

Note (not part of the Rulings):

These two public rulings, BR Pub 13/05 to BR Pub 13/06, deal with certain aspects of the income tax treatment of the standard form contract for public-private partnerships prepared by the Treasury. These two rulings do not consider the tax implications of any funding agreements or other contracts entered into by the parties. For example, these rulings do not address the potential application of the thin capitalisation rules in subpart FE, goods and services tax (GST), the financial arrangements rules or the general anti avoidance provision in s BG 1.

Any person entering into a public-private partnership with the New Zealand Government is strongly advised to apply for a private ruling and a financial arrangements rules determination in respect of its specific structure to provide certainty on issues that are not addressed in these rulings.

INCOME TAX – STANDARD PROJECT AGREEMENT FOR A PUBLIC–PRIVATE PARTNERSHIP - COMPANIES

PUBLIC RULING - BR Pub 13/05

This is a public ruling made under s 91D of the Tax Administration Act 1994.

Taxation Laws

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

This Ruling applies in respect of ss CB 1, CH 2, DA 1, DA 2, DB 50, EA 2 and EA 3.

The Arrangement to which this Ruling applies

The Arrangement is the design, construction, operation and maintenance of an asset (the Facility) by a company (the special purpose vehicle – SPV) under a public–private partnership agreement with Her Majesty, The Queen in Right of New Zealand acting by and through a government department (the Crown).

The Arrangement is governed by a standard form contract prepared by the Treasury (the Project Agreement). Key clauses of the Project Agreement and relevant definitions have been included in Appendix B to the Commentary of this Ruling. This Ruling will not apply if the clauses of the Project Agreement that are referred to in this Ruling are altered in a material way.

The Project Agreement has three main components:

- The **Design and Construction (D&C) Phase** involves the SPV providing design and construction supplies in return for a lump sum design and construction payment (the D&C Payment).
- The **Facility Lease** is the lease into which the SPV and the Crown enter and under which the SPV prepays an amount representing the rental the SPV will pay to the Crown (the Rental Prepayment).
- The **Operation and Maintenance (O&M) Phase** involves the SPV providing operational and maintenance services over a period of approximately 25 years in return for a regular payment (the Unitary Charge). The date on which the O&M Phase starts is referred to as the Service Commencement Date.

Each of the three components is summarised below. The Project Agreement details the rights and obligations of the SPV and the Crown.

Design and Construction Phase

During the D&C Phase, the SPV will design and construct the Facility in accordance with the Project Agreement on behalf of the Crown. The Facility consists of all of the structures that are to be designed, constructed, commissioned and maintained by the SPV in accordance with the terms of the Project Agreement, and includes the entire physical infrastructure, the grounds and all of the fixtures, fit-out, plant and equipment. The SPV will be solely responsible to the Crown for the design and construction of the Facility, including the provision of infrastructure, plant, equipment and other related obligations, to the standard required by the Project Agreement.

Throughout the term of the Project Agreement, the SPV will not own the Facility or the land on which the Facility will be built (the Crown Site) (cl 11.1). Under cl 11.2(a) of the Project Agreement, any Fixtures that the SPV supplies before the start of the Facility Lease (whether or not affixed to the land) (the Initial Fixtures) will remain the property, and in the ownership, of the SPV until the date of payment of the D&C Payment. For the purposes of the Project Agreement, Fixtures includes all buildings (including component parts of buildings), other structures, improvements, and roads. If the Crown fails to pay the D&C Payment in full when it is due, the SPV can exercise its ownership rights and remove the Initial Fixtures (cl 11.2(b)). The ownership of the Initial Fixtures retained by the SPV under cl 11.2(a) will be automatically transferred to the Crown on the date of payment of the D&C Payment (cl 11.2(c)).

The D&C Payment is a single, contractually fixed, lump sum that the Crown must pay to the SPV on the Service Commencement Date. The D&C Payment is paid to the SPV by the Crown in consideration for the completion of the Facility and the transfer of the ownership in the Initial Fixtures (cl 12.3). No milestone or progress payments are provided for under the Project Agreement.

The amount of the D&C Payment is determined by direct reference to the agreed design and construction costs of the Facility (excluding fit-out) together with the SPV's funding costs during the D&C Phase. Under cl 12.5(c), the Crown and the SPV agree that the D&C Payment includes capitalised interest to the extent that it exceeds the agreed design and construction costs of the Facility. The SPV does not apply a separate margin in respect of the D&C Phase. The D&C Payment is set off against the amount payable by the SPV as the Rental Prepayment for the Facility Lease, as described below.

To construct the Facility, the SPV will incur expenditure in connection with designing, obtaining, affixing, constructing and implementing the Initial Fixtures. Other than the costs of fit-out and any funding costs, the expenditure incurred by the SPV on the Facility during the D&C Phase is referred to in this Ruling as the D&C Expenditure.

Facility Lease

Clause 12.2 of the Project Agreement provides for the Crown and the SPV to enter into a lease in respect of the Facility on or before the date of operational completion. Operational completion is the point at which the SPV has met all the completion criteria specified in the Project Agreement.

On the Service Commencement Date, the SPV will be obliged to pay the Rental Prepayment to the Crown, representing the rental to be paid under the Facility Lease (cl 12.3 of the Project Agreement). The Rental Prepayment is (in whole) a payment in the nature of rent that the SPV will make for the use and enjoyment of the land covered by the lease, and substitutes for the rent that the SPV would otherwise need to pay over the term of the lease. Clause 12.4 of the Project Agreement provides for the D&C Payment and the Rental Prepayment to be set off against each other. The total amount of the Rental Prepayment payable by the SPV will equal the amount of the D&C Payment payable by the Crown.

Operation and Maintenance Phase

During the O&M Phase, the SPV must provide ongoing operational and maintenance services to the Crown as described in the Project Agreement. Broadly, the operational and maintenance services are those services necessary to meet the asset management requirements and will vary depending on the type of asset being constructed.

Under cl 49.1 of the Project Agreement, the Crown will pay the SPV a regular payment for the ongoing services provided (the Unitary Charge). The Unitary Charge will be paid following receipt by the Crown of a valid invoice (as defined in cl 49.2) issued by the SPV in accordance with cl 49.3. Payment of the Unitary Charge may be monthly or quarterly, depending on the nature of the Facility.

The amount of the Unitary Payment may include incentive payments and will be subject to abatement if the SPV does not meet key performance measures. The total amount of the Unitary Payment over the O&M Phase is expected to recover all of the SPV's costs in relation to the project and provide for its profit margin.

Termination of the Project Agreement

The Project Agreement will terminate at the conclusion of the Facility Lease and the O&M Phase, at which time any fit-out will be transferred to the ownership of the Crown for no consideration.

The Project Agreement may also be terminated early if either party defaults on its obligations. For the purposes of this Ruling, the Arrangement does not include any early termination that may take place, and this Ruling does not rule on the consequences of early termination.

Other contracts

To fulfil its obligations under the Project Agreement, the SPV will enter into funding agreements and subcontracts. For the purposes of this Ruling, the Arrangement does not include these other agreements or subcontracts or any ownership structures that may be entered into.

These agreements and subcontracts, together with the Project Agreement, will be an "arrangement" as defined in s YA 1 (the wider arrangement. For the avoidance of doubt, this Ruling does not apply where the Project Agreement is part of a wider arrangement that is a "tax avoidance arrangement" (as defined in s YA 1) such that subpart BG applies to void the wider arrangement.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows.

D&C Payment

- A portion of the D&C Payment will be income under the financial arrangements rules in subpart EW. To the extent that the D&C Payment is not income under the financial arrangements rules:
 - the D&C Payment will be income of the SPV under s CB 1(1) and will not be of a capital nature under s CB 1(2); and
 - for the purposes of s CB 1, the SPV will derive the D&C Payment on the Service Commencement Date.

D&C Expenditure

- The D&C Expenditure is deductible under s DA 1(1), provided that s DA 2(2) to (6) does not apply. The capital limitation in s DA 2(1) does not apply to the D&C Expenditure.
- The SPV's interest in the Initial Fixtures is "revenue account property" as defined in s YA 1. For the purpose of s DB 23, the cost of this revenue account property is equal to the D&C Expenditure.
- Section EA 2 applies to the D&C Expenditure, because the D&C Expenditure is the cost of the "revenue account property". Under s EA 2(2), the deduction for the D&C Expenditure will be allocated to the year in which the Service Commencement Date takes place, because that is when the SPV disposes of the "revenue account property".
- Section GC 1 will not apply to the disposal of the SPV's interest in the Initial Fixtures.

Rental Prepayment

- The Rental Prepayment is deductible under s DA 1(1). The capital limitation in s DA 2(1) does not apply to the Rental Prepayment.
- The accrual expenditure rules (in ss EA 3, CH 2 and DB 50) apply to the Rental Prepayment each year from the Service Commencement Date. To the extent of the unexpired amount (determined under s EA 3(4)) of the Rental Prepayment at the end of an income year, an amount of income is derived by the SPV in that income year and the SPV is allowed a deduction for this amount in the subsequent income year.
- The SPV must spread the Rental Prepayment on a straight-line basis over the period of the lease term in order to determine the value of the unexpired portion of expenditure under s EA 3.

Unitary Charge

- The Unitary Charge will be assessable income of the SPV under s CB 1.
- For the purpose of s BD 3, the SPV will derive the Unitary Charge in the income year in which it issues a valid invoice to the Crown.

The period or tax year for which this Ruling applies

This Ruling will apply for an indefinite period beginning on 21 October 2013.

This Ruling is signed by me on 21 October 2013.

Howard Davis

Director, Taxpayer Rulings

INCOME TAX – STANDARD PROJECT AGREEMENT FOR A PUBLIC–PRIVATE PARTNERSHIP - PARTNERSHIPS

PUBLIC RULING - BR Pub 13/06

This is a public ruling made under s 91D of the Tax Administration Act 1994.

Taxation Laws

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

This Ruling applies in respect of ss CB 1, CH 2, DA 1, DA 2, DB 50, EA 2 and EA 3.

The Arrangement to which this Ruling applies

The Arrangement is the design, construction, operation and maintenance of an asset (the Facility) by a partnership (as that term is defined in s YA 1) (the special purpose vehicle – SPV) under a public–private partnership agreement with Her Majesty, The Queen in Right of New Zealand acting by and through a government department (the Crown). The definition of “partnership” in s YA 1 includes a limited partnership and a joint venture that chooses to be treated as a partnership.

The Arrangement is governed by a standard form contract prepared by Treasury (the Project Agreement). Key clauses of the Project Agreement and relevant definitions have been included in Appendix B to the Commentary of this Ruling. This Ruling will not apply if the clauses of the Project Agreement that are referred to in this Ruling are altered in a material way.

The Project Agreement has three main components:

- The **Design and Construction (D&C) Phase** involves the SPV providing design and construction supplies in return for a lump sum design and construction payment (the D&C Payment).
- The **Facility Lease** is the lease into which the SPV and the Crown enter and under which the SPV prepays an amount representing the rental the SPV will pay to the Crown (the Rental Prepayment).
- The **Operation and Maintenance (O&M) Phase** involves the SPV providing operational and maintenance services over a period of approximately 25 years in return for a regular payment (the Unitary Charge). The date on which the O&M Phase starts is referred to as the Service Commencement Date.

Each of the three components is summarised below. The Project Agreement details the rights and obligations of the SPV and the Crown.

Design and Construction Phase

During the D&C Phase, the SPV will design and construct the Facility in accordance with the Project Agreement on behalf of the Crown. The Facility consists of all of the structures that are to be designed, constructed, commissioned and maintained by the SPV in accordance with the terms of the Project Agreement, and includes the entire physical infrastructure, the grounds and all of the fixtures, fit-out, plant and equipment. The SPV will be solely responsible to the Crown for the design and construction of the Facility, including

the provision of infrastructure, plant, equipment and other related obligations, to the standard required by the Project Agreement.

Throughout the term of the Project Agreement, the SPV will not own the Facility or the land on which the Facility will be built (the Crown Site) (cl 11.1). Under cl 11.2(a) of the Project Agreement, any Fixtures that the SPV supplies before the start of the Facility Lease (whether or not affixed to the land) (the Initial Fixtures) will remain the property, and in the ownership, of the SPV until the date of payment of the D&C Payment. For the purposes of the Project Agreement, Fixtures includes all buildings (including component parts of buildings), other structures, improvements, and roads. If the Crown fails to pay the D&C Payment in full when it is due, the SPV can exercise its ownership rights and remove the Initial Fixtures (cl 11.2(b)). The ownership of the Initial Fixtures retained by the SPV under cl 11.2(a) will be automatically transferred to the Crown on the date of payment of the D&C Payment (cl 11.2(c)).

The D&C Payment is a single, contractually fixed, lump sum that the Crown must pay to the SPV on the Service Commencement Date. The D&C Payment is paid to the SPV by the Crown in consideration for the completion of the Facility and the transfer of the ownership in the Initial Fixtures (cl 12.3). No milestone or progress payments are provided for under the Project Agreement.

The amount of the D&C Payment is determined by direct reference to the agreed design and construction costs of the Facility (excluding fit-out) together with the SPV's funding costs during the D&C Phase. Under cl 12.5(c), the Crown and the SPV agree that the D&C Payment includes capitalised interest to the extent that it exceeds the agreed design and construction costs of the Facility. The SPV does not apply a separate margin in respect of the D&C Phase. The D&C Payment is set off against the amount payable by the SPV as the Rental Prepayment for the Facility Lease, as described below.

To construct the Facility, the SPV will incur expenditure in connection with designing, obtaining, affixing, constructing and implementing the Initial Fixtures. Other than the costs of fit-out and any funding costs, the expenditure incurred by the SPV on the Facility during the D&C Phase is referred to in this Ruling as the D&C Expenditure.

Facility Lease

Clause 12.2 of the Project Agreement provides for the Crown and the SPV to enter into a lease in respect of the Facility on or before the date of operational completion. Operational completion is the point at which the SPV has met all the completion criteria specified in the Project Agreement.

On the Service Commencement Date, the SPV will be obliged to pay the Rental Prepayment to the Crown, representing the rental to be paid under the Facility Lease (cl 12.3 of the Project Agreement). The Rental Prepayment is (in whole) a payment in the nature of rent that the SPV will make for the use and enjoyment of the land covered by the lease, and substitutes for the rent that the SPV would otherwise need to pay over the term of the lease. Clause 12.4 of the Project Agreement provides for the D&C Payment and the Rental Prepayment to be set off against each other. The total amount of the Rental Prepayment payable by the SPV will equal the amount of the D&C Payment payable by the Crown.

Operation and Maintenance Phase

During the O&M Phase, the SPV must provide ongoing operational and maintenance services to the Crown as described in the Project Agreement. Broadly, the operational and maintenance services are those services necessary to meet the asset management requirements and will vary depending on the type of asset being constructed.

Under cl 49.1 of the Project Agreement, the Crown will pay the SPV a regular payment for the ongoing services provided (the Unitary Charge). The Unitary Charge will be paid following receipt by the Crown of a valid invoice (as defined in cl 49.2) issued by the SPV in accordance with cl 49.3. Payment of the Unitary Charge may be monthly or quarterly, depending on the nature of the Facility.

The amount of the Unitary Payment may include incentive payments and will be subject to abatement if the SPV does not meet key performance measures. The total amount of the Unitary Payment over the O&M Phase is expected to recover all of the SPV's costs in relation to the project and provide for its profit margin.

Termination of the Project Agreement

The Project Agreement will terminate at the conclusion of the Facility Lease and the O&M Phase, at which time any fit-out will be transferred to the ownership of the Crown for no consideration.

The Project Agreement may also be terminated early if either party defaults on its obligations. For the purposes of this Ruling, the Arrangement does not include any early termination that may take place, and this Ruling does not rule on the consequences of early termination.

Other contracts

To fulfil its obligations under the Project Agreement, the SPV will enter into funding agreements and subcontracts. For the purposes of this Ruling, the Arrangement does not include these other agreements or subcontracts or any ownership structures that may be entered into.

These agreements and subcontracts, together with the Project Agreement, will be an "arrangement" as defined in s YA 1 (the wider arrangement. For the avoidance of doubt, this Ruling does not apply where the Project Agreement is part of a wider arrangement that is a "tax avoidance arrangement" (as defined in s YA 1) such that subpart BG applies to void the wider arrangement.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows.

D&C Payment

- A portion of the D&C Payment will be income under the financial arrangements rules in subpart EW. To the extent that the D&C Payment is not income under the financial arrangements rules:
 - each partner's share of the D&C Payment (calculated in accordance with s HG 2) will be income of the partner under s CB 1(1) and will not be of a capital nature under s CB 1(2); and

- for the purposes of s CB 1, each partner will derive the D&C Payment on the Service Commencement Date.

D&C Expenditure

- Subject to s HG 11 in the case of a “limited partnership” (as defined in s YA 1), each partner’s share of the D&C Expenditure (calculated in accordance with s HG 2) is deductible under s DA 1(1), provided that s DA 2(2) to (6) does not apply. The capital limitation in s DA 2(1) does not apply to the D&C Expenditure.
- Each partner’s share of the SPV’s interest in the Initial Fixtures (calculated in accordance with s HG 2) is “revenue account property” as defined in s YA 1. For the purpose of s DB 23, the cost of this revenue account property is equal to the D&C Expenditure.
- Section EA 2 applies to the D&C Expenditure, because the D&C Expenditure is the cost of the “revenue account property”. Under s EA 2(2), the deduction for the D&C Expenditure will be allocated to the year in which the Service Commencement Date takes place, because that is when the “revenue account property” is disposed of.
- Section GC 1 will not apply to the disposal of each partner’s share of the SPV’s interest in the Initial Fixtures.

Rental Prepayment

- Subject to s HG 11 in the case of a “limited partnership” (as defined in s YA 1), each partner’s share of the Rental Prepayment (calculated in accordance with s HG 2) is deductible under s DA 1(1). The capital limitation in s DA 2(1) does not apply to the Rental Prepayment.
- The accrual expenditure rules (in ss EA 3, CH 2 and DB 50) apply to the Rental Prepayment each year from the Service Commencement Date. To the extent of the unexpired amount (determined under s EA 3(4)) of the Rental Prepayment at the end of an income year, an amount of income is derived by each partner in that income year and the partner is allowed a deduction for this amount in the subsequent income year.
- Each partner must spread their share of the Rental Prepayment (calculated in accordance with s HG 2) on a straight-line basis over the period of the lease term in order to determine the value of the unexpired portion of expenditure under s EA 3.

Unitary Charge

- Each partner’s share of the Unitary Charge (calculated in accordance with s HG 2) will be assessable income of the partner under s CB 1.
- For the purpose of s BD 3, each partner will derive the Unitary Charge in the income year in which the SPV issues a valid invoice to the Crown.

The period or tax year for which this Ruling applies

This Ruling will apply for an indefinite period beginning on 21 October 2013.

This Ruling is signed by me on 21 October 2013.

Howard Davis

Director, Taxpayer Rulings

COMMENTARY ON PUBLIC RULINGS BR PUB 13/05 AND BR PUB 13/06

This commentary is not a legally binding statement. The commentary is intended to help readers understand and apply the conclusions reached in Public Rulings BR Pub 13/05 and BR Pub 13/06 (the Public Rulings).

Legislative references are to the Income Tax Act 2007 unless otherwise stated. Relevant legislative provisions are reproduced in Appendix A to this commentary.

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Background

1. The Treasury has prepared a standard form contract to govern all public–private partnership (PPP) projects in New Zealand (the Project Agreement). Key clauses of the Project Agreement are included in Appendix B. The Project Agreement will form the basis of the agreement between the Crown and the preferred or successful bidder (the special purpose vehicle – SPV) in any future PPP project.
2. The Project Agreement also forms the basis of the Arrangement on which the Public Rulings are issued. The Public Rulings set out the income tax treatment of the main components of the Project Agreement.

Tax Administration Act 1994

3. Under Part 5A of the Tax Administration Act 1994 (TAA), the Commissioner has the ability to make binding rulings. The purpose of this ability is to provide taxpayers with certainty about the way the Commissioner will apply taxation laws and to help taxpayers to meet their obligations under those laws (s 91A).
4. Under s 91D, the Commissioner can make public rulings on how a taxation law applies to any type of person and any type of arrangement. Public rulings interpret how a taxation law applies to a specific type of arrangement that has a wide general application. The Public Rulings are public rulings that set out how the income tax laws apply to the standard form Project Agreement, as the Project Agreement will be used as the basis for all future PPP projects. Provided that the relevant clauses of the Project Agreement are not amended in a material way, the Public Rulings

will apply to give certainty to future preferred bidders regarding the application of the taxation laws contained in the Public Rulings.

5. Under s 91E, the Commissioner can make private rulings on how a taxation law applies to a specific person(s) and a specific arrangement on which the ruling is sought. A private ruling can be applied for by a preferred bidder in relation to the specific structure being entered into, to give certainty on the application of the taxation laws to that structure (particularly in relation to taxation laws that are not included in the Public Rulings). For more information on private rulings, see our booklet *Binding rulings: How to get certainty on the tax position of your transaction* (IR715) which is available from the Inland Revenue website.
6. The term "taxation law" is defined in s 91C, which provides that the Commissioner can make a ruling on most provisions of the Income Tax Act 2007. For current purposes, the key exception is that the Commissioner is unable to make a ruling where the matter is or could be the subject of a determination under s 90AC (which relates to the application of the financial arrangements rules). This means that the Commissioner is unable to provide a binding ruling in respect of many issues relating to the application of the financial arrangements rules in subpart EW, but must instead make a financial arrangements rules determination under s 90AC in order to give taxpayers certainty.
7. Therefore, in order for a bidder to obtain certainty in relation to the application of the taxation laws in any particular PPP project, it is likely that a combination of the Public Rulings, a private ruling and a financial arrangements rules determination will be necessary.
8. Any preferred or successful bidder is strongly advised to apply for a private ruling and a financial arrangements rules determination in respect of its specific structure to provide certainty on any issues that are not addressed in the Rulings. The Crown may require the successful bidder to obtain a favourable private ruling in respect of issues not addressed in the Public Rulings.

Application of the Legislation

9. The term SPV is used in this commentary as a generic term to refer to the successful bidder who enters into a Project Agreement with the Crown. It is used in this commentary to refer to either a company or a partner's share in a partnership, as relevant.

SPV is carrying on a "business"

10. The term "business" is defined in s YA 1, and includes "any profession, trade, or undertaking carried on for profit". The leading New Zealand case on the meaning of "business" is *Grieve v CIR* (1984) 6 NZTC 61,682 (CA).
11. In *Grieve*, Richardson J held that determining whether a business existed involved a two-fold enquiry into the:
 - nature of the activities carried on; and
 - intention of the taxpayer in engaging in those activities.

12. By entering into the Project Agreement with the Crown, the SPV will be responsible for the design and construction of the Facility and the provision of ongoing operational services to the Crown over a period of approximately 25 years. The SPV will also intend to make a profit from entering into the Project Agreement through the receipt of the Unitary Charge.
13. Therefore, the SPV will have the requisite level of activities and intention to profit and will be carrying on a "business" (as defined in s YA 1). This will be the case even if all of the obligations under the Project Agreement are subcontracted to other persons.

Application of the financial arrangement rules

14. The Project Agreement is a "financial arrangement" as defined in s EW 3, and will be part of a wider financial arrangement that also includes any funding agreements and subcontracts the SPV enters into.
15. The Design and Construction (D&C) Phase of the Project Agreement is a financial arrangement as defined in s EW 3. Under the D&C Phase, the SPV will receive consideration from the Crown (in the form of the D&C Payment) and will provide consideration to the Crown (in the form of the Facility). The SPV and the Crown agree that the D&C Payment includes capitalised interest (cl 12.5(c) of the Project Agreement). The effect of cl 12.5(c) will be that part of the D&C Payment will be income under the financial arrangements rules in subpart EW. It is likely that Commissioner would determine that the amount of income will be equal to the capitalised interest that the parties agree is included in the D&C Payment. However, to obtain certainty on this point, the SPV is strongly advised to apply for a financial arrangements rules determination, which will determine the value of the Facility (under s EW 32(6) of the Income Tax Act 2007 and s 90AC of the Tax Administration Act 1994), the amount of income derived under the financial arrangement rules and how that income should be spread over the term of the D&C Phase.
16. It is likely that no income or expenditure arises under the financial arrangement rules in subpart EW in relation to the Facility Lease and the Operation and Maintenance (O&M) Phase of the Project Agreement, for the following reasons:
 - The Facility Lease is an excepted financial arrangement under s EW 5(9). The Rental Prepayment is solely attributable to that excepted financial arrangement, so is not taken into account under the financial arrangement rules in accordance with s EW 6(2).
 - The O&M Phase is a "short-term agreement for sale and purchase" (as defined in s YA 1) of services and is an excepted financial arrangement under s EW 5(22). In accordance with s EW 6(3), amounts solely attributable to this excepted financial arrangement are taken into account under the financial arrangement rules. However, because the consideration the SPV pays (that is, the services provided to the Crown) is equal in value to the consideration the SPV receives (the Unitary Charge), there is no amount to spread under the financial arrangement rules.

17. Therefore, the SPV must recognise amounts paid and received under the Facility Lease and the O&M Phase of the Project Agreement as income derived or expenditure incurred under the relevant provisions of the Income Tax Act 2007 (outside the financial arrangement rules) in accordance with the Public Rulings.
18. Any successful bidder is strongly advised to apply for a financial arrangements rules determination in respect of its specific structure. See Special Determination S22: "Application of the financial arrangements rules to a public-private partnership" (*Tax Information Bulletin* Vol 24, No 9 (October/November 2012)) for an example of a financial arrangements rules determination issued in respect of a PPP project dealing with similar issues.

Design and Construction Payment

19. As noted in para 15, to the extent that the D&C Payment consists of capitalised interest, the financial arrangements rules in subpart EW apply to the D&C Payment. The remainder of the D&C Payment will be an amount that the SPV derives from a business, so will be income under s CB 1(1). The D&C Payment will not be of a capital nature under s CB 1(2).
20. Other than any amount required to be spread under the financial arrangements rules, the SPV will derive the D&C Payment on the Service Commencement Date in consideration for performing its obligations under the Project Agreement and the transfer of the SPV's ownership interest in the Initial Fixtures.

Design and Construction Expenditure

21. Clause 11.2 of the Project Agreement makes it clear that the SPV retains ownership of the Initial Fixtures and disposes of that ownership on the Service Commencement Date in consideration for the D&C Payment. The ownership interest retained by the SPV in the Initial Fixtures (under cl 11.2) is "revenue account property" (as defined in s YA 1). The "cost" of the revenue account property is equal to the D&C Expenditure. Therefore, s DB 23 applies to override the capital limitation in s DA 2(1).
22. As the SPV is in business, the D&C Expenditure will be deductible under s DA 1. The capital limitation in s DA 2(1) will not apply to the D&C Expenditure, because of the application of s DB 23. Whether the other limitations in s DA 2 apply to the D&C Expenditure will depend on the nature of the structure and other arrangements the SPV enters into, which is outside the scope of the Public Rulings.
23. Section EA 2 applies to determine the timing of the deduction for the D&C Expenditure. Section EA 2(2) provides that the SPV will be entitled to a deduction for the cost of revenue account property in the earlier of the income year in which the person disposes of the property or the property ceases to exist.
24. Under the Project Agreement, the SPV will dispose of the "revenue account property" for the D&C Payment on the Service Commencement Date. Therefore, the SPV will be entitled to claim a deduction for the D&C

Expenditure in the income year in which the Service Commencement Date occurs.

Matching of Design and Construction Expenditure and Payment

25. The effect of the above conclusions are that the D&C Expenditure will be deductible to the SPV in the same income year that the SPV receives the D&C Payment, being the income year in which the Service Commencement Date occurs.

Rental Prepayment

26. The courts have held that if a taxpayer incurs rental expenditure as part of their income-earning process that expenditure will be of a revenue nature: *FCT v South Australian Battery Makers Pty Ltd* (1978) 78 ATC 4,412; *Wattie v CIR* (1996) 17 NZTC 12,712.
27. The Rental Prepayment is (in whole) a payment in the nature of rent that the SPV will make for the use and enjoyment of the land covered by the Facility Lease, and substitutes for the rent that the SPV would otherwise need to pay over the term of the Facility Lease. That the Lease Prepayment is "prepaid" in one lump sum does not change its character for tax purposes: *JP Hancock v General Reversionary and Investment Co Ltd* [1919] 1 KB 25; *J Gadsden & Co v CIR* [1965] NZLR 385; *National Australia Bank Ltd v FC of T* (1997) 37 ATR 378.
28. As the SPV is in business and the Facility Lease is part of its income-earning process, the Rental Prepayment will be deductible under s DA 1. The Rental Prepayment will not be subject to the capital limitation in s DA 2(1).
29. Section EA 3 applies in relation to the timing of the deduction for the Rental Prepayment. Where s EA 3 applies, s EA 3(3) states:
- The unexpired portion of a person's expenditure at the end of an income year—
- (a) is income of the person in the income year under section CH 2 (Adjustment for prepayments); and
 - (b) is an amount for which the person is allowed a deduction in the following income year under section DB 50 (Adjustment for prepayments).
30. The Rental Prepayment is made in respect of the Facility Lease, which is a "good" for the purposes of s EA 3 (being an interest in land and therefore real property). The Rental Prepayment is not made in respect of services, a chose in action or an allowance reimbursing employees. Therefore, the unexpired portion must be determined in accordance with s EA 3(4).
31. Section EA 3(4) states that an amount of expenditure on goods is unexpired at the end of an income year if the:
- person has not used up the goods in deriving income; and
 - goods are not destroyed or rendered useless for the purpose of deriving income.

32. The term “used” in the context of s EA 3(4) means being expended through being consumed or incorporated into other assets: *Thornton Estates Ltd v CIR* (1998) 18 NZTC 13,577 (CA).
33. In the context of a lease of property, the goods are used up evenly over the term of the lease. The unexpired portion at the end of an income year will cover the portion of the expenditure that relates to the portion of the lease that is yet to take place.
34. Therefore, the “unexpired” portion of the Rental Prepayment, in terms of s EA 3(4), will be the portion that relates to the outstanding term of the lease at the end of each income year. This means the Rental Prepayment will be spread evenly over the term of the lease (on a straight-line basis).

Unitary Charge

35. Because the SPV is in business, the Unitary Charge will be income of the SPV under s CB 1.
36. Section BD 3 requires every amount of income to be allocated to the income year in which it is derived. Case law on the meaning of the term establishes that an amount is “derived” when the income-earning process is complete. Once the SPV has undertaken the operational and maintenance services and issued the Crown with a valid invoice (as defined in cl 49.2 of the Project Agreement), the income-earning process will be complete and the Unitary Charge will have been derived.

Section BG 1

37. It is the Commissioner’s opinion that the Project Agreement is not a “tax avoidance arrangement” (as defined in s YA 1) for the purposes of s BG 1. However, as noted in the Public Rulings, the Project Agreement is part of a wider arrangement that also consists of any funding agreements and subcontracts that the SPV may enter into.
38. For the purposes of s BG 1, the wider arrangement will be an “arrangement” (as defined in s YA 1) and the Commissioner could potentially conclude that the wider arrangement entered into by the SPV is a “tax avoidance arrangement” that is void pursuant to s BG 1.
39. Although the Commissioner considers it unlikely, if s BG 1 applied to the wider arrangement, any reconstruction under s GA 1 could potentially affect the conclusions reached in the Public Rulings in relation to the income tax treatment of the Project Agreement. The Commissioner is unable to reach a conclusion on the application of s GA 1 and the appropriate reconstruction to make without knowing the full details of the “tax avoidance arrangement” entered into. For this reason, the Public Rulings do not and cannot rule on the potential application of s BG 1.
40. It is the Commissioner’s view that s BG 1 is unlikely to apply to any arrangement where:
 - the funding agreements are straight-forward loans entered into on an arm’s length basis with third-party lenders on market terms;

- any related party funding does not have any artificial features and is entered into on an arm's length basis on market terms; and
 - any subcontracts are entered into on an arm's length basis on market terms.
41. However, because each particular PPP arrangement entered into will differ, the Commissioner needs to consider the facts of any arrangement entered into before reaching a definitive conclusion on the potential application of s BG 1. Any successful bidder is strongly advised to apply for a private binding ruling in respect of its specific arrangement if it wants certainty regarding the Commissioner's view on s BG 1.

References

Subject references

public-private partnership (PPP)

Legislative references

Income Tax Act 2007, ss CB 1, CH 2, DA 1, DA 2, DB 50, EA 2 and EA 3 and subpart EW

Case references

FCT v South Australian Battery Makers Pty Ltd (1978) 78 ATC 4,412
Grieve v CIR (1984) 6 NZTC 61,682 (CA)
J Gadsden & Co v CIR [1965] NZLR 385
JP Hancock v General Reversionary and Investment Co Ltd [1919] 1 KB 25

National Australia Bank Ltd v FC of T (1997) 37 ATR 378

Thornton Estates Ltd v CIR (1998) 18 NZTC 13,577 (CA)

Wattie v CIR (1996) 17 NZTC 12,712

Other references

Binding rulings: How to get certainty on the tax position of your transaction (IR715)

Special Determination S22: "Application of the financial arrangements rules to a public-private partnership" *Tax Information Bulletin* Vol 24, No 9 (October/November 2012)

Appendix A – Legislation

Income Tax Act 2007

1. Section BD 3 provides:

BD 3 Allocation of income to particular income years

Application

- (1) Every amount of income must be allocated to an income year under this section.

General rule

- (2) An amount of income is allocated to the income year in which the amount is derived, unless a provision in any of Parts C or E to I provides for allocation on another basis.

Interpretation of derive

- (3) When the time of derivation of an amount of income is being determined, regard must be had to case law, which—
- (a) requires some people to recognise income on an accrual basis; and
 - (b) requires other people to recognise income on a cash basis; and
 - (c) more generally, defines the concept of derivation. Income credited in account
- (4) Despite subsection (3), income that has not previously been derived by a person is treated as being derived when it is credited in their account or, in some other way, dealt with in their interest or on their behalf.

Role of Part E

- (5) Part E (Timing and quantifying rules) contains a number of provisions that—
- (a) specifically modify the allocation of income or have the effect of modifying the allocation of income; or
 - (b) allocate income as part of the process of quantifying it.

Single allocation

- (6) An amount of income may be allocated only once.

2. Section CB 1 provides:

CB 1 Amounts derived from business

Income

- (1) An amount that a person derives from a business is income of the person.

Exclusion

- (2) Subsection (1) does not apply to an amount that is of a capital nature.

3. Section CH 2 provides:

CH 2 Adjustment for prepayments

When this section applies

- (1) This section applies when a person has, under section EA 3 (Prepayments), an unexpired amount of expenditure at the end of an income year.

Income

- (2) The unexpired amount is income of the person in the income year.

4. Section DA 1 provides:

DA 1 General permission

Nexus with income

- (1) A person is allowed a deduction for an amount of expenditure or loss, including an amount of depreciation loss, to the extent to which the expenditure or loss is—

- (a) incurred by them in deriving—
 - (i) their assessable income; or
 - (ii) their excluded income; or
 - (iii) a combination of their assessable income and excluded income; or
- (b) incurred by them in the course of carrying on a business for the purpose of deriving—
 - (i) their assessable income; or
 - (ii) their excluded income; or
 - (iii) a combination of their assessable income and excluded income.

General permission

- (2) Subsection (1) is called the **general permission**.

Avoidance arrangements

- (3) Section GB 33 (Arrangements involving depreciation loss) may apply to override the general permission in relation to an amount of depreciation loss.

5. Section DB 2 provides:

DA 2 General limitations

Capital limitation

- (1) A person is denied a deduction for an amount of expenditure or loss to the extent to which it is of a capital nature. This rule is called the **capital limitation**.

Private limitation

- (2) A person is denied a deduction for an amount of expenditure or loss to the extent to which it is of a private or domestic nature. This rule is called the **private limitation**.

Exempt income limitation

- (3) A person is denied a deduction for an amount of expenditure or loss to the extent to which it is incurred in deriving exempt income. This rule is called the **exempt income limitation**.

Employment limitation

- (4) A person is denied a deduction for an amount of expenditure or loss to the extent to which it is incurred in deriving income from employment. This rule is called the **employment limitation**.

Withholding tax limitation

- (5) A person is denied a deduction for an amount of expenditure or loss to the extent to which it is incurred in deriving non-resident passive income of the kind referred to in section RF 2(3) (Non-resident passive income). This rule is called the **withholding tax limitation**.

Non-residents' foreign-sourced income limitation

- (6) A person is denied a deduction for an amount of expenditure or loss to the extent to which it is incurred in deriving non-residents' foreign-sourced income. This rule is called the **non-residents' foreign-sourced income limitation**.

Relationship of general limitations to general permission

- (7) Each of the general limitations in this section overrides the general permission.

6. Section DB 23 provides:

DB 23 Cost of revenue account property

Deduction

- (1) A person is allowed a deduction for expenditure that they incur as the cost of revenue account property.

No deduction

- (2) Despite subsection (1), a person is denied a deduction for expenditure incurred as the cost of revenue account property if—
 - (a) Repealed.
 - (b) section CX 55, CX 56B, or CX 56C (which relate to portfolio investment income) applies to income derived by the person from the disposal of the revenue account property.

Link with subpart DA

- (3) Subsection (1) overrides the capital limitation but the general permission must still be satisfied. Subsection (2) overrides the general permission. The other general limitations still apply.

7. Section DB 50 provides:

DB 50 Adjustment for prepayments

When this section applies

- (1) This section applies when a person has, under section EA 3 (Prepayments), an unexpired amount of expenditure at the end of an income year.

Deduction

- (2) The person is allowed a deduction for the unexpired amount for the following income year.

Link with subpart DA

- (3) This section supplements the general permission. The general limitations still apply, but not to the extent to which any relevant general limitation was overridden by a provision that initially allowed a deduction for the expenditure, whether in this Act or an earlier Act.

8. Section EA 2 provides:

EA 2 Other revenue account property

When this section applies

- (1) This section applies to revenue account property that is not—
 - (a) trading stock valued under subpart EB (Valuation of trading stock (including dealer's livestock));
 - (b) livestock valued under subpart EC (Valuation of livestock);
 - (c) an excepted financial arrangement valued under subpart ED (Valuation of excepted financial arrangements);
 - (d) a film or a film right to which sections EJ 4toEJ 8 (which relate to films) apply;
 - (e) a specified lease or a lease to which section EJ 10 (Personal property lease payments) applies;
 - (f) property that arises as a result of petroleum development expenditure or petroleum exploration expenditure to which sections EJ 12toEJ 20 (which relate to petroleum mining) apply;
 - (g) a financial arrangement valued under subpart EW (Financial arrangements rules).

Timing of deduction

- (2) A deduction for the cost of revenue account property of a person is allocated to the earlier of—
 - (a) the income year in which the person disposes of the property; and
 - (b) the income year in which the property ceases to exist.

9. Section EA 3 provides:

EA 3 Prepayments

When this section applies

- (1) This section applies when—

- (a) a person has been allowed a deduction for expenditure under this Act or an earlier Act; and
- (b) the expenditure was not incurred on the items described in subsection (2); and
- (c) some or all of the expenditure is unexpired under subsections (4) to (7) at the end of the person's income year.

Exclusions

- (2) This section does not apply to expenditure incurred on—
 - (a) revenue account property to which section EA 2 applies;
 - (b) trading stock valued under subpart EB (Valuation of trading stock (including dealer's livestock));
 - (c) livestock valued under subpart EC (Valuation of livestock);
 - (d) an excepted financial arrangement valued under subpart ED (Valuation of excepted financial arrangements);
 - (e) a film or a film right to which sections EJ 4 to EJ 8 (which relate to films) apply;
 - (f) a specified lease or a lease to which section EJ 10 (Personal property lease payments) applies;
 - (g) property that arises as a result of petroleum development expenditure or petroleum exploration expenditure to which sections EJ 12 to EJ 20 (which relate to petroleum mining) apply;
 - (h) a financial arrangement valued under subpart EW (Financial arrangements rules).

Unexpired portion

- (3) The unexpired portion of a person's expenditure at the end of an income year—
 - (a) is income of the person in the income year under section CH 2 (Adjustment for prepayments); and
 - (b) is an amount for which the person is allowed a deduction in the following income year under section DB 50 (Adjustment for prepayments).

Unexpired portion: expenditure on goods

- (4) An amount of expenditure on goods is unexpired at the end of an income year if, by the end of the income year,—
 - (a) the person has not used up the goods in deriving income; and
 - (b) the goods are not destroyed or rendered useless for the purpose of deriving income.

Unexpired portion: expenditure on services

- (5) An amount of expenditure on services is unexpired at the end of an income year if the services have not been performed by the end of the income year.

Unexpired portion: expenditure on choses in action

- (6) An amount of expenditure on a chose in action is unexpired at the end of an income year if the amount relates to a period of enforceability of the chose in action falling after the income year.

Allowances reimbursing employees

- (7) In the case of expenditure subject to sections CW 17, CW 17B, CW 17C, and CW 18 (which relate to expenditure, reimbursement, and allowances of employees), this section applies on the basis that the relevant services were performed in the income year in which the employee's expenditure is expected to occur.

Commissioner's discretionary relief

- (8) The Commissioner may excuse a person from complying with this section under section 91AAC of the Tax Administration Act 1994.

10. Section HG 2 provides:

HG 2 Partnerships are transparent

Look-through in accordance with share

- (1) For the purposes of a partner's liabilities and obligations under this Act in their capacity of partner of a partnership, unless the context requires otherwise,—
- (a) the partner is treated as carrying on an activity carried on by the partnership, and having a status, intention, and purpose of the partnership, and the partnership is treated as not carrying on the activity or having the status, intention, or purpose:
 - (b) the partner is treated as holding property that a partnership holds, in proportion to the partner's partnership share, and the partnership is treated as not holding the property:
 - (c) the partner is treated as being party to an arrangement to which the partnership is a party, in proportion to the partner's partnership share, and the partnership is treated as not being a party to the arrangement:
 - (d) the partner is treated as doing a thing and being entitled to a thing that the partnership does or is entitled to, in proportion to the partner's partnership share, and the partnership is treated as not doing the thing or being entitled to the thing.

No streaming

- (2) Despite subsection (1), for a partner in their capacity of partner of a partnership, the amount of income, tax credit, rebate, gain, expenditure, or loss that they have from a particular source, or of a particular nature, is calculated by multiplying the total income, tax credit, rebate, gain, expenditure, or loss of the partners of the partnership from the particular source or of the particular nature by the partner's partnership share in the partnership's income.

Expenditure or loss previously incurred

- (3) A partner of a partnership may be treated as incurring an expenditure or loss which the partnership incurs ignoring this section, despite the partner not being a partner at the time the expenditure or loss is incurred. This subsection does not allow 2 deductions for 1 expenditure or loss.

Excluded amounts

- (4) Subsection (2) does not apply to the following amounts:
- (a) expenditure or loss that relates to a person entering a partnership by acquiring partner's interests disposed of by another partner, to the extent to which sections HG 5 to HG 10 do not apply to the partner's interests:
 - (b) supplementary dividends, to the extent to which subpart LP (Tax credits for supplementary dividends) applies:
 - (c) Repealed.
 - (d) imputation credits, to the extent to which section LE 6 (Partners in partnerships) applies:
 - (e) FDP credits, to the extent to which section LF 4 (Partners in partnerships) applies.

11. Section HG 11 provides:

HG 11 Limitation on deductions by partners in limited partnerships

When this section applies

- (1) This section applies for a limited partnership and an income year when, but for this section, a deduction by virtue of section HG 2 or HG 12 is allowed to—
- (a) a limited partner of the limited partnership:
 - (b) a general partner of the partnership who—

- (i) was a limited partner of the limited partnership within 60 days of the last day of the income year; and
- (ii) is or will be a limited partner of the limited partnership within 60 days after the last day of the income year.

No deduction

- (2) The partner is denied the deduction for an income year to the extent to which their limited partnership deduction for the income year is greater than the amount (the **partner's basis**) calculated using the formula in subsection (3) on the last day of the income year.

Partner's basis

- (3) For the purposes of subsection (2), the amount that is the partner's basis is calculated using the following formula:

investments – distributions + income – deductions – disallowed amount.

Definition of items in formula

- (4) The items in the formula are defined in subsections (5) to (9).

Investments

- (5) **Investments** is the total of—
 - (a) the market value of capital contributions made by the partner to the limited partnership at the time the relevant contribution is contributed or agreed to be contributed by them;
 - (b) the amount paid by the partner for the assignment of capital contributions to them;
 - (c) the secured amounts.

Distributions

- (6) **Distributions** is the total of—
 - (a) the market value of distributions to the partner from the limited partnership;
 - (b) the amount paid to the partner for the assignment of capital contributions by them.

Income

- (7) **Income** is the total of—
 - (a) income that the partner has by virtue of section HG 2 in the income year and previous income years;
 - (ab) if the partner has FIF income or a FIF loss, an amount under subsection (7B);
 - (b) capital gain amounts under section CD 44(7)(a) (Available capital distribution amount) that the partner would have by virtue of section HG 2 in the income year and previous income years, if the partner were treated as a company for the purposes of section CD 44(7)(a), unless the gain is accounted for under paragraph (a);
 - (c) assessable income that the partner has in previous income years from goods and services they contributed to the limited partnership, if the income is not accounted for under subsection (5) or paragraph (a) or (b) of this subsection.

Formula

- (7B) The amount described in subsection (7)(ab) is given by the following formula, but if the calculation returns a negative number, the amount is zero:

dividend – FIF amount.

Definition of items in formula

(7C) In the formula,—

- (a) **dividend** is the amount that would be the partner's share of the dividend paid by a FIF to the limited partnership, if section CD 36(1) (Foreign investment fund income) were ignored:
- (b) **FIF amount** is—
 - (i) zero, if subparagraph (ii) does not apply:
 - (ii) the amount that is the person's FIF income, for the relevant income year and FIF, if the person has such an amount.

Deductions

(8) **Deductions** is the total of—

- (a) expenditure or loss in previous income years, to the extent to which the expenditure or loss is incurred by virtue of section HG 2 in the partner deriving income by virtue of section HG 2, excluding any deductions denied in those previous years under this section:
- (b) capital loss amounts under section CD 44(9) that the partner would have by virtue of section HG 2 in the income year and previous income years..., if the partner is treated as a company for the purposes of section CD 44(9), unless the loss is accounted for under paragraph (a):
- (c) deductions that the partner is allowed in previous income year in relation to assessable income described in subsection (7)(c), if the deduction is not accounted for under subsection (6) or paragraphs (a) or (b) of this section.

Disallowed amounts

(9) **Disallowed amount** is the amount of investments, as defined in subsection (5), made by the partner within 60 days of the last day of the income year, if those investments are or will be distributed or reduced within 60 days after the last day of the income year.

Exclusion

(10) This section does not deny a partner (the exiting partner) a deduction that is equal to or less than the amount of net income that **the** exiting partner has for the amount paid or payable to the exiting partner for the disposal of their partner's interests, ignoring other transactions.

Relationship with subject matter

(11) This section is modified by sections HZ 3, HZ 4 and HZ 4B (which relate to transitions to limited partnerships).

Some definitions

(12) In this section,—

capital contribution includes—

- (a) a capital contribution for the purposes of the Limited Partnerships Act 2008:
- (b) amounts that the limited partnership is debtor for in relation to the partner, including a loan to the limited partnership and a credit balance in a current account

guarantor means—

- (a) a partner, if—
 - (i) the partner secures the relevant debt by guarantee or indemnity:
 - (ii) the partner's associate secures the relevant debt by guarantee or indemnity:
- (b) a person who is not described in paragraph (a)(i) and (ii) but who secures the relevant debt by guarantee or indemnity, if the partner

or a partner's associate also secures the relevant debt as described in paragraph (a)(i) and (ii)

limited partnership deduction means, for the partner and the income year, the amount of any deductions that the partner would be allowed if the partner is treated as having no income or deductions other than those that arise by virtue of sections HG 2 and HG 12

partner's associate means, for a partner, a person who is not a partner of the relevant limited partnership, and who is—

- (a) a relative of the partner, but excluding a person under section YA 1 (Definitions), definition of "relative", paragraph (v):
- (b) a company in the same wholly-owned group as the partner

recourse property means property to which a creditor has recourse, to enforce a guarantee or indemnity for the relevant debt, if the guarantee or indemnity expressly provides recourse to only that property

secured amounts means, for the partner, the lesser of the following applicable amounts—

- (a) the amount of the limited partnership's debt ignoring section HG 2 (the secured debt) for which the partner is a guarantor, divided by the total number of guarantors for the secured debt:
- (b) the market value of the recourse property for the secured debt to the extent of the interest that the partner and the partner's associates have in it, net of higher-ranking calls whether actual, future, or contingent, divided by the total number of guarantors described in the definition of "guarantor", paragraph (a), who have an interest in the recourse property or have a partner's associate with an interest in the recourse property.

12. Section YA 1 contains the following relevant definitions:

business—

- (a) includes any profession, trade, or undertaking carried on for profit:
- (b) includes the activities of—
 - (i) a statutory producer board:
 - (ii) an airport operator:
- (c) is further defined in section DD 11 (Some definitions) for the purposes of subpart DD (Entertainment expenditure)

limited partnership—

- (a) means a limited partnership registered under the Limited Partnerships Act 2008; and
- (b) includes an "overseas limited partnership" as defined in section 4 of that Act; and
- (c) despite paragraph (a) or (b), does not include a listed limited partnership or a foreign corporate limited partnership

revenue account property, for a person, means property that—

- (a) is trading stock of the person:
- (b) if disposed of for valuable consideration, would produce income for the person other than income under section EE 48 (Effect of disposal or event), FA 5 (Assets acquired or disposed of after deductions of payments under lease), or FA 9 (Treatment when lease ends: lessee acquiring asset):
- (c) is an emissions unit of the person:
- (d) is a non-Kyoto greenhouse gas unit

partnership means—

- (a) a group of 2 or more persons who have, between themselves, the relationship described in section 4(1) of the Partnership Act 1908:
- (b) a joint venture, if the joint venturers all choose to be treated as a partnership for the purposes of this Act and the Tax Administration Act 1994:

- (c) co-owners of property, other than persons who are co-owners only because they are shareholders of the same company, or settlors, trustees, or beneficiaries of the same trust, if the co-owners all choose to be treated as a partnership for the purposes of this Act and the Tax Administration Act 1994:
- (d) a limited partnership

Appendix B – Key Clauses from the Project Agreement

The following clauses are those that the Commissioner considers key to the issues considered in the Public Rulings. The Public Rulings will not apply if these clauses of the Project Agreement are altered in a material way.

1. Clause 11 states:

11. Construction of Facilities for Crown

11.1 Ownership of Facility

- (a) The Facility shall be designed and constructed by the Contractor under and in accordance with this Agreement on behalf of the Crown.
- (b) Subject to the rights of the Contractor set out in this Part 5, the Crown will at all times before and after the Service Commencement Date own the Facility (excluding the Fitout, to which clause 11.2(e) applies) and the Crown Site.

11.2 Ownership of Fixtures and Fitout

- (a) Any Fixtures supplied by the Contractor prior to the commencement of the term of the Facility Lease (**Initial Fixtures**) will remain the property, and in the ownership, of the Contractor (notwithstanding any affixing to the Crown Site) until the earlier of:
 - (i) the date of payment in full of the Design and Construction Payment; and
 - (ii) the date of payment in full of the Compensation Sum,(such date being the **Transfer Date**).
- (b) The Crown acknowledges and agrees that the Contractor shall, until the Transfer Date, have the right (in addition and without prejudice to its other rights and remedies under the Project Documents, including the rights of access set out in Part 7 (Access to Site and Site Issues)) to enter and re-enter on to the Crown Site and remove and repossess the Initial Fixtures, but only if and to the extent the Crown fails to pay in full:
 - (i) the Design and Construction Payment in accordance with clauses 12.3 (Payments on Service Commencement Date) and 12.4 (Set-off); or
 - (ii) the Compensation Sum in accordance with clause 79.1 (Payment of Compensation Sum),in each case within 5 Business Days after the due date for payment of such amount under this Agreement.
- (c) Upon the Transfer Date, the Contractor shall immediately transfer to the Crown its ownership of the Initial Fixtures together with all associated rights in and to the Initial Fixtures and the Crown Site reserved under clause 11.2(b). The Initial Fixtures will automatically vest in the Crown on the Transfer Date, by operation of this clause, without the need for any additional action by any person.
- (d) The expenditure incurred by or for the Contractor in connection with the Initial Fixtures will be included in the Design and Construction Payment.
- (e) Any Fitout on the Crown Site will belong to the Contractor until the earlier of the Actual Termination Date and the Expiry Date. On such date, the Fitout will be transferred by the Contractor to the Crown, for no additional consideration, as part of the Disengagement Deliverables in accordance with clause 85 (Contractor's Disengagement Deliverables), the terms of Schedule 24 (Disengagement) and the requirements of the Disengagement Plan.
- (f) Any Fixtures in respect of which the Contractor has incurred expenditure, other than for repairs and maintenance, after the commencement of the Facility Lease will be treated as owned by the Contractor rather than the Crown for the purposes of this Agreement.

On the earlier of the Expiry Date and the Actual Termination Date, any such Fixtures, to the extent ownership is vested in the Contractor, will be transferred by the Contractor to the Crown, for no additional consideration, as part of the Disengagement Deliverables in accordance with clause 85 (Contractor's Disengagement Deliverables), the terms of Schedule 24 (Disengagement) and the requirements of the Disengagement Plan.

2. Clause 12 states:

12. Facility Lease and payments on Service Commencement Date

12.1 Prior to Service Commencement Date

The Contractor will, prior to the Service Commencement Date, have the rights to access the Crown Site set out in Part 7 (Access to Site and Site Issues).

12.2 Entry into Facility Lease

- (a) On or prior to the Crown issuing the Operational Completion Notice, the parties must enter into the Facility Lease. The Facility Lease will have a term commencing at 9.00am on the Service Commencement Date and terminating on the earlier of the Actual Termination Date and the Expiry Date.
- (b) If the Contractor requires registration of the Facility Lease under the Land Transfer Act 1952, each party must do all things necessary to enable the Facility Lease to be registered in the form of a lease instrument at Land Information New Zealand via e-dealing, including without limitation signing an authority and instruction form (so that the relevant solicitor is authorised to provide the certifications required by section 164A of the Land Transfer Act 1952).

12.3 Payments on Service Commencement Date

On the Service Commencement Date, immediately on commencement of the Facility Lease:

- (a) the Crown must pay the Design and Construction Payment to the Contractor in consideration of the completion of the Facility and the transfer of the rights set out in clause 11.2(c) (Ownership of Fixtures and Fitout); and
- (b) the Contractor must pay the Rental Prepayment to the Crown, representing the rental to be prepaid under the Facility Lease,

with the payments to be made in accordance with clause 12.3 (Payments on Service Commencement Date).

12.4 Set off

- (a) The Crown's obligation to pay the Design and Construction Payment to the Contractor and the Contractor's obligation to pay the Rental Prepayment to the Crown:
 - (i) will arise at the same time; and
 - (ii) will be set off against each other immediately on the obligations arising, with the set-off to be recorded in a written notice given by the Crown to the Contractor.
- (b) GST payable as between the parties in respect of the Rental Prepayment and the Design and Construction Payment will be addressed in accordance with clauses 49.8 (Zero rating of Facility Lease) and 49.9 (Design and Construction Payment – GST).

12.5 Financial Arrangements Rules

For the purposes of the financial arrangements rules in the Income Tax Act 2007, the parties agree that:

- (a) they are independent parties dealing at arm's length with each other in relation to the Project;
- (b) the Rental Prepayment is the lowest price the parties would have agreed for the rental of the Facility for the term of the Facility Lease, on the date of this Agreement, if payment had been required in full at the time

the first right in the Facility Lease passes from the Crown to the Contractor;

- (c) the Design and Construction Payment includes capitalised interest to the extent that it exceeds the agreed design and construction costs (which by definition exclude Fitout and debt funding costs) of the Facility;
- (d) the Rental Prepayment is the value of the rental under the Facility Lease and therefore does not include any capitalised interest; and
- (e) in the case of the Contractor only, it will compute its taxable income for the relevant period on the basis that the total consideration includes capitalised interest as set out in clause 12.5(c) above and it will file its Tax returns accordingly.

3. Clause 49 states:

49. Unitary Charge

49.1 Obligation to pay and sole remedy

- (a) The Crown must pay the Contractor the Monthly Unitary Payment in respect of each Payment Period, calculated in accordance with Schedule 14 (Payment Mechanism).
- (b) Subject to clause 49.1(d), the sole remedies of the Crown in respect of a failure to provide the Operational Services in accordance with this Agreement are:
 - (i) where Deductions are applicable for any such failure, the operation of Schedule 14 (Payment Mechanism);
 - (ii) the granting of injunctive relief, a decree of specific performance or other discretionary remedies available from any Court of competent jurisdiction (whether or not Deductions are applicable for any such failure); and
 - (iii) the remedies set out in clause 75 (Termination on Contractor Default).
- (c) Subject to clause 49.1(d), the sole remedies of the Crown in respect of any delay in respect of the carrying out of the Works Provisioning are:
 - (i) where the Contractor fails to comply with clause 25.6 (Milestones) the remedies set out in clause 25.7 (Monitoring);
 - (ii) where the Service Commencement Date does not occur on or prior to the Planned Service Commencement Date, the remedies set out in clause 25.9 (Delays - liquidated damages); and
 - (iii) the remedies set out in clause 75 (Termination on Contractor Default) where the circumstances set out in clauses 75.2(a)(i), 75.2(a)(ii) or 75.2(a)(vi) apply.
- (d) In addition to its remedies under clauses 49.1(b) and 49.1(c), the Crown may exercise:
 - (i) any other express right or remedy of the Crown under this Agreement; and
 - (ii) its right to claim, on or after termination of this Agreement, the amount of its costs, losses, damages and expenses suffered or incurred as a result of rectifying or mitigating the effects of:
 - (A) any breach of this Agreement by the Contractor; or
 - (B) any negligent act or omission on the part of the Contractor,after taking account of:
 - (C) sums already recovered by the Crown under this Agreement; and
 - (D) any compensation payable by the Crown under Part 19 (Termination).

49.2 Report and invoice

- (a) No later than the tenth Business Day of each Payment Period, the Contractor shall submit to the Crown:
 - (i) a report certified by the Contractor:
 - (A) specifying the Monthly Unitary Payment for the immediately preceding Payment Period;
 - (B) setting out individually each item that has been taken into account in calculating the Monthly Unitary Payment in accordance with Schedule 14 (Payment Mechanism);
 - (C) setting out full details of any relief from Deductions claimed under clause 49.4;
 - (D) setting out any Additional Payments due to the Contractor and/or any Moneys Owing to the Crown;
 - (E) setting out a comprehensive explanation of the basis on which such Additional Payments are being claimed, and when the costs associated with such Additional Payments were incurred (including supporting documentation, where applicable); and
 - (F) setting out any other matters required to be included in that report in accordance with Schedule 12 (Service Requirements) and Schedule 7 (Governance and Service Management); and
 - (ii) an invoice (the form of which must have been previously approved by the Crown) (a **valid invoice**) for the amount (if any) shown by the report as owing by the Crown to the Contractor and for all GST payable by the Crown in respect of that amount.
- (b) If the Contractor becomes entitled to any Additional Payments prior to the Service Commencement Date, the Contractor shall submit to the Crown a valid invoice for such Additional Payments and a report certified by the Contractor setting out:
 - (i) the Additional Payments due to the Contractor; and
 - (ii) a comprehensive explanation of the basis on which such Additional Payments are being claimed, and when the costs associated with such Additional Payments were incurred.
- (c) If the Contractor submits a report or an invoice that is incomplete, incorrect or in breach of clause 49.2(a) or clause 49.2(b), the Crown may reject the invoice and that invoice will not be considered as valid.

49.3 Payment

- (a) No moneys are payable to the Contractor by the Crown unless the Crown has received a valid invoice from the Contractor and the report for the Payment Period to which that invoice relates.
- (b) The Crown shall pay the amount stated in any valid invoice submitted under clause 49.2 on or before the 20th of the month following the month in which such invoice was received by the Crown (or if such day is not a Business Day, on the next Business Day) (the **Relevant Payment Date**). This clause 49.3(b) is subject to clause 49.5.
- (c) Payment of the Monthly Unitary Payment, any Additional Payment or any other moneys by the Crown to the Contractor does not constitute acceptance by the Crown that the Contractor has performed its obligations, nor does it constitute (nor is it to be construed as) a waiver of any of the Crown's rights and remedies, whether under this Agreement or at Law.
- (d) If a report shows a net amount owed by the Contractor to the Crown, then the Contractor shall pay that amount to the Crown on or before the 20th of the month following the month in which such report was received by the Crown (or if such day is not a Business Day, on the next Business Day).

- (e) Except where otherwise specifically provided in this Agreement, where any payment due from the Contractor to the Crown or from the Crown to the Contractor under any provision of this Agreement is not paid on or before its due date, it shall bear interest at the Prescribed Rate from the due date (whether before or after any judgment) until the date of actual payment.
- (f) All moneys payable to or by the Crown under this Agreement are to be invoiced and paid only in Dollars.

49.4 **Relief from Deductions**

No Deductions may be made if and to the extent that it has been demonstrated to the reasonable satisfaction of the Crown that the event or circumstance giving rise to the Deduction is a direct result of:

- (a) a Confirmed Change implemented by the Contractor under clause 46.1 (Contractor's obligations), to the extent specified in that Confirmed Change;
- (b) a Change implemented by or on behalf of the Crown under clause 46.2(c), to the extent agreed under clause 46.2(d);
- (c) Scheduled Maintenance being carried out in accordance with the Asset Management Plan and the requirements of this Agreement;
- (d) the Crown or the Retained Services Operator making a specific request or giving specific instructions to the Contractor (in any case, against the reasonable advice of the Contractor, and provided that the Contractor has advised the Crown or the Retained Services Operator in writing of the impact such request or instructions will have on the ability of the Contractor to perform its obligations under this Agreement);
- (e) an Intervening Event, for so long as and to the extent that the Contractor is eligible for relief in respect of that Intervening Event under Part 11 (Events); or
- (f) the Crown exercising its Step-in Rights under Part 17 (Crown Step-in).

49.5 **Disputed Amounts**

- (a) The Crown may withhold the payment of any amount invoiced by the Contractor that the Crown considers on reasonable grounds:
 - (i) is not an amount to which the Contractor is entitled under the terms of this Agreement; or
 - (ii) is not an amount to which the Contractor is entitled on the Relevant Payment Date,
 (each a **Disputed Amount**), pending agreement or determination with respect to that Disputed Amount.
- (b) The Crown must pay any amount invoiced by the Contractor that is not disputed by the Crown on or before the Relevant Payment Date.
- (c) The Crown shall notify the Contractor in writing within 10 Business Days of receipt by the Crown of the relevant invoice of any Disputed Amount, together with a report setting out:
 - (i) particulars as to the quantum of that Disputed Amount;
 - (ii) the reasons for such dispute; and
 - (iii) such supporting evidence as the Crown may wish to provide in respect of the dispute.
- (d) Within five Business Days following receipt by the Contractor of a notice served by the Crown under clause 49.5(c), the Contractor shall respond by notifying the Crown as to whether or not it agrees with the statements made in that notice. If the Contractor indicates that it does agree, or if the Contractor fails to respond within five Business Days, the Crown will not be required to pay to the Contractor any amounts withheld under clause 49.5(a).

- (e) If the Contractor responds under clause 49.5(d) indicating that it does not agree with all or any of the statements made in a notice served by the Crown under clause 49.5(c), the matter or matters in question shall be determined in accordance with the Accelerated Dispute Resolution Procedures.
- (f) If it is agreed or determined that:
 - (i) the Crown has withheld an amount that the Contractor was entitled to be paid; or
 - (ii) the Contractor has claimed under clause 49.2 an amount that it was not entitled to be paid,
 the Crown shall pay such amount to the Contractor or the Contractor shall repay such amount to the Crown (as applicable) together with interest on that amount at the Prescribed Rate from the date on which payment was or should have been made until all relevant monies have been paid in full (whether before or after judgment).
- (g) The Contractor is not excused from the performance of any of its obligations under this Agreement because the Crown has exercised its rights under this clause 49.5.

49.6 **Rights of set-off**

- (a) The Crown may at any time deduct from any amount payable to the Contractor:
 - (i) any Moneys Owing to the Crown; and
 - (ii) any Claim to Moneys Owing which the Crown may have against the Contractor, under any Project Document.
- (b) The Contractor must not at any time deduct from money otherwise due to the Crown (including any Moneys Owing to the Crown) under any Project Document:
 - (i) any debt or other money due from the Crown to the Contractor; or
 - (ii) any Claim to money which the Contractor may have against the Crown.
- (c) The Crown will provide the Contractor with reasonable details of the basis on which it is setting off any amount under this clause 49.6.
- (d) Notwithstanding clause 49.6(a), the Crown acknowledges that it will not be entitled to deduct any Moneys Owing from any payment to or for the account of the Contractor if:
 - (i) this Agreement has been terminated under clause 74 (Termination for Convenience), clause 76 (Termination on Uninsurable Event) or clause 77 (Termination on Uninsurability); and
 - (ii) such deduction would reduce the amount payable to or for the account of the Contractor in connection with the termination of this Agreement to an amount less than the Base Senior Debt Termination Amount.

49.7 **Goods and Services Tax (GST)**

- (a) In this clause 49.7 and in clauses 49.8 and 49.9, words and phrases defined in the GST Act have the meaning given in that Act, unless the context requires otherwise.
- (b) Unless expressly provided to the contrary, any consideration payable for a supply made under this Agreement is stated before the addition of any GST chargeable on that supply.
- (c) The parties agree that where GST is chargeable on a supply made by one party (the **Supplier**) to the other party (the **Recipient**) under this Agreement, the Supplier will issue a tax invoice to the Recipient and the Recipient will pay to the Supplier the GST chargeable on that supply, in addition to the consideration payable for that supply, unless section 5(23) of the GST Act applies to that supply. Subject to clauses 49.8 and

49.9, the Recipient shall pay the GST to the Supplier at the same time as the consideration is paid to the Supplier.

- (d) The Contractor shall provide the Crown with any information reasonably requested by the Crown in relation to the amount of GST chargeable on a supply made under this Agreement and payable by the Crown to the Contractor.

49.8 **Zero rating of Facility Lease**

- (a) The Contractor undertakes that:
 - (i) it will be a registered person on the Service Commencement Date and will provide its tax registration number to the Crown before that date;
 - (ii) it is acquiring the Facility Lease with the intention of using it for making taxable supplies;
 - (iii) it does not intend to use the Facility Lease as a principal place of residence for itself or a person treated as associated with it under section 2A(1)(c) of the GST Act; and
 - (iv) it will not at any time be a member of a group registered for GST under section 55 of the GST Act other than any group comprising the Contractor and HoldCo.
- (b) The parties agree that the supply of the Facility Lease evidences a supply of an interest in land and accordingly, in reliance on the Contractor's undertakings in clause 49.8(a), the Crown will treat the supply of the Facility Lease as zero rated for GST purposes under section 11(1)(mb) of the GST Act.
- (c) Unless section 5(23) of the GST Act applies to the supply of the Facility Lease, if for any reason it is determined that the supply of the Facility Lease is chargeable with GST other than at a rate of zero per cent, the Contractor shall be entitled to recover (and the Crown will pay to the Contractor) the amount of any direct costs (including penalties and interest, legal or other advisory costs, and any costs of financing the additional GST amount), resulting from the supply of the Facility Lease being chargeable with GST other than at a rate of zero per cent, on the Contractor providing reasonable evidence to the Crown of the Contractor's liability for such costs.

49.9 **Design and Construction Payment - GST**

- (a) Each party acknowledges and agrees that:
 - (i) the Design and Construction Payment is consideration for a taxable supply (the **Supply**) under the GST Act;
 - (ii) it will not seek to treat the Supply as zero rated for GST purposes; and
 - (iii) on or before the Service Commencement Date it will be registered under the GST Act on a monthly return cycle and on an "invoice" accounting basis.
- (b) Subject to clause 49.9(c), the Crown must pay the GST chargeable on the Supply to the Contractor by no later than one Business Day prior to the date on which that GST is due to be paid by the Contractor to Inland Revenue.
- (c) If the Crown wishes to satisfy its obligation to pay the GST chargeable on the Supply to the Contractor by way of a GST offset (as agreed with Inland Revenue), the parties will each use their reasonable endeavours to agree on any documentation and other arrangements required to facilitate that offset.

49.10 **Rates and Taxes**

- (a) The Crown is responsible for and will pay all Rates and Taxes assessed on or in relation to the Crown Site, except to the extent that the Contractor causes such Rates or Taxes or any applicable penalty component to be assessed by or as a result of an act or omission of the Contractor.

- (b) Subject only to clause 49.10(a), the Contractor will pay all Rates and Taxes assessed on it, under any Project Document or any transaction evidenced or contemplated by it or in respect of, or because of its involvement in the Project.
- (c) The Contractor will use its reasonable endeavours to ensure that any Rates or Taxes for which the Crown is liable under clause 49.10(a) are invoiced directly by the relevant Governmental Entity to the Crown. Where any invoices for which the Crown is liable under clause 49.10(a) are addressed to the Contractor rather than to the Crown, the Crown will meet the invoiced costs by way of an Additional Payment.

4. Clause 1 contains the following key definitions:

Design and Construction Payment means a payment of the amount specified in cell [*insert reference*] of the Base Case sheet entitled [*insert title*] as at Financial Close, to be made by the Crown to the Contractor on the Service Commencement Date, representing the agreed design and construction costs of the Facility (excluding Fitout) which includes an allocation of the Contractor's debt funding costs, as incurred or deemed incurred during or prior to the Works Provisioning phase;

Facility means all of the structures located or to be located on the Crown Site, that together or separately are to be designed, constructed, commissioned and maintained by the Contractor in accordance with the terms of this Agreement, including:

- (a) the entire physical infrastructure on the Crown Site (including Works Infrastructure);
- (b) the grounds situated within the Crown Site;
- (c) all Fixtures and Fitout; and
- (d) all plant and equipment that is to be exclusively used in or as part of the Facility following Service Commencement,

and includes all Changes made to the Facility (or any part of them) under Part 12 (Changes);

Facility Lease means a deed of lease in the form set out in Annexure 4 to Schedule 3 (Project and Ancillary Documents);

Financial Close means the later of the dates on which:

- (a) all the Conditions Precedent are satisfied or waived, as set out in a notice given by the Crown under clause 10.4 (Conditions Precedent); and
- (b) the Effective Base Rate is first determined and incorporated in the Base Case;

Fitout means all alterations and additions, fittings and partitioning, service facilities, plant and machinery, furnishings, light fittings, and equipment, made to or installed in the Facilities by the Contractor, but excludes Fixtures;

Fixtures means those buildings, including component parts of buildings, other structures and improvements and other property that are or have become attached or affixed to the Crown Site and would at Law, at the relevant time, comprise a 'fixture' and, for the avoidance of doubt, for the purposes of this Agreement includes a road;

Operational Services means each and all of the services described in Schedule 12 (Service Requirements) and includes:

- (a) building management services;
- (b) building maintenance and refurbishment services;
- (c) utilities management services;
- (d) cleaning services;
- (e) waste management services;
- (f) grounds and gardens maintenance;
- (g) security services;
- (h) pest control services; and

(i) *[insert any other services]*,

in each case to be provided in accordance with the Service Requirements;

Payment Period means each calendar month or (in the case of the first and final Payment Periods) part thereof during the period starting on the Service Commencement Date and ending on the last day of the Contract Term;

PPP means the New Zealand Government's public private partnership initiative;

Project Documents means those agreements listed as "Project Documents" in Part 1 (Overview of Project Documents and Ancillary Documents) of Schedule 3 (Project and Ancillary Documents) and includes any document or agreement entered into for the purpose of supplementing, amending, replacing or novating any of those listed documents that the parties have agreed (in writing) to be a Project Document;

Rental Prepayment means payment of the amount specified in *[insert Base Case reference as at Financial Close]* to be made by the Contractor to the Crown on the Service Commencement Date, representing the rental to be paid under the Facility Lease from its commencement until the earlier of the Actual Termination Date and the Expiry Date;

Service Commencement Date means the later of:

- (a) the day specified in the Operational Completion Notice on which all of the Operational Services are to commence; and
- (b) the day on which the Operational Services actually commence,

and **Service Commencement** shall have a corresponding meaning;

Unitary Charge means the fee payable by the Crown during the Operating Term in consideration of the obligations performed by the Contractor under this Agreement, as set out in the Base Case and as calculated and subject to adjustment in accordance with Schedule 14 (Payment Mechanism);