

QUESTION WE'VE BEEN ASKED QB 16/07

INCOME TAX – LAND SALE RULES – MAIN HOME AND RESIDENTIAL EXCLUSIONS – REGULAR PATTERN OF ACQUIRING AND DISPOSING, OR BUILDING AND DISPOSING

The purpose of this Question We've Been Asked (QWBA) is to provide guidance about when **someone will have a "regular pattern" of transactions that means they cannot use the residential exclusion from ss CB 6 to CB 11, and when someone will have a "regular pattern" of transactions that means they cannot use the main home exclusion from the 2-year bright-line test.**

Before the issue of whether there is a **"regular pattern"** arises, one of the taxing provisions in ss CB 6A to CB 11 has to potentially apply, and the residential exclusion or the main home exclusion has to potentially apply (see the flowchart at [10]). This QWBA briefly sets out the criteria for those taxing provisions and exclusions, but the **focus is on when there will be a "regular pattern" of transactions that means the relevant exclusion cannot be used.**

In this QWBA, we use the term **"house" for ease of reference. The term in the residential exclusion from ss CB 6 to CB 11 is "dwellinghouse", and the term in the exclusion from the 2-year bright-line test is a "dwelling".** Those terms could include other dwellings that are not houses (eg, a unit or an apartment).

All legislative references are to the Income Tax Act 2007 unless otherwise stated.

This QWBA is about ss CB 16 and CB 16A.

Question

1. One of the land sale rules in ss CB 6 to CB 11 or the 2-year bright-line test in s CB 6A potentially applies to the sale of my house. I might qualify for exclusions from those rules for my residence or for my main home, but those exclusions may not apply if I have a "regular pattern" of transactions. When will I have a "regular pattern" of transactions that means I cannot use the exclusions for my residence or for my main home?

Answer

2. There are a number of land sale rules in the Act that might tax you on the proceeds of land that you sell or otherwise dispose of. But the provisions that might apply if you are selling your house have exclusions you might be able to use, which would mean you are not taxed. There are different exclusions depending on which provision you could be taxed under.
3. There is an exclusion (in s CB 16) called the **"residential exclusion" which is relevant if you might be taxed under ss CB 6 to CB 11. If that exclusion applies, you will not be taxed under those provisions. But you will not be able to use that exclusion if you have a "regular pattern" of acquiring and disposing of or building and disposing of houses that you occupied mainly as residences.**
4. There is an exclusion (in s CB 16A) called the **"main home exclusion" which is relevant if you might be taxed under the 2-year bright-line test in s CB 6A. If that exclusion applies, you will not be taxed under the bright-line test. But you will not be able to use that exclusion if you have already used the main home**

exclusion twice in the last two years **or if you have a "regular pattern"** of acquiring and disposing of residential land that had your main home on it.

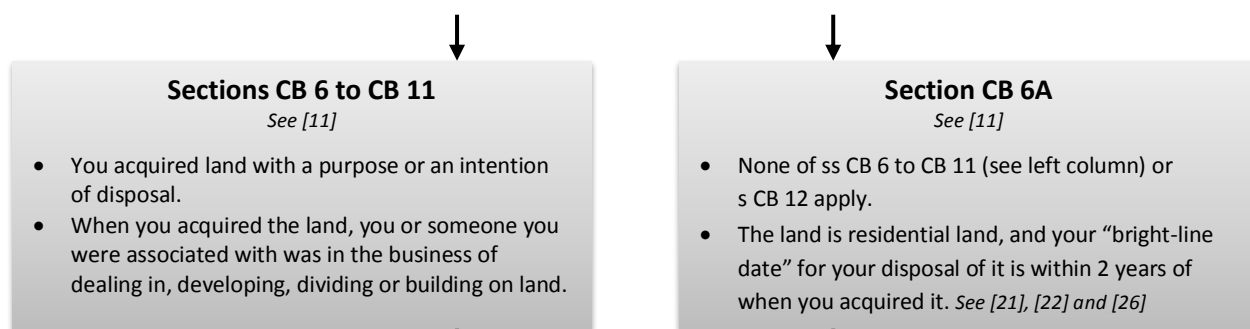
5. Whether **you have a "regular pattern"** of transactions that will mean you cannot use the relevant exclusion will depend on the number of similar transactions and the intervals of time between them. It will be a matter of fact and degree whether you have a regular pattern of such transactions.
6. There is no hard and fast rule about the number of times or how frequently you can buy and sell, build and sell, or renovate and sell houses that you live in and not be taxed. However, generally at least three prior transactions would be needed for there to be a regular pattern.
7. **For there to be a "pattern" there has to be a similarity or likeness between the transactions**. The reason or purpose for each transaction is irrelevant; it is the **similarity of the transactions that is important**. **For a pattern to be "regular" the transactions must occur at sufficiently uniform or consistent intervals**.
8. The transaction being considered as potentially subject to tax is **not** taken into account in deciding whether you have a regular pattern of such transactions.
9. As mentioned at [4], there is also a cap on how frequently you can use the main home exclusion from the 2-year bright-line test. You are not able to use that exclusion if you have already used it twice in the two years before **the "bright-line" date for land you are selling**. This cap applies even if you do not have a "regular pattern" of acquiring and disposing of residential land.

Flowchart – the taxing provisions and exclusions that may be relevant if you sell your house

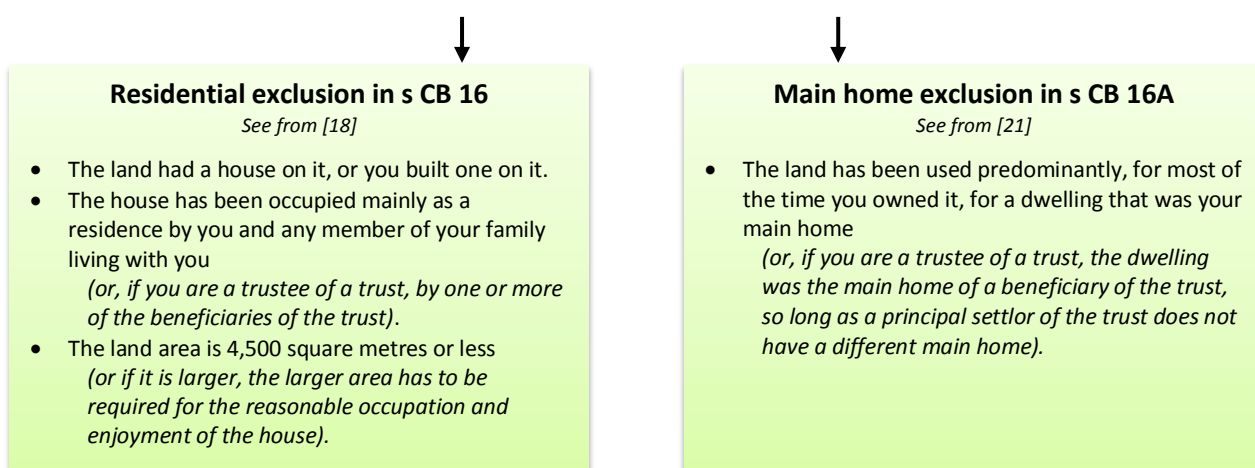
10. The following flowchart shows the main taxing provisions that could apply if you sell your house, the requirements for the residential exclusion and for the main home exclusion that you might be able to use because it was your house, and when you cannot use those exclusions.

For a list of all the land sale provisions that might apply see [11].

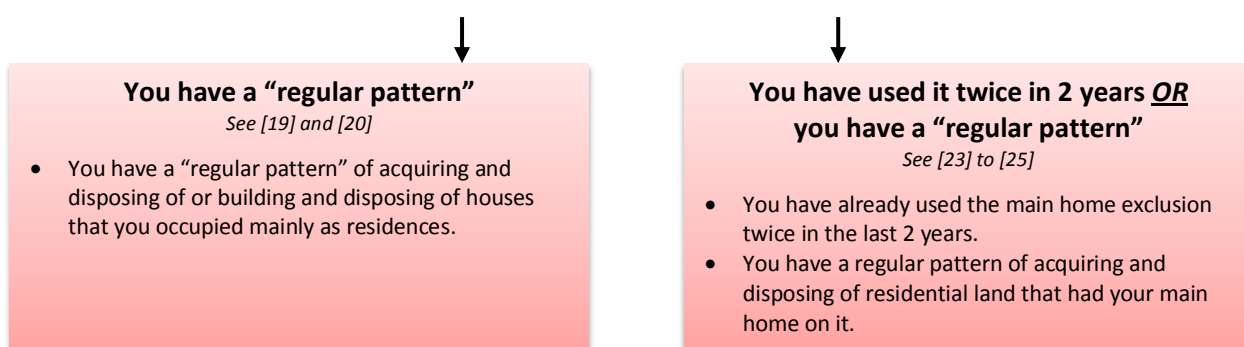
One of these taxing provisions might apply



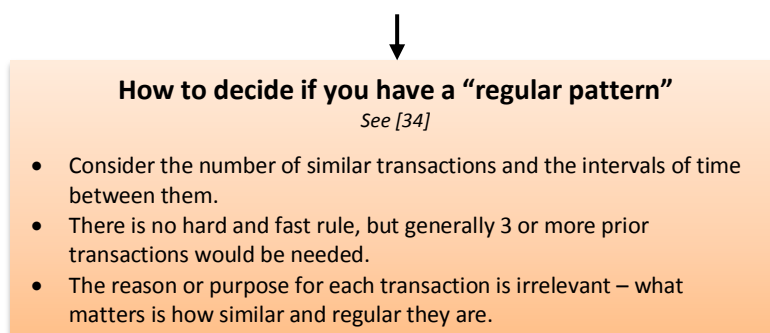
You might get an exclusion because you lived at the property



But the exclusion cannot be used if:



Do you have a “regular pattern”?



Explanation

What taxing provisions might apply to me?

11. There are a number of land sale rules in the Act. These rules might tax you on the proceeds of land you sell or otherwise dispose of. You might be taxed on the proceeds of disposing of land if:
- you acquired the land for a purpose or with an intention of disposing of it (s CB 6);
 - you acquired the land for the purpose of a business (carried on by you or by an associated person) of dealing in land, developing land, dividing land into lots, or erecting buildings (s CB 7);
 - you dispose of the land within 10 years of acquiring it, if at the time you acquired it you were (or were associated with someone who was) in the business of dealing in land, or developing or dividing land (ss CB 9 and CB 10);
 - you dispose of the land within 10 years of completing improvements to it, if at the time the improvements were started you were (or were associated with someone who was) in the business of erecting buildings (s CB 11);
 - the land was part of an undertaking or scheme, meeting certain criteria, that involved the development of land or the division of land into lots (ss CB 12 and CB 13);
 - the land was used as landfill (s CB 8);
 - you dispose of the land within 10 years of acquiring it and 20% or more of the increase in its value arises from any of various factors such as a change to the rules of a district plan, the granting of a consent, or a decision of the Environment Court under the Resource Management Act 1991 (s CB 14);¹
 - you received the land from someone you were associated with, who would have been taxable if they had retained and disposed of the land (s CB 15); or
 - none of sections CB 6 to CB 12 apply, the land is residential land, and the **"bright-line date" for your disposal of the land is within two years of when you acquired it** (s CB 6A).²

But I am not taxed if I lived in the property, am I?

12. There are a number of exclusions from each of the above rules that might be relevant to you. If one of those exclusions applies, you will not be taxed on the sale proceeds.
13. There are exclusions from most of the land provisions for your residence, and there is an exclusion from the 2-year bright-line test for your main home.
14. Section CB 16 is the residential exclusion from ss CB 6 to CB 11, s CB 17 is the residential exclusion from ss CB 12 and CB 13, and s CB 18 is the residential exclusion from s CB 14. Section CB 16A is the main home exclusion from the 2-year bright-line test. Each of those exclusions has different requirements.

¹ See s CB 14(2) for the full list of factors.

² **"Residential land" is defined in s YA 1.** For the purposes of this rule (known as the 2-year bright-line test), the 2-year period generally does not start at the date you acquire land for the purposes of the other land provisions in the Act. In a standard land purchase situation, the 2-year period will start on the date the land title is registered to you. **The "bright-line date" for a disposal of land is typically the date you enter into an agreement for the disposal, but may be different in different circumstances (see s CB 6A(7)).**

15. This QWBA is about one of the criteria of the residential exclusion from ss CB 6 to CB 11 (which is in s CB 16) and the main home exclusion from the 2-year bright-line test (which is in s CB 16A). Both of those exclusions have a requirement that you do not have a regular pattern of transactions. If you do have a regular pattern of the relevant transactions, you cannot use the residential exclusion or the main home exclusion (as the case may be), even though you lived at the property.
16. Note that the residential exclusions in ss CB 17 (relevant for ss CB 12 and CB 13) and CB 18 (relevant for s CB 14) do not have a requirement that there is no "regular pattern".
17. This QWBA explains when a "regular pattern" of transactions will prevent you from being able to use the residential exclusion in s CB 16, and when a "regular pattern" of transactions will prevent you from being able to use the main home exclusion in s CB 16A.

What are the requirements for the residential exclusion from ss CB 6 to CB 11?

18. The residential exclusion in s CB 16 is the relevant exclusion if the proceeds from the sale of your house might be taxed under any of ss CB 6 to CB 11 (those provisions include the purpose or intention provision, and the dealer, developer, subdivider and builder provisions).³
19. To qualify for the exclusion in s CB 16, you have to meet **all** of the following requirements:
 - You acquired the land with a house on it, or built one on it.
 - The house has been occupied mainly as a residence by you and any member of your family living with you or, if you are a trustee of a trust, by one or more of the beneficiaries of the trust.

This means your occupation of the house cannot be incidental to another more significant purpose such as sale (see, for example, *Case G76* (1985) 7 NZTC 1,348, *Case K21* (1988) 10 NZTC 218 and *Case M102* (1990) 12 NZTC 2,634).
 - If there is any land related to the land with the house on it, the total area of the related land has to be 4,500 square metres or less. If it is larger than that, the larger area has to be required for the reasonable occupation and enjoyment of the house.
 - You have not engaged in a regular pattern of acquiring and disposing of houses, or building and disposing of houses, that you occupied mainly as residences (discussed from [31]).
20. As can be seen, one of the requirements of the residential exclusion in s CB 16 is that you do not have a "regular pattern" involving the disposal of land with a house on it. The "regular pattern" has to be either of **acquiring and disposing of houses that you occupied mainly as residences**, or of building and disposing of **houses that you occupied mainly as residences**. It does not matter if you have any other regular pattern involving acquiring and disposing of land, such as industrial land, or residential land that you did not live on.

³ Which also apply if you are associated with a dealer, developer, subdivider or builder, even if you are not one yourself.

What are the requirements for the main home exclusion from the 2-year bright-line test?

21. If you acquire residential land and sell it (or otherwise dispose of it) within two years of when you are treated as acquiring it, any gains may be taxed under the 2-year bright-line test (s CB 6A). This test can only apply if none of ss CB 6 to CB 12 apply.
22. There are special rules about when you are treated as acquiring the land for the 2-year bright-line test, which differ from when you are treated as acquiring the land for the other land sale rules. In a typical land purchase situation, the 2-year period for the bright-line test will start when the land title is registered to you.
23. Your main home may be excluded from the 2-year bright-line test. To qualify for that exclusion (which is in s CB 16A) you have to meet **all** of the following requirements:
 - The land has been used predominantly, for most of the time you owned it, for a dwelling that was your main home.⁴
 - You have not already used the main home exclusion twice within the two **years immediately before the "bright-line date"**⁵ for the land in question.
 - You have not engaged in a regular pattern of acquiring and disposing of residential land that had your main home on it (discussed from [31]).
24. If you have a "**regular pattern**" of acquiring and disposing of residential land that had your main home on it, you will still be taxed on the proceeds of the sale of the land even if you have not already used the main home exclusion twice in the two years **before the "bright-line date"**.
25. The "**regular pattern**" has to be of **acquiring and disposing of residential land that had your main home on it** (see further from [27]). It does not matter if you have a regular pattern of acquiring and disposing of other land, such as farmland, land that a dwelling cannot be built on under the relevant district plan (eg, industrial land), or residential land that you did not live on.
26. The 2-year bright-line test can only potentially apply to a disposal of land if you first acquired an estate or interest in the land on or after 1 October 2015. However, if the first interest in the land was acquired on or after 1 October 2015, you must take into account acquisitions and disposals before that date in deciding **whether you have a "regular pattern" of acquiring and disposing of residential land that had your main home on it.**

Requirement that the regular pattern relates to land that you occupied mainly as a residence, or that had your main home on it

27. As noted above, for a "**regular pattern**" to prevent the relevant exclusion from applying, it has to be a regular pattern of acquiring and disposing of land that you occupied **mainly as a residence** (in the case of the land sale rules that the exclusion in s CB 16 is relevant to), or that had your **main home** on it (in the case of the 2-year bright-line test).
28. While the legislation does not expressly state that the regular pattern has to be of acquiring and disposing of land that you occupied mainly as a residence, or that

⁴ Note, if you are a trustee of a trust, the exclusion can apply if the dwelling was the main home of a beneficiary of the trust. This is as long as a principal settlor of the trust does not have a main home or, if they do, it is the property you are disposing of.

⁵ In a typical land sale situation, this will be the date that you enter into an agreement for the disposal of the land. But your "**bright-line date**" could be a different date, depending on how you dispose of the land (see s CB 6A(7)).

had your main home on it, the Commissioner considers this is the correct interpretation.

29. In terms of the s CB 16 exclusion, the Commissioner considers this interpretation to be correct because of the way the legislation was worded before the Act was re-written for simplicity. There was no intention to narrow the scope of the exclusion when the Act was re-written. It is also supported by the fact that if the pattern did not need to relate to land that you occupied mainly as a residence, people who are in the business of dealing in land would likely not be able to use the exclusion in s CB 16. However, it was clearly intended that they could, because s CB 16 is an exclusion from all of ss CB 6 to CB 11, including the dealer, builder and developer provisions.
30. Similarly, the Commissioner considers that the regular pattern has to be of acquiring and disposing of land that had your main home on it for you to be prevented from using the main home exclusion from the 2-year bright-line test. This is because the wording of the main home exclusion was based on the wording of the residential exclusion in s CB 16, and because of what the context of the land provisions as a whole and the ordering of the different land sale rules suggest about how the provisions are intended to operate. It is also supported by comments in the special report *Bright-line Test for Residential Land* (Inland Revenue, Wellington, 2015).

So what is a “regular pattern” of acquiring and disposing or building and disposing?

31. The High Court and the Taxation Review Authority have considered a number of cases that required looking at **whether there was a “regular pattern” of acquiring and disposing of houses or building and disposing of houses**, which would mean the residential exclusion in s CB 16 could not be used. The same principles are **relevant when considering whether there has been a “regular pattern” of acquiring and disposing of residential land for the purposes of the main home exclusion from the 2-year bright-line test.**
32. In *Parry v CIR* (1984) 6 NZTC 61,820 (HC), the High Court made the following **comments about the meaning of “regular pattern” in what is now s CB 16** (at 61,824):

I commence with the phrase “a regular pattern of such transactions”. In my view, in the context in which it is used, “pattern” denotes a similarity or likeness in the transactions. The transactions relied on must bear a similarity or likeness each to the others.

In the same context the word “regular” is used in the sense of recurring at uniform or near uniform intervals. There must therefore be a sufficient degree of uniformity or at least consistency of occurrence.

So in considering whether there has been a regular pattern of erecting dwellinghouses and subsequent sale, the Court must consider each transaction to assess the degree of similarity each to the others. This involves considering factors such as the type and location of the sections, the type of the dwellinghouses, the method of erection, the use to which the dwellinghouses were put and, in particular, whether occupied by the objector, and any other characteristics of the transaction that may be relevant in assessing similarity. The Court must also consider the number of transactions and the intervals of time between each, thereby assessing the degree of uniformity or consistency of occurrence. In the end it will have to determine as a matter of fact and degree whether the events that occurred demonstrate a regular pattern of such transactions.

On this approach it does not seem to me to be relevant to consider the reason or purpose for each transaction. It is the similarity of the transactions that is significant, not any similarity in the reason, purpose or intention for entering into each transaction.

33. The court also noted that the regular pattern has to exist independently of and before the transaction in question.

34. In deciding whether **there is a "regular pattern"** for the purposes of the residential exclusion in s CB 16, the key things to bear in mind are:

- **For there to be a "pattern"**, there has to be a similarity or likeness between the transactions.
- The reason or purpose for each transaction is irrelevant; it is the similarity of the transactions that is important.
- Assessing the similarity between the transactions involves considering factors such as the type and location of each of the sections of land, the type of dwellinghouses, the method of erection, the use to which the dwellinghouses were put (in particular whether you occupied them),⁶ and any other relevant characteristics of the transactions.
- For a pattern to be established, there must be more than one transaction. The greater the number of similar transactions, the more likely there is a pattern.
- **For a pattern to be "regular"**, the transactions must occur at sufficiently uniform or consistent intervals.
- The number of similar transactions and the intervals of time between them must be assessed, and it is a matter of fact and degree whether there is a regular pattern of such transactions.
- There must be at least two similar transactions for there to potentially be a regular pattern (**Case C9** (1977) 3 NZTC 60,058). But the Commissioner accepts that generally at least three prior transactions would be needed for there to be a regular pattern.
- You must have engaged in a regular pattern of the relevant type of transactions independently of and before the transaction in question. The transaction being considered as potentially subject to tax is not taken into account in deciding whether there is a regular pattern of transactions.

(See also **Case 5/2013** [2013] NZTRA 05 (2013) 26 NZTC 2,004, **Case M102** and **Case C9**.)

35. As noted above, **the type of "regular pattern"** that will mean you cannot use the exclusion for your house is:

in the case of any of the land sale rules in ss CB 6 to CB 11:

- a **"regular pattern" of acquiring and disposing of houses** that you occupied mainly as residences; or
- a **"regular pattern" of building and disposing of houses** that you occupied mainly as residences; and

in the case of the 2-year bright-line test (s CB 6A):

- a **"regular pattern" of acquiring and disposing of residential land** that had your main home on it.

36. If you have any other pattern involving acquiring or disposing of land, it will not prevent you from relying on the exclusion for your house. For example, if you have a pattern of speculative buying and selling of land you have not lived on, or if, as part of your business, you buy and sell land you have not lived on.

⁶ As discussed from [27], the regular pattern has to be of acquiring and disposing of land that you occupied mainly as a residence, or that had your main home on it. As such, whether, and the extent to which, you occupied any particular property is important in terms of the relevance of that transaction to deciding whether you have a regular pattern.

Is it true that I can renovate and sell a house every year or two and not be taxed, as long as I lived in the house?

37. A common misconception is that you can renovate and sell a house every year or two and not be taxed on the sale proceeds, as long as you lived in the house. This is not true. Whether you are taxed on the sale proceeds of a house you have lived in depends on whether there is a taxing provision you might be caught by (these are listed at [11]), and then whether you meet the requirements for an exclusion from that provision.
38. As noted above, the exclusions for a person's house **cannot be used** if you have:
- a **"regular pattern" of acquiring and disposing** or building and disposing of houses that you occupied mainly as residences (in the case of the provisions in ss CB 6 to CB 11 – which include the purpose or intention provision, and the dealer, developer, subdivider and builder provisions); or
 - a **"regular pattern" of acquiring and disposing of residential land** that had your main home on it (in the case of the 2-year bright-line test (s CB 6A)).
39. If you renovated and sold your house every year, you would establish a regular pattern that would prevent you from being able to use the residential exclusion from ss CB 6 to CB 11 or the main home exclusion from the 2-year bright-line test.
40. Note that even if you do not have a regular pattern of acquiring and disposing of residential land that had your main home on it, you would not be able to use the main home exclusion from the 2-year bright-line test if you had already used it twice in the two years before **the "bright-line date"** for land you are selling.
41. If you renovated and sold houses that you lived in less frequently, for example every two or more years, you would at some stage establish a regular pattern. If one of the land sale rules in ss CB 6 to CB 11 was potentially applicable (for example, if you purchased the land with a purpose or an intention of disposing of it, or if you or someone you are associated with is a land dealer, developer, subdivider or builder), your regular pattern may mean that you cannot use the residential exclusion and might be taxed on the sale of a house you lived in.
42. You could also potentially be taxed under one of the undertaking or scheme provisions (s CB 12 in particular) if your renovations involved more than minor development or division work. As noted above, the undertaking or scheme provisions have their own separate residential exclusion, which does not have a requirement that there is no **"regular pattern"** involving the disposal of land. But there are a number of requirements that must be met for you to be able to use that exclusion, so you would need to consider whether those requirements were met.
43. Even if you sell a property that you live in without renovating it, one of the land sale rules could apply to you, so you may need to consider whether you have a regular pattern involving disposal of property that you lived in.
44. There is no hard and fast rule about the number of times or how frequently you can buy and sell, build and sell, or renovate and sell houses and not be taxed.

What if I have to sell a number of houses because of circumstances outside my control?

45. The reason or purpose for buying and selling or building and selling is irrelevant in deciding **whether you have a "regular pattern" of transactions** – even if the reason or purpose for the sale is outside your control. What matters is whether you have engaged in a regular pattern of transactions of the relevant type.
46. If you sold one or two houses that you lived in, you would not be taxed on the sale proceeds (as long as you meet the other criteria for the residential exclusion or the main home exclusion), as you **would not have a "regular pattern" involving disposal** at that point. If you sold more than that, for whatever reason, there may be a question of whether you have a regular pattern. As noted above, this would involve considering the number of similar transactions and the intervals of time between them. Generally, at least three prior transactions would be needed for there to be a regular pattern.

If I cannot use the residential exclusion or the main home exclusion and have to pay tax on a land sale, can I get any tax deductions?

47. Yes. If one of the land sale rules applies to tax you on the proceeds of selling land, you will get a deduction for the cost of the land and any capital improvements you make to it, to the extent that those costs are incurred in deriving the income and are not private in nature (ss DB 23, DA 1 and DA 2(2)). The deduction is taken in the income year in which you dispose of the land (see s EA 2).
48. You may also be able to deduct other expenditure, such as interest on money borrowed to purchase the land, insurance premiums, and the cost of repairs and maintenance. Deductions for these expenses will be allowed to the extent that they are incurred in deriving the income and are not private in nature (ss DA 1, DA 2 and DB 6).

Examples

49. The following examples are included to assist in explaining the application of the law. **The focus of the examples is on the "regular pattern" aspect** of both the residential exclusion from ss CB 6 to CB 11 and the main home exclusion from s CB 6A. The examples are therefore premised on the other criteria for the relevant exclusion being satisfied. The examples are also premised on the relevant taxing provision being applicable, subject to the potential availability of the residential exclusion or the main home exclusion.

Example 1 – A “regular pattern” of transactions established

50. Melody and David are keen house renovators and have purchased a number of properties to improve and sell at a profit. These purchases and sales are shown in the following table.

Property	Date acquired	Land / activity	Date sold
1 (N Road)	June 2006	Cottage in inner-city Wellington suburb purchased. Renovations undertaken over the period of ownership, while Melody and David lived in the house.	May 2008
2 (P Street)	May 2008	Bungalow in Wellington suburb purchased. Renovations and landscaping undertaken over the period of ownership, while Melody and David lived in the house.	July 2010
3 (E Place)	July 2010	House in Wellington suburb purchased. Off-street parking built during the period of ownership, while Melody and David lived in the house.	February 2011
4 (J Avenue)	January 2011	Larger family home in Wellington suburb purchased, as Melody and David had started a family. Some minor redecorating undertaken during the period of ownership, while Melody and David lived in the house.	March 2013

51. Melody and David purchased the properties for a purpose and with an intention of selling them after they had completed some improvements. Their aim was to renovate the properties while they lived in them and sell them at a profit, enabling them to move up the property ladder. As such, the proceeds from the sales may be subject to tax under s CB 6 – the purpose or intention provision. This depends on whether Melody and David can rely on the residential exclusion in s CB 16.
52. Melody and David acquired the properties with houses on them, and it is assumed that they occupied the houses mainly as their residences. It is also assumed that the area of each property was 4,500 square metres or less. Therefore, the only issue is whether Melody and David are precluded from using the residential exclusion, which they will be if they have engaged in a regular pattern of acquiring and disposing of houses that they occupied mainly as residences.
53. When the first three properties (N Road, P Street and E Place) were sold, Melody and David did not yet have a regular pattern of acquiring and disposing of houses. A regular pattern has to exist independently of the transaction being considered. By the time E Place was sold, there had only been two prior acquisitions and sales. The Commissioner accepts that generally at least three transactions would be needed for there to be a regular pattern.
54. By the time the J Avenue property was sold, Melody and David had previously acquired and disposed of three houses that they had lived in. The question is whether those three transactions amount to a regular pattern of acquiring and disposing of houses that were occupied by the couple mainly as residences. If

they do amount to such a regular pattern, Melody and David will not be able to rely on the residential exclusion for the sale of the J Avenue property.

55. For there to be a pattern, there has to be a similarity or likeness between the transactions. In this case, there is. The N Road, P Street and E Place properties were all residential properties in Wellington acquired, occupied, renovated and sold by Melody and David. It does not matter that the nature of the renovations done to each property was different. The pattern only needs to involve acquiring and disposing of houses that have been occupied mainly as residences.
56. For a pattern of acquisition and disposal to be regular, the transactions need to occur at sufficiently uniform or consistent intervals. In this case, the properties were held for 1 year 11 months, 2 years 2 months, and 7 months, respectively. Three properties were acquired and disposed of in a period of 4 years 8 months. The Commissioner considers that the intervals between the transactions are consistent enough for this to be a regular pattern. The intervals between the transactions do not need to be identical.
57. Because Melody and David have engaged in a regular pattern of acquiring and disposing of houses that they occupied mainly as residences, they cannot use the residential exclusion in s CB 16. Therefore, the proceeds from the sale of the J Avenue property will be income to Melody and David under s CB 6. Melody and David can deduct the costs of the property and the redecorating, to the extent that those costs are not private in nature.
58. The 2-year bright-line test does not apply to the sales of the N Road, P Street or E Place properties, because they were all acquired before 1 October 2015 (and in the case of the P Street property, the land was held for over two years, in any event).

Example 2 – A “pattern” of transactions, but not a “regular pattern”

59. Enzo, who is in the business of dealing in land, has purchased and sold dozens of residential properties over the last decade as part of his business. In that time, he has also sold four properties that he lived in, as shown in the following table.

Property	Date acquired	Land / activity	Date sold
1 (Q Street)	February 2006	Apartment in Auckland CBD purchased. Lived in by Enzo, and then subsequently by his partner too.	June 2007
2 (M Place)	July 2007	House on the North Shore purchased, as Enzo and his partner decided to adopt a child. Lived in by the family for the period of ownership.	December 2012
3 (G Road)	December 2012	Larger house in Auckland purchased to accommodate the expanding family. Lived in by the family for the period of ownership.	October 2015
4 (T Road)	October 2015	House on a small lifestyle property outside of Hamilton purchased. Lived in by the family until early January 2016, when Enzo’s partner accepted an exciting job offer in Sydney and the family decided to move there. The sale of the house was settled at the end of January 2016.	January 2016

60. Because Enzo is in the business of dealing in land and all of the above properties were sold within 10 years of being acquired, Enzo (and his partner, where relevant) may be taxed on the proceeds of the sales under s CB 9. However, this depends on whether Enzo and his partner can rely on the residential exclusion in s CB 16.
61. Enzo (and his partner, where relevant) acquired the properties with houses on them, and it is assumed that they occupied the houses mainly as their residences. It is also assumed that the area of each property was 4,500 square metres or less. Therefore, the only issue is whether Enzo and his partner are precluded from using the residential exclusion, which they will be if they have engaged in a regular pattern of acquiring and disposing of houses that they occupied mainly as residences.
62. The numerous residential properties Enzo has purchased and sold as part of his business are not relevant to deciding whether there is a regular pattern of the type that would prevent Enzo and his partner from relying on the residential exclusion.
63. When the first three properties (Q Street, M Place and G Road) were sold, Enzo and his partner did not yet have a regular pattern of acquiring and disposing of houses that they occupied mainly as residences. A regular pattern has to exist independently of the transaction being considered. By the time the G Road property was sold, there had only been two prior acquisitions and sales. The Commissioner accepts that generally at least three transactions would be needed for there to be a regular pattern.

64. By the time the T Road property was sold, Enzo (and his partner, where relevant) had previously acquired and disposed of three houses that they lived in. The question is whether those three transactions amount to a regular pattern of acquiring and disposing of houses that were occupied by the couple mainly as residences. If they do amount to such a regular pattern, Enzo and his partner will not be able to rely on the residential exclusion for the sale of the T Road property.
65. For there to be a **pattern**, there has to be a similarity or likeness between the transactions. In this case, there is. The Q Street, M Place and G Road properties were all residential properties in Auckland acquired, occupied, and sold by Enzo and his partner.
66. For a pattern of acquisition and disposal to be **regular**, the transactions need to occur at sufficiently uniform or consistent intervals. In this case, the properties were held for 1 year 4 months, 5 years 5 months, and 2 years 10 months, respectively. Three properties were acquired and disposed of in a period of 9 years 8 months. The Commissioner considers that the intervals between the transactions are not consistent enough for this to be a regular pattern.
67. Because Enzo and his partner have not engaged in a **regular pattern** of acquiring and disposing of houses that they occupied mainly as residences, they can use the residential exclusion in s CB 16. As noted at [61], it is assumed that the other requirements for the exclusion are met. Enzo and his partner will, therefore, not be taxed under s CB 9 on the proceeds of the sale of the T Road property.
68. However, the T Road property was acquired on or after 1 October 2015, sold **within two years, and is "residential land" for the purposes of the 2-year bright-line test**. This is because it has a dwelling on it, and it is not used predominantly as business premises and is not farmland. (It is not "farmland" as defined in the Act because, due to its size, it is not capable of being worked as a farming or agricultural business.) As such, it is also necessary to consider whether the proceeds of the sale of the T Road property are taxed under the 2-year bright-line test. This comes down to whether Enzo and his partner can rely on the main home exclusion in s CB 16A.
69. Enzo and his partner used the house on the T Road property predominantly, for most of the time they owned it, as their main home. Therefore, the only issue is whether Enzo and his partner are precluded from using the main home exclusion, which they will be if they have either:
- already used the main home exclusion twice within the two years **immediately before the "bright-line date"**⁷ for the T Road property, or
 - engaged in a regular pattern of acquiring and disposing of residential land that had their main home on it.
70. Enzo and his partner have not used the main home exclusion at all before, so they will only be precluded from using the main home exclusion if they have engaged in a regular pattern of acquiring and disposing of land that was their main home.
71. As with the residential exclusion from the land dealer provision, the numerous properties Enzo has purchased and sold as part of his business are not relevant to deciding whether there is a regular pattern of the type that would prevent Enzo and his partner from relying on the main home exclusion from the 2-year bright-line test.

⁷ In this case, the date that Enzo and his partner entered into the contract to sell the T Road property.

72. Therefore, the only transactions that are relevant are the purchases and sales of the Q Street, M Place and G Road properties. Although the 2-year bright-line test only potentially applies to disposals of land acquired on or after 1 October 2015, acquisitions and disposals of residential land before then are relevant in deciding whether **there is a "regular pattern" that means the main home exclusion cannot be used.**
73. As with the residential exclusion from the land dealer provision, the Commissioner considers that the acquisitions and sales of the Q Street, M Place and G Road properties do not make up a regular pattern.
74. Because Enzo and his partner have not used the main home exclusion before and have not engaged in a regular pattern of acquiring and disposing of residential land that had their main home on it, they can use the exclusion when they sell the T Road property. Therefore, Enzo and his partner will not be taxed on the proceeds of the sale of the T Road property under the 2-year bright-line test (s CB 6A).

Example 3 – Transactions not similar enough to be a “pattern”

75. Hemi and Kirrily have acquired and sold a number of properties since they married five years ago, as shown in the following table.

Property	Date acquired	Land / activity	Date sold
1 (C Road)	May 2011	Investment property purchased before Hemi and Kirrily went overseas on their “OE”, so they could get a foot on the property ladder. Property rented out from when purchased until when sold.	November 2013
2 (A Street)	November 2013	House purchased upon Hemi and Kirrily’s return to NZ and the sale of their investment property. Lived in for the period of ownership.	October 2015
3 (H Street)	September 2015	Inherited Kirrily’s father’s unit upon his death. Listed for sale soon after, and never lived in by the couple.	October 2015
4 (K Avenue)	November 2015	When Kirrily and Hemi inherited the H Street property, they decided to sell it and the A Street property and buy a larger house (the K Avenue property) and a holiday bach (the B Esplanade property). The K Avenue property was lived in by the couple for the period of ownership.	February 2016
5 (B Esplanade)	November 2015	Seaside bach purchased with the proceeds of the A Street and H Street properties. The couple stayed in the bach most weekends during the period of ownership. The bach (the B Esplanade property) and the K Avenue property were both sold when Kirrily was diagnosed with a life-threatening illness, and the couple decided to use their equity to fund experimental medical treatment in Germany.	February 2016

76. The C Road, A Street and H Street properties are not potentially subject to tax under any of the land provisions in the Act.
77. However, the K Avenue and B Esplanade properties were both acquired after 1 October 2015, sold within two years, and are both “residential land” for the purposes of the 2-year bright-line test. This is because those properties both have dwellings on them, are not used predominantly as business premises, and are not farmland. As such, it is necessary to consider whether the proceeds of the sales of the K Avenue and B Esplanade properties are taxed under the 2-year bright-line test. This comes down to whether Hemi and Kirrily can rely on the main home exclusion in s CB 16A.

78. Hemi and Kirrily used the K Avenue property predominantly, for most of the time they owned it, as their main home. Therefore, the only issue is whether Hemi and Kirrily are precluded from using the main home exclusion, which they will be if they have either:
- already used the main home exclusion twice within the two years **immediately before the "bright-line date"**⁸ for the K Avenue property; or
 - engaged in a regular pattern of acquiring and disposing of residential land that had their main home on it.
79. Hemi and Kirrily have not used the main home exclusion at all before, so they will only be precluded from using the main home exclusion for the sale of the K Avenue property if they have engaged in a regular pattern of acquiring and disposing of land that was their main home.
80. By the time the K Avenue property was sold, Hemi and Kirrily had previously acquired and disposed of three residential properties – the C Road, A Street and H Street properties. The question is whether those three transactions amount to a regular pattern of acquiring and disposing of houses that were occupied by the couple mainly as residences. In this case, they clearly do not. This is because, for there to be a pattern, there has to be a similarity or likeness between the transactions. That is not the case here. The C Road, A Street and H Street properties were all residential properties, but one (the C Road property) was an investment property, one (the H Street property) was inherited by the couple, and one (the A Street property) was their home. The acquisitions and sales of those properties are not **sufficiently similar to amount to a "pattern"**.
81. Because Hemi and Kirrily have not used the main home exclusion before and have not engaged in a regular pattern of acquiring and disposing of residential land that had their main home on it, they could use the exclusion when they sold the K Avenue property. Therefore, Hemi and Kirrily were not taxed on the proceeds of the sale of the K Avenue property under the 2-year bright-line test (s CB 6A).
82. However, Hemi and Kirrily did not use the house on the B Esplanade property as their main home. Therefore, they could not use the main home exclusion when they sold that property, and the proceeds of the sale of the property were income to them under the 2-year bright-line test (s CB 6A). Hemi and Kirrily could deduct the cost of the B Esplanade property and any other expenditure that was incurred in deriving the income, to the extent that those costs were not private in nature.

⁸ In this case, the date that Hemi and Kirrily entered into the contract to sell the K Avenue property.

References

Subject references

Income tax, sale of land, main home exclusion, residential exclusion, regular pattern involving disposal

Legislative references

Income Tax Act 2007 – ss CB 6A, CB 6, CB 7, CB 9, CB 10, CB 11, CB 12, CB 13, CB 16A, CB 16, CB 17, DA 1, DA 2(2), DB 6, DB 7, DB 23 and EA 2

Case references

Case 5/2013 [2013] NZTRA 05, 26 NZTC 2,004
Case C9 (1977) 3 NZTC 60,058
Case G76 (1985) 7 NZTC 1,348
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Other references

Bright-line Test for Residential Land (Inland Revenue, Wellington, 2015)