the following matters:

- The complexity of the claim;
- Whether there are any overlapping claims or interests that need to be taken into account;



- Whether there is consensus within the claimant group regarding the negotiations;
- The size of the claimant group and whether the members are scattered throughout the country;
- Whether consultation is likely to require hui to be arranged outside the main city centres.

The funding for the negotiation process is paid in instalments. Periodicity, recurrence and regularity are indicators that receipts are income but these factors are not conclusive: *Reid v CIR*. In order to determine the character of a payment in the hands of the recipient it is necessary to establish what is the consideration provided for the payment and if no consideration was given for the payment, the circumstances in which the payment is received must be considered: *Federal Coke*.

Although the timing of the payment of instalments is linked to milestones in the settlement negotiations, there is no obligation to repay instalments already received if milestones are not met. The OTS publication also makes it clear that the Terms of Negotiation and the Heads of Agreement are entered into on a “without prejudice” basis. Neither party is bound until the Deed of Settlement is finally executed following ratification.

At the time when funding is approved the Crown accepts that the claimant group has suffered from breaches of the Treaty and its principles. No funding is provided before the claimant group has established that it has a mandate because the Crown does not wish to be seen to take sides. The negotiations relate to the content of the settlement package, including what is to be included in the Crown’s acknowledgement and apology, the nature of cultural redress and the nature or quantum of the assets or cash that are to be transferred to the claimants: see p. 84 OTS publication.

The funding is provided by the Crown in order to facilitate the settlement of Treaty grievances. The benefit sought by the Crown from the provision of funding is comprehensive and lasting settlements. Comprehensive and lasting settlements are not possible unless they are supported by the members of the claimant group and unless all historical grievances are addressed in the settlement. Funding is provided to claimant groups to enable them to consult with their members and in order to enable all grievances to be dealt with in the settlement. The amount of the funding is determined by the complexity of the Treaty claim and by the degree of difficulty likely to be encountered by the claimant group in consulting with members and obtaining ratification of the settlement.

The Commissioner considers that claimant funding does not represent consideration for any income earning activity carried on by claimant groups and is not income under ordinary concepts. The funding is not a payment for a product or a service supplied by the claimants and is not income from a business. The funding is not made available for the provision of research to the Crown. Normally direct negotiations are undertaken in circumstances where sufficient historical research has already been carried out to enable the Crown to determine that there has been a breach. The OTS publication specifically says that the Crown does not provide funding for research (p. 43 OTS publication). The negotiation process is not a business in itself and is not part of the ordinary business operations of a business carried on by a claimant group. Claimant funding is provided when it is accepted that there is a basis for a Treaty claim and the funding is provided in order to facilitate the comprehensive and lasting

settlement of Treaty grievances by enabling claimant groups to consult with their members and by enabling all grievances to be addressed in the settlement.

*Payment in the nature of a subsidy or grant in respect of a business carried on by claimant groups – section DC 1*

Section DC 1(2) applies to a payment in the nature of a subsidy or grant in respect of any business carried on by a taxpayer made to the taxpayer by the Development Finance Corporation New Zealand or the New Zealand Film Commission or any department or instrument of the Executive Government of New Zealand and to expenditure in respect of which such a grant is made: section DC 1(1). The effect of section DC 1(2) is that any deduction allowable in respect of the expenditure incurred by the taxpayer in respect of which such a grant is made is reduced by the amount of the grant and the amount of the grant is deemed not to be gross income. Therefore, if section DC 1(2) applied, the expenditure equivalent to the amount of the claimant funding would not be an allowable deduction and the amount of the claimant funding would not be income.

The test of whether an entity is an instrument of the executive government of New Zealand is the degree of control which Ministers or central government agencies exercised over the entity: *CIR v Medical Council of NZ* (1997) 1 NZTC 13,088. The OTS which is subject to a high degree of control from its Minister and Cabinet is an instrument of the executive government of New Zealand. However, the Commissioner considers that even if claimant funding was a payment in the nature of a grant or subsidy, the claimant funding is not a grant made in respect of any business carried on by claimant groups. As outlined previously, the negotiation of a Treaty settlement is not a business, or part of any other business carried on by the claimant group or individual members of the claimant group. Therefore, section DC 1 does not apply to funding towards negotiating costs provided to claimant groups by the OTS.

*Conclusion*

The Commissioner considers that funding provided to claimant groups to cover the costs of negotiating a Treaty settlement is not an amount derived from any business carried on by a claimant group (section CD 3) and is not income under ordinary concepts (section CD 5). As the funding is not a payment in respect of any business carried on by a claimant group, section DC 1 does not apply.

**Conclusions**

The Commissioner considers that:

1. Financial redress paid by the Crown to a claimant group as compensation for historical breaches of the Crown's obligations under the Treaty:
  - is not gross income under section CD 3. The pursuit of a Treaty claim is not a business in itself as a Treaty claim is made to recover compensation for a loss for both economic losses and non-economic losses rather than with the intention of making a profit. Although some claimant groups or individual members of a claimant group may carry on a business, the payment would not be an amount derived from any business carried on by the claimant group as the payment is made to compensate for a loss of a capital nature; and

- is not gross income under section CD 5 as the payments are made to compensate the claimant group for the loss of an asset of a capital nature. The payments do not involve a gain from property, do not involve the provision of services and are not made for undertakings given by the claimant group.
2. Compensation paid under the First Schedule to the CFAA on the return of Crown forestry land to a claimant group is exempt income under section CB 5(1)(n) where the amount of the compensation is calculated under clauses 3(a) and 3(b) of the First Schedule, that is, by reference to the market value of forests on the land returned or by reference to the net proceeds received by the Crown from the sale of the forests. In the absence of section CB 5(1)(n) compensation paid under the First Schedule to the CFAA (including compensation calculated by reference to market stumpage in terms of clause 3(b)) would not be income as the compensation:
- is not gross income under section CD 3 as a Treaty claim does not constitute a business in itself and the compensation would not be an amount derived from any business that may be carried on by the claimant group or the members of a claimant group;
  - is not gross income under section CE 1(1)(e). The compensation is not an amount derived by the claimants from a licence or for the grant of cutting rights in respect of timber on the land or for the grant of a right of taking profits of the land. Licences and cutting rights are granted by the Crown to the licensees before the return of any Crown forestry land to a claimant group under a Treaty settlement. Past licence payments in respect of the land are held by the Crown Forestry Rental Trust for the benefit of the claimant group and future licence payments would be made to the claimant group in addition to compensation under the CFAA.
  - is not gross income under section CE 2. The compensation is not derived by the claimant group from the use or occupation of land. The compensation is paid, in part, as compensation for the fact that the claimant group does not immediately have the use and occupation of the land as the land is returned subject to the rights of the licensees.
  - is not gross income under section CJ 1. The compensation is not derived from the sale of timber, the right to take timber or standing timber. The right to take timber is sold by the Crown to the licensees before the return of the land to the claimant group.
  - where compensation is calculated under clause 3(c) of the First Schedule to the CFAA and includes an imputed return on the net proceeds of sale received by the Crown from the sale of the forests on the land, the compensation does not include interest which is gross income under section CE 1(1)(a). The compensation is not consideration for the use of money owed to or belonging to the claimant group, and is not paid in respect of “money lent”, as defined in section OB 1.
  - is not gross income under section CD 5 as the payment is paid as compensation for the fact that the land is returned subject to the rights of the licensees (so that the

ability of the claimant group to use the land is impeded) and as compensation in respect of capital assets of the claimant group.

3. Where the payment of financial redress under a Treaty settlement is delayed until settlement legislation is enacted, the financial redress will not be gross income under section CE 1(1)(c). A Treaty settlement does not constitute a financial arrangement as:
  - A settlement that is conditional upon the passing of settlement legislation is not a debt or debt instrument in terms of paragraph (a) of the definition of “financial arrangement”; and
  - A Treaty settlement does not constitute an arrangement under which the Crown receives money in consideration for the Crown providing money to the claimant group because any benefit received by the Crown under the settlement is an intangible benefit and is not, therefore, “money’s worth”.
4. Funding provided by the Crown through the OTS to a claimant group to enable the claimant group to carry out direct negotiations with the Crown in respect of a Treaty settlement is not gross income under sections CD 3 or CD 5. The benefit sought by the Crown from the provision of the funding is the promotion of comprehensive and lasting settlements by enabling the claimant groups to consult with their members and by enabling all issues to be addressed in the settlement. The funding is not an amount derived from a business carried on by the claimant group as the negotiation process is not a business in itself and is not part of the ordinary business operations of the claimant group. The funding is not income under ordinary concepts as it is not consideration for any product or service provided by the claimant group.