

QUESTIONS WE'VE BEEN ASKED

Do certain supplies wholly or partly consist of land for the compulsory zero-rating (CZR) rules?

Issued: 16 December 2020

Publication number QB 20/04

This Question We've Been Asked is a follow-up to Interpretation Statement: IS 17/08 and provides guidance on the meaning of land for the CZR rules.

Key provisions

Section 11(1)(mb) of the Goods and Services Tax Act 1985 requires a supply that wholly or partly consists of **land** (and which satisfies certain other requirements) to be zero-rated for GST purposes.

The definition of **land** in s 2 includes an estate or interest in land and a right that gives rise to an interest in land.

RELATED TO: IS 17/08

Question

Do the following supplies wholly or partly consist of land for the compulsory zero-rating (CZR) rules:

- the sale of transferable development rights?
- the sale by way of assignment of a purchaser's interest in a sale and purchase agreement for land?
- the grant of an easement?

Answer

Supplies that wholly or partly consist of land for the CZR rules include:

- the sale by way of assignment of a purchaser's interest in a sale and purchase agreement for land where that agreement gives rise to an equitable interest in land; and
- the grant of an easement.

Supplies that do not wholly or partly consist of land for the CZR rules are:

- the sale of transferable development rights;
- the sale by way of assignment of a purchaser's interest in a sale and purchase agreement for land where that agreement does not give rise to an equitable interest in land.

Key terms

Transferable development rights are created by various district councils throughout New Zealand. They are a market-based mechanism that encourages the voluntary transfer of development potential from locations where a council supports restrictions on land use to places where a council would like to see development enabled.

Equitable interest in a sale and purchase agreement for land (for this QWBA) means that the purchaser can obtain relief by way of specific performance or injunction.

Easement is an interest in land that is essentially a right to use the land of another person in a particular way, or a right which prevents a landowner from using their land in a particular way.

Explanation

1. All legislative references are to the Goods and Services Tax Act 1985 (GST Act), unless otherwise stated.
2. This Question We've Been Asked follows up "Interpretation Statement: IS 17/08 – Goods and services tax – Compulsory zero-rating of land rules (general application)".

What land is for compulsory zero-rating purposes

3. A supply that wholly or partly consists of land (and that satisfies certain other requirements) must be zero-rated for GST purposes under s 11(1)(mb).
4. Section 11(1)(mb) is intended to prevent "phoenix" fraud schemes. These schemes involve Inland Revenue refunding GST to a purchaser of land with no corresponding payments being made by the vendor because the supplying company deliberately winds up before making payment (Commentary on the Taxation (GST and Remedial Matters) Bill 2010, Policy Advice, Inland Revenue, August 2010).
5. Section 2 provides:

land, in the zero-rating of land rules,—

 - (a) includes—
 - (i) an estate or interest in land:
 - (ii) a right that gives rise to an interest in land:
 - ...
6. A wide definition of land was included in the CZR rules to ensure broad application of the CZR rules and to prevent avoidance opportunities.

Estate or interest in land

7. The GST Act does not define the words estate, interest and interest in land. Accordingly, for the CZR rules, those words take their ordinary meaning.

8. An estate is an interest or “bundle of rights” in land. An interest in land includes both legal and equitable estates. Estates and interests in land vary from fee simple, the largest estate in land, to smaller estates and interests such as rent charges. The estates and interests most relevant to this QWBA are:
- equitable estates or interests; and
 - easements.

Right that gives rise to an interest in land

9. In addition, the definition of land in the GST Act includes “a right that gives rise to an interest in land”. This element is not present in the definition of land under the Income Tax Act 2007 (s YA 1).
10. Paragraph (a)(ii) of the definition of land in the GST Act contains the following elements:
- a right;
 - that gives rise to;
 - an interest in land.
11. The first two elements are considered next. Interest in land was discussed in [8].

A right

12. A right is a legal entitlement to have or do something (*Concise Oxford English Dictionary*, 12th ed, Oxford University Press, 2011).

Gives rise to

13. If something gives rise to an event or situation, it causes that event or situation to happen (*Concise Oxford English Dictionary*).
14. However, the extent of the causative link between the right and the interest in land is not clear from the ordinary meaning of the words used in the definition of land. In keeping with the policy intent of preventing avoidance opportunities, the phrase should be interpreted broadly, although there will be a point where the causative link is too remote.

Do the specified supplies wholly or partly consist of land?

Sale of transferable development rights

15. Transferable development rights (TDRs) are not defined in the GST Act, Income Tax Act 2007 or Resource Management Act 1991.
16. TDRs are created by various district councils throughout New Zealand. The rules governing such rights are contained in each council's district plan. The specific rights granted differ between districts depending on the council's objectives and may be described differently, for example, transferable rural lot, transferable title right, and transferable subdivision entitlements.
17. TDRs are a market-based mechanism that encourages the voluntary transfer of development potential from locations where a council supports restrictions on land use (referred to as donor areas) to places where a council would like to see development enabled (referred to as receiving areas).
18. Donor areas may be environmentally sensitive properties, open space, wildlife habitats, historic landmarks, or any other places that have value to a community (but that are typically not a market commodity). Receiving areas are considered appropriate for extra development due to their proximity to jobs, shops, schools, transport, and other urban services.
19. Some TDRs arise from the amalgamation of existing titles, the donor property landowner covenanting not to subdivide a lot that meets the requirements for subdivision, or the setting aside of land for conservation purposes.
20. The following analysis considers whether TDRs fall within the definition of land for CZR purposes.

Whether a transferable development right is an estate or interest in land

21. A TDR is merely a right that entitles the owner of a receiving site to obtain subdivision consent. It is not an estate or interest in land (whether it is a right that gives rise to an interest in land is considered from [24]). While the subdivision itself will give rise to an interest in land (that is, the owner's interest in the newly subdivided section), the TDR relates only to the consent process.
22. Case law on TDRs is sparse. However, TDRs are referred to in the Land Valuation Tribunal decision in *Taheke Paengaroa Trust v Western Bay of Plenty District Council*

(LVP 2/2005, 26 February 2008). The tribunal in that case considered the affairs of a trust that had land covered in native vegetation that met the council's specific criteria for designation and preservation in a natural state. In relation to the nature of TDRs, the tribunal said:

- no estate or interest in land was being transferred on the sale of TDRs;
- TDRs are purely a creature of the Resource Management Act 1991; and
- as consents, TDRs are not an estate or interest in land.

23. For completeness, s 122 of the Resource Management Act 1991 specifies that a resource consent is neither real nor personal property. While a TDR forms part of the process in applying for a resource consent, it is not a resource consent in itself. It is a right that enables the owner of a receiving site to obtain subdivision consent. Accordingly, s 122 of the Resource Management Act 1991 does not assist in determining whether a TDR is an estate or interest in land.

Whether a transferable development right is a right that gives rise to an interest in land

24. Based on analysis of various district plans it appears that a TDR is a form of right that the owner of donor land can generate that enables the owner of a receiving site to obtain subdivision consent. It seems likely that legal action could be taken against a district council that refused to grant subdivision consent where a TDR complies with the requirements of the relevant district plan.
25. Further, the exercise of the rights conferred by the TDR may ultimately give rise to an interest in land, being the receiving owner's estate in the newly subdivided section (notwithstanding that the owner already owns the undivided land).
26. The issue, as it relates to TDRs, is whether a sufficient causative link exists between the right and the interest in land. As already noted, in keeping with the policy intent of preventing avoidance opportunities, the phrase should be interpreted broadly, but there will be a point where the causative link is too remote.
27. The generation and transfer of a TDR is a step in the process that enables the creation of the newly subdivided section at the receiver site (an interest in land). However, there is insufficient causative link between the creation and transfer of the TDR and the newly subdivided land to conclude that the TDR "gives rise to" that interest in land.
28. A TDR merely enables a landowner to subdivide in circumstances where they would not otherwise be able to – ie, the TDR merely removes a restriction under a regulatory

regime. While a TDR may allow the receiver site to be subdivided, it does not cause the receiver site to be subdivided, nor does it require any subdivision to proceed. It follows that the TDR merely puts the owner of the receiver site in a position to be able to subdivide the land and, therefore, is one step too far removed from being a right that gives rise to an interest in land.

Conclusion

29. A TDR is neither an estate or interest in land, nor a right that gives rise to an interest in land. Accordingly, the CZR rules will not apply to the supply of a TDR. This is illustrated in example 1.

Example 1: Transferable development right

James is GST-registered and owns farmland in a coastal area as part of his taxable activity. Along the shoreline is a large wetland area that has become a significant wildlife habitat. James hears about transferable development rights (TDRs) when reading a newspaper article. He approaches his local council to ask whether he could generate a TDR in exchange for agreeing to fence off the wetland area and not use it for general farming purposes. The council agrees.

Martyn (who is also GST-registered) is a property developer whose niche market is in lifestyle blocks. The local council has minimum size restrictions on the sections that Martyn is developing but they are in an identified receiver zone for TDRs. James is aware of Martyn's development and approaches Martyn to see whether he would be interested in purchasing the TDR. If Martyn purchases the TDR from James he will be able to subdivide his current development into more lots than would otherwise be the case.

Martyn and James reach an agreement, and Martyn purchases the TDR from James for \$30,000. This is a supply that must be standard-rated under s 8(1) because the TDR is not an estate or interest in land, nor does it give rise to an interest in land. The TDR merely puts Martyn in a position to be able to subdivide his land and, therefore, is one step too far removed from being a right that gives rise to an interest in land.

Assignment of a purchaser's interest in a sale and purchase agreement (SPA) for land

30. A purchaser who has entered into a SPA for land may wish to sell their rights or interests under that SPA for land to a third person. This could be done by way of an assignment of the purchaser's contractual rights.¹ A question that arises is whether a sale by way of assignment of a purchaser's interest in a SPA for land is a supply that the CZR rules could apply to.
31. A purchaser's interest in a SPA for land will be "land" for the CZR rules if it is an equitable interest in land or a right that gives rise to an interest in land.
32. A purchaser's interest in a SPA for land will give rise to an equitable interest in the land when equitable remedies are available to protect the purchaser's rights under the contract, even if specific performance in the strict sense (that is, for the transfer of title) would not yet be available (*Foreman v Hazard* [1984] 1 NZLR 586 (CA); *Bevin v Smith* [1994] 3 NZLR 648 (CA); *McDonald v Isaac Construction Co Ltd* [1995] 3 NZLR 612 (HC)). This will be the case where a SPA for land is unconditional. It will also be the case where the conditions in a conditional SPA for land do not prevent there being a binding contract.
33. There is further discussion in [QB 17/02: Income tax – date of acquisition of land, and start date for 2-year bright-line test](#) on when a person has an equitable interest in a SPA for land. While QB 17/02 concerns income tax, the same issue of whether there is an equitable interest in land arises for GST purposes, and the same considerations are relevant.
34. As stated in QB 17/02, the most common conditions in SPAs for land (such as finance, a building report or LIM conditions) would not prevent there being a binding contract. But sometimes conditions will mean that there is not yet a binding contract, so it is necessary to consider the terms of the particular SPA for land to determine whether there is an equitable interest in the land that the original purchaser has passed to the buyer (see, for example, *Fletcher Challenge Energy Ltd v Electricity Corporation of New*

¹ It may be that a document that is described as a nomination in fact amounts to an assignment of the contractual rights. For more details see [QB 17/02: Income tax – date of acquisition of land, and start date for 2-year bright-line test](#) at [52].

Zealand Ltd [2002] 2 NZLR 433 (CA); *Willetts v Ryan* [1968] NZLR 863 (CA); *Barrett v IBC International Ltd* [1995] 3 NZLR 170 (CA)).

35. Where there is not yet a binding contract, the purchaser will not have an equitable interest in the land. Nor will they have a right that gives rise to an interest in land. Until there is a binding contract, the purchaser has no enforceable rights.
36. The application of the CZR rules is assessed at the time of settlement of the relevant transaction relating to the supply (in this case, being the assignment of the purchaser's interest in the SPA, not the underlying sale of the land) under s 11(8B).

Summary

37. In summary, a purchaser's interest in a SPA for land will be "land" for the CZR rules where the SPA gives rise to an equitable interest in land. Accordingly, where a person sells by way of assignment their interest in a SPA for land to another person, and the SPA is one which gives rise to an equitable interest in land, this will be the supply of land under the CZR rules. Such a supply may be subject to the CZR rules.
38. This is illustrated in example 2.

Example 2: Sale by way of assignment of a purchaser's interest in a SPA for land

James (from example 1) enters into an unconditional agreement to sell a portion of his farmland to Development Ltd. Development Ltd carries on a taxable activity of commercial property development and is acquiring the farmland to either develop or sell for profit, depending on the opportunities that arise.

TA Ltd carries on a taxable activity. It would like to purchase the farmland and build a workshop and retail shop to operate from. TA Ltd enters into an agreement with Development Ltd, under which it agrees to pay Development Ltd a fee to acquire by way of assignment Development Ltd's interest as purchaser of the land under the agreement it has entered into with James.

This transaction must be zero-rated under s 11(1)(mb) because it wholly or partly consists of land (assuming the other CZR requirements are satisfied).

Easements

39. An easement is an interest in land. A positive easement is essentially the right to use the land of another person in a particular way without any right to occupation of the land, or to take any part of the soil or its produce, or to prevent a landowner from using his or her land in a particular way. A negative easement is a right which does prevent a landowner from using his or her land in a particular way.²

Example 3: Easement over land

A lines company wants to put power lines across James's (from example 1) farmland. The lines company approaches James and offers to pay \$20,000 for the grant of an easement to enable them to install and maintain the lines.

If James grants the easement, the CZR rules will apply to the transaction because he will be granting the lines company an interest in land (assuming the other CZR requirements are satisfied).

References

Legislative References

Goods and Services Tax Act 1985, ss 2 ("land"), 5(1), 11(1)(mb), s 11(8B)

Income Tax Act 2007, s YA 1 ("land")

Resource Management Act 1991, s 122

² Hinde McMorland and Sim *Land Law in New Zealand* (online ed, LexisNexis, July 2020) at [16.002] and [16.009].

Case References

Barrett v IBC International Ltd [1995] 3 NZLR 170 (CA).

Bevin v Smith [1994] 3 NZLR 648 (CA).

Fletcher Challenge Energy Ltd v Electricity Corporation of New Zealand Ltd [2002] 2 NZLR 433 (CA).

Foreman v Hazard [1984] 1 NZLR 586 (CA).

McDonald v Isaac Construction Co Ltd [1995] 3 NZLR 612 (HC).

Taheke Paengaroa Trust v Western Bay of Plenty District Council (LVP 2/2005, 26 February 2008).

Willetts v Ryan [1968] NZLR 863 (CA).

Other References

Concise Oxford English Dictionary, 12th ed, Oxford University Press, 2011.

Dictionary of New Zealand Law, LexisNexis, originally published as the New Zealand Law Dictionary, 9th ed.

Hinde McMorland and Sim *Land Law in New Zealand* (online ed, LexisNexis, July 2020).

Interpretation Statement: IS 17/08 – *Goods and services tax – Compulsory zero-rating of land rules (general application)*.

QB 17/02: *Income tax – date of acquisition of land, and start date for 2-year bright-line test*.

Taxation (GST and Remedial Matters) Bill; Commentary on the Bill (Policy Advice, Inland Revenue, August 2010).

About this document

"Questions we've been asked" are issued by the Tax Counsel Office. They are published items about specific tax issues that set out the answers to enquiries we have received which may be of general interest to taxpayers. A general similarity to the items will not necessarily lead to the same tax result. Each case should be considered on its own facts.