ⓘ This is a reissue of BR Pub 09/07. For more information about the history of this Public Ruling see the Commentary to this Ruling.

**FRINGE BENEFIT TAX – PROVISION OF BENEFITS BY THIRD PARTIES – SECTION CX 2(2)**

## PUBLIC RULING - BR Pub 14/10

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 s CX 2(2) and the definition of "arrangement" in s YA 1.

### The Arrangement to which this Ruling applies

The Arrangement is the receipt of a benefit by an employee from a third party where there is an arrangement between the employer and the third party and where the benefit would amount to a "fringe benefit" if it had been provided by the employer.

The Arrangement does not include situations where the remuneration given by an employer to an employee is reduced because a benefit has been received from the third party, or otherwise takes the receipt of a benefit provided by a third party into account (including salary sacrifice situations). There cannot be any trade-off between the benefits provided and the remuneration that would otherwise have been received by the employee, or any difference between the remuneration levels of employees who receive benefits and those who do not.

### How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

(a) For the purposes of s CX 2(2), there will be an arrangement for the provision of a benefit to an employee where:

  (i) consideration passes from the employer to the third party for the benefit being provided; or

  (ii) the employer requests (other than merely initiating contact), instructs or directs the third party to provide the benefit; or

  (iii) there is negotiation or discussion between the employer and the third party that (explicitly or implicitly) involves the threat or suggestion that the employer would withhold business or other benefits from the third party unless a benefit is provided to the employee; or

  (iv) the third party and the employer are associated parties and there is a group policy (whether formal or informal), or any other agreement between the associated parties, that employees of the group will be entitled to receive benefits from the other companies in the group.

(b) Where the benefit has not been provided in circumstances within any of the categories identified above, s CX 2(2) will not apply where the benefit is provided in any of the following circumstances:

(i) there is negotiation or discussion between the employer and the third party that results in no more than:

(A) the employer granting the third party access to the premises or work environment to discuss the benefit with employees; and/or

(B) agreement between the parties as to the level of benefit that is to be offered by the third party to employees; and/or

(C) the employer agreeing to advertise or make known the availability of the benefit; or

(ii) the employer has done no more than initiate contact or discussions with the third party; or

(iii) there is no significant contact between the employer and the third party.

## The period or tax year for which this Ruling applies

This Ruling will apply for an indefinite period beginning on the first day of the 2014/2015 income year.

This Ruling is signed by me on 28 November 2014.

**Susan Price**
Director, Public Rulings

**COMMENTARY ON PUBLIC RULING BR PUB 14/10**

This commentary is not a legally binding statement. The commentary is intended to help readers understand and apply the conclusions reached in Public Ruling BR Pub 14/10 (the Ruling).

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

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## Summary

1. A benefit will be treated as having been provided to an employee under s CX 2(2) where an "arrangement" is made between their employer and another person "for" the "benefit" to be "provided".

2. "Arrangement" is defined in s YA 1 and encompasses various degrees of formality and enforceability. An "arrangement" may be a legally enforceable contract, a less formal agreement or plan, or an informal, unenforceable understanding. An "arrangement" may exist even if no consideration is given by the employer to the third party so as to create a legally binding contract.

3. Section CX 2(2) provides that the arrangement made between the employer and another party must be "for the benefit to be provided". These words mean that the arrangement must be made "for the purpose" or "with the object" of providing a benefit to an employee. This requires consideration of the purpose or object of the employer and third party in making the arrangement.

4. Where the employer and the third party have a different purpose or object in making the arrangement, s CX 2(2) will apply only if the employer's purpose or object in making the arrangement was to provide a benefit to an employee.

5. In determining the employer's purpose or object, the relevant consideration is the subjective purpose or object of the employer in making the "arrangement". For s CX 2(2) to apply, the employer must have, at least, a more than incidental purpose or object of providing a benefit to an employee in making the arrangement.

6. An employee-third party arrangement for a benefit to be provided does not prevent the same benefit being considered as having been provided through an employer-third party arrangement to which s CX 2(2) applies.

7. A "benefit" for s CX 2(2) purposes is an advantage that is sufficiently clear and definite that it can reasonably, practically and sensibly be understood as a tangible benefit.

8. For s CX 2(2) to apply, the benefit must have been "provided" to an employee by a third party. The word "provided" requires that the benefit must have been supplied, furnished or made available to the employee.

9. The Commissioner considers that these requirements will be met and s CX 2(2) will apply where:

   - consideration passes from the employer to the third party for the benefit being provided;
   - the employer requests (other than merely initiating contact), instructs or directs the third party to provide a benefit;
   - there is negotiation or discussion between the employer and the third party that (explicitly or implicitly) involves the threat or suggestion that the employer would withhold business or other benefits from the third party unless a benefit is provided to the employee; or
   - the third party and the employer are associated parties and there is a group policy (whether formal or informal), or any other agreement between the associated parties, that an employee of the group will be entitled to receive benefits from the other companies in the group.

10. Where the benefit has not been provided in circumstances within any of the categories identified above, s CX 2(2) will not apply where the benefit is provided in any of the following circumstances:

    - there is negotiation or discussion between the employer and the third party that results in no more than:
      - the employer granting the third party access to the premises or work environment to discuss the benefit with employees; and/or

- agreement between the parties as to the level of benefit that is to be offered by the third party to employees; and/or
- the employer agreeing to advertise or make known the availability of the benefit; or

- the employer has done no more than initiate contact or discussions with the third party; or
- there is no significant contact or arrangement between the employer and the third party.

11. A benefit may be provided in circumstances that fall within both of the above categories. In such cases, the Commissioner considers the requirements of s CX 2(2) have been satisfied. For example, if a benefit is provided in circumstances that come within the "requests …, instructs or directs" category in [9] above, s CX 2(2) applies even if it can be argued that those circumstances also come within the "agreement … as to the level of benefit that is to be offered" subcategory in [10].

12. A consequence of this Ruling may be that the employer is required to put into place systems to enable them to obtain the relevant information required to fulfil their fringe benefit tax (FBT) obligations. In the Commissioner's opinion, where the employer is involved in the types of arrangements contemplated in [9] above, the employer will generally have a sufficient relationship with the third party to obtain the information they require to fulfil their obligations. The onus is on employers who are involved in arrangements for the provision of benefits in any of these ways to ensure that they can comply with their obligations (for example, by requiring record keeping by the third party).

13. This Ruling does not consider or rule on the taxation implications of salary sacrifice situations. Different considerations may apply to determine the tax treatment. For example, the benefit may have been provided by the employer in such a situation, or there may be other relevant aspects of the arrangement. These considerations may affect whether or not s CX 2(2) will have any application.

## Background

14. BR Pub 14/10 is a reissue of BR Pub 09/07, which expired on the last day of the 2013/2014 income year. This Ruling is essentially the same as BR Pub 09/07. However, the analysis under the heading "What is the meaning of "benefit"?" has been amended to ensure consistency with other statements made by the Commissioner. The Commissioner considers that these changes do not affect the outcome of this Ruling.

15. This Ruling considers the scope of s CX 2(2) and what will be an "arrangement" that falls within the scope of that provision.

## Application of the Legislation

### Introduction

16. Under the Act, an employer may be liable to pay FBT on fringe benefits that it provides to an employee. "Fringe benefit" is defined in s CX 2(1) as follows:

> *Meaning*
>
> (1) A **fringe benefit** is a benefit that—

(a) is provided by an employer to an employee in connection with their employment; and

(b) either—

(i) arises in a way described in any of sections CX 6, CX 9, CX 10, or CX 12 to CX 16; or

(ii) is an unclassified benefit; and

(c) is not a benefit excluded from being a fringe benefit by any provision of this subpart.

17. This definition is broad and intended to include all non-cash payments made by an employer to an employee in connection with their employment.

18. As a rule, an employer will not be liable to pay FBT on a benefit provided to an employee by a third party. However, under s CX 2(2) an employer may be liable to pay FBT on a benefit provided to an employee by a third party if that benefit is provided through an "arrangement" made between the employer and the third party.

19. Section CX 2(2) provides:

*Arrangement to provide benefit*

(2) A benefit that is provided to an employee through an arrangement made between their employer and another person for the benefit to be provided is treated as having been provided by the employer.

20. Section CX 2(2) is an anti-avoidance provision. Its purpose is to prevent an employer avoiding a liability for FBT by arranging for a third party to provide a benefit to an employee in circumstances where FBT would have been payable had that benefit been provided by the employer directly. If s CX 2(2) applies, the benefit provided by the third party is treated as if it were provided by the employer to the employee directly. This enables the other provisions of subpart CX to be applied to determine whether FBT is payable on the benefit.

21. This Ruling considers only what will be an "arrangement" that comes within the scope of s CX 2(2). It does not consider whether FBT will be payable on a benefit that is provided through an arrangement to which s CX 2(2) applies. An arrangement may satisfy the requirements of s CX 2(2), but no FBT will be payable because of the other provisions of subpart CX or the operation of the valuation rules in subpart RD.

## Issue

22. A benefit will be treated as having been provided by an employer to an employee under s CX 2(2) where an "arrangement" is made between the employer and another person "for" the "benefit" to be "provided".

23. The wording of s CX 2(2) is broad and would apply where any form of consideration passes from an employer to a third party to compensate for the third party providing a benefit to an employee. However, where there is no direct or indirect consideration (in any form) provided by the employer to the third party, the issue is in what circumstances the provision will apply.

24. In considering this issue, the analysis below will consider:

- What is meant by "arrangement"?
- What is the meaning of "for"?
  - Is it the purpose of the arrangement or purpose of the parties?

- Which party's purpose is relevant?
- Is it an objective or subjective test?
- Which purpose test should be applied?
- Can s CX 2(2) apply where there is an employee–third party arrangement?

- What is the meaning of "benefit"?
- What is the meaning of "provided"?

**What is meant by "arrangement"?**

25. "Arrangement" is defined in s YA 1 as follows:

> **arrangement** means an agreement, contract, plan, or understanding, whether enforceable or unenforceable, including all steps and transactions by which it is carried into effect

26. This definition makes it clear that "arrangement" is very wide in its application, and that it encompasses not only legally binding contracts, but also unenforceable understandings. It is clear that what is required for an arrangement to exist is less than that required for a binding contract.

27. The *Concise Oxford English Dictionary* (12th ed, Oxford University Press, New York, 2011) defines the individual words contained in the s YA 1 definition as follows:

- "Agreement" – a negotiated and typically legally binding arrangement.
- "Contract" – a written or spoken agreement intended to be enforceable by law.
- "Plan" – a detailed proposal for doing or achieving something.
- "Understanding" – an informal or unspoken agreement or arrangement.

28. The above definitions show that the words used to describe an "arrangement" in s YA 1 all appear to be slightly different concepts.

29. The courts have not considered the definition of "arrangement" in the context of s CX 2(2), nor have they considered the application of s CX 2(2) in its entirety. However, the courts have considered the definition of "arrangement" contained in s YA 1 in the context of the general anti-avoidance rule in s BG 1.

30. The predecessor to the s YA 1 definition was discussed by Richardson P in *CIR v BNZ Investments Ltd* (2001) 20 NZTC 17,103 (CA). His Honour considered the definition of "arrangement" in s 99(1) of the Income Tax Act 1976 at [45] as follows:

> The words contract, agreement, plan and understanding appear to be in descending order of formality. A contract is more formal than an agreement, and in ordinary usage is usually written while an agreement is generally more formal than a plan, and a plan more formal or more structured than an understanding. And it is accepted in the definition of arrangement that the contract, agreement, plan or understanding need not be enforceable. Section 99 thus contemplates arrangements which are binding only in honour.

31. Richardson P cited with approval the statement by the High Court of Australia in *Bell v FCT* (1953) 87 CLR 548, 573 that "arrangement" in an

earlier Australian general anti avoidance provision extended beyond contracts and agreements "so as to embrace all kinds of concerted action by which persons may arrange their affairs for a particular purpose or so as to produce a particular effect" (at [46]). His Honour noted that statements to similar effect were made in *Newton v Commissioner of Taxation* [1958] AC 450, 465 (PC), where Lord Denning stated that the word "arrangement" under the then Australian general anti-avoidance provision:

> …is apt to describe something less than a binding contract or agreement, something in the nature of an understanding between two or more persons – a plan arranged between them which may not be enforceable at law.

32. The definition of "arrangement" in s 99(1) of the 1976 Act, considered by Richardson P in *BNZ Investments*, differs from the definition of "arrangement" in s YA 1. The order of the words has been changed to be listed alphabetically in the 2007 Act (ie, "agreement" precedes "contract"). Despite this, the same observation can be made that the inclusion of the words "agreement, contract, plan, or understanding" mean that "arrangement" provides for varying degrees of enforceability and formality. As defined in s YA 1, an "arrangement" may be a legally enforceable contract, a less formal agreement or plan that may or may not be legally enforceable, or an informal, unenforceable understanding. Accordingly, "arrangement" is defined widely to include all kinds of concerted action by which persons seek to bring about the fulfilment of a particular purpose or the production of a particular effect. It includes agreements, contracts, plans or understandings that are not intended to be legally binding, and arrangements that are unenforceable at law, for example, contracts unenforceable due to reasons of public policy, contractual incapacity or illegality.

33. In the context of s BG 1, the courts have considered whether "arrangement" requires a consensus or meeting of minds. This issue was considered by the Court of Appeal in *BNZ Investments*. In that decision, Thomas J dissented, holding that no such requirement existed. His Honour held that "arrangement" does not require that one party knew of, or agreed to, all the steps and transactions undertaken by the other party to discharge its obligations under the "agreement, contract, plan or understanding". Thomas J's approach was later endorsed by the majority of the Privy Council in *Peterson v CIR* (2005) 22 NZTC 19,098 (at [34]).

34. However, in s CX 2(2), an "arrangement" is qualified by the words "made between their employer and another person for the benefit to be provided". As will be discussed, these words mean that s CX 2(2) applies only if the employer's purpose or object in making the arrangement is for a benefit to be provided to an employee (see [66]–[71] below). For this purpose or object to exist, the employer must have authorised the third party to provide a benefit to an employee.

35. The case law on the meaning of "arrangement" as used in commerce-related legislation (for example, the Commerce Act 1986) is also useful. This case law makes clear the following:

- An "arrangement" exists where each party intentionally creates in the other party an expectation that the first party will act in a certain way. In so doing, the parties agree to mutual rights and obligations in respect of the course of action to be undertaken.
- An "arrangement" is unlikely to exist when only one party makes a commitment to the proposed course of action.

(See *Apple Fields Ltd v New Zealand Apple and Pear Marketing Board* [1991] 1 NZLR 257 (PC); *Re British Basic Slag Ltd's Agreements* [1963] 2 All ER 807 (CA); *Trade Practices Commission v Email Ltd* (1980) 31 ALR 53 (FCA)).

36. In the context of s CX 2(2), "arrangement" will include situations where the employer arranges with the third party to provide a benefit, where the employer agrees to allow the third party to approach an employee, or where the employer agrees to allow an employee to join a scheme promoted by the third party. Where this type of significant contact does not occur, the parties will not have entered into an arrangement for the purposes of s CX 2(2).

37. However, for an "arrangement" to be caught under s CX 2(2), it must be an arrangement "for" a benefit to be "provided" to an employee. This means that not every "arrangement" that exists between an employer and a third party will be caught by s CX 2(2). Similarly, not every instance where a benefit is provided to an employee by a person who is not their employer will be caught by the section.

**What is the meaning of "for"?**

38. Section CX 2(2) provides that the "arrangement" made between the employer and another party be "for" the benefit to be provided.

39. The word "for" can have a wide variety of meanings depending on its context. The Court of Appeal in *Wilson & Horton v CIR* (1995) 17 NZTC 12,325 stated at 12,330:

> Reference to any standard dictionary brings home the wide variety of senses in which the preposition "for" may be employed. The *Oxford English Dictionary* (2nd ed) identifies 11 separate categories of meaning and many distinct usages within particular categories. The discussion in the text extends over 9 columns in the dictionary. Again the *Tasman Dictionary,* which as its name suggests is directed to Australian English and New Zealand English, lists 33 meanings of the word. **The particular meaning intended necessarily hinges on the context in which the word is used and how it is used in that context**. [Emphasis added.]

40. The use of the word "for" was interpreted in *Patrick Harrison & Co v AG for Manitoba* [1967] SCR 274 (CASCC) as imposing a purpose test. In this case, the court held that "for the extraction of minerals" meant "with the object or purpose of extracting minerals".

41. In *G v CIR* [1961] NZLR 994 (SC), McCarthy J held that the word "for" points to intention, which is similar to looking at a person's purpose. McCarthy J stated at 999:

> "For" points to intention … the essential test as to whether a business exists is the intention of the taxpayer as evidenced by his conduct, and that the various tests discussed in the decided cases are merely tests to ascertain the existence of that intention. I think that it conforms with this approach to construe the word "for", when considering a phrase such as "carried on for pecuniary profit" used in relation to an occupation, as importing intention.

42. These cases show that in several statutory contexts the courts have interpreted "for" to mean "for the purpose" or "with the object of" something. It is noted that, in this context, a person's purpose is similar to their intention. However, to determine the meaning of "for" in s CX 2(2), the rest of the wording must be looked at.

43. As already noted, s CX 2(2) requires the benefit to be provided to the employee through an arrangement made between the employer and another person "for" the benefit to be provided. The use of "for" in this

context can mean that the "arrangement" must have been made "for" the provision of a benefit to an employee.

44. In the Commissioner's opinion, based on the case law and dictionary definitions, an "arrangement" will satisfy s CX 2(2) if it is made "for the purpose" or "with the object" of providing such a benefit to an employee.

***Purpose of the arrangement or purpose of the parties?***

45. Given that the words "for the benefit to be provided" mean for the purpose or with the object of providing the benefit, the issue arises as to who or what must have this purpose or object. This requires interpreting the words "an arrangement made between their employer and another person for the benefit to be provided".

46. There are two possible interpretations of these words:

- First, "for the benefit to be provided" could be read as relating to the word "arrangement". Under this interpretation, s CX 2(2) applies if the **arrangement** has the purpose or object of providing a benefit to an employee of the employer. This would require an objective inquiry into the arrangement itself, and would not consider the purpose or object of the parties to the arrangement.
- Second, "for the benefit to be provided" could be read as relating to the word "made". Under this interpretation, s CX 2(2) applies if the purpose or object of **the parties in making the arrangement** was for a benefit to be provided to an employee of the employer.

47. Under the first interpretation, s CX 2(2) could have a wider scope than under the second interpretation. It could be possible that, objectively, an arrangement has the purpose or object of providing an employee of the employer with a benefit in circumstances where, subjectively, the parties did not make the arrangement for the purpose or object of providing a benefit to an employee.

48. The meaning of a section must be determined from its text and in the light of its purpose (s 5, Interpretation Act 1999). In determining purpose, the immediate and general legislative context must be considered, as well as the objective of the enactment (*Commerce Commission v Fonterra Co-operative Group Ltd* [2007] NZSC 36). Therefore, the purpose of s CX 2(2) must be considered to determine the best interpretation.

49. An argument favouring the first interpretation of s CX 2(2) above, is that this interpretation is consistent with s BG 1. Under s BG 1, only the objective purpose or effect of the "arrangement", and not the intention of the parties to the arrangement, is relevant to whether there is a "tax avoidance arrangement" (*Newton v FCT*; *Glenharrow Holdings Ltd v CIR* [2008] NZSC 116; *Ben Nevis Forestry Ventures v CIR, Accent Management v CIR* [2008] NZSC 115). Arguably, it is appropriate that s CX 2(2) is interpreted consistently with s BG 1, given they both have an anti-avoidance purpose and share the same definition of "arrangement".

50. However, the second interpretation, requiring consideration of the purpose or object of the parties, could be seen as consistent with the FBT rules. The FBT rules apply where there is a "fringe benefit", which is defined in s CX 2(1)(a) as being a benefit that "is provided by an employer to an employee in connection with their employment". This indicates that the focus of the FBT rules is on benefits that the employer has chosen to give its employees. Understood in this way, the purpose of s CX 2(2) appears to be to prevent employers from deliberately avoiding a

liability for FBT by arranging for a third party to provide the benefit instead.

51. The second interpretation is not inconsistent with s BG 1. Unlike s CX 2(2), the wording in s BG 1 is unambiguous in requiring consideration of the purpose or effect of the arrangement.

52. Moreover, the first interpretation, requiring consideration of the purpose or object of the arrangement, arguably creates the potential for overlap with s GB 31. Section GB 31 provides an anti-avoidance rule that applies when "a purpose or effect of the arrangement [entered into by two or more persons] is to defeat the intent and application of any of the FBT rules". Section CX 2(5)(a) provides that a benefit may be treated as having been provided by an employer to an employee under s GB 31.

53. Section GB 31(1) is clear that it concerns the purpose or effect of the arrangement and not the purpose or object of the parties to the arrangement. If the drafters had intended the purpose or object of the arrangement to be relevant under s CX 2(2), it would be reasonable to expect that the drafters would have adopted language similar to that used in ss BG 1 and GB 31.

54. The background to s 336N(2) of the Income Tax Act 1976, the earliest predecessor to s CX 2(2), also provides some assistance in understanding the purpose of s CX 2(2) and the FBT rules generally.

55. The FBT rules were enacted in light of the recommendations in the *Report of the Task Force on Tax Reform* (Wellington, Government Printer, 1982) (the McCaw report). Before the enactment of the FBT rules, fringe benefits were generally not taxed. The McCaw report considered that the non-taxable status of fringe benefits was unsatisfactory because it increased the inequity in the tax system and narrowed the tax base (at [6.185]).

56. In the third reading debate of the Income Tax Amendment Bill (No 2), which introduced the FBT rules, the Minister of Finance stated that the purpose of fringe benefit tax was to "close … off loopholes that are a major source of unfairness in income distribution", and that ((22 March 1985) 462 NZPD 3920):

> In the Government's view it is fair to tax the employers, the basic reason being that it is the employers which have been using fringe benefit payments to lower the cost structures of their business. I gave the example in the Committee of an employer who might want to put together a package of $100,000. He could pay $40,000 in terms of salary, then put together a fringe benefit package of about $20,000 in various forms, which was the equivalent of tax paid income of $60,000. In other words, for $60,000 in terms of cost structure to the business the employer was able to put together a salary package equivalent of $100,000. In those circumstances the Government believes it is fair and equitable to tax the employer.

57. The Minister of Finance's speech indicates that the mischief Parliament sought to remedy by enacting the FBT rules was the ability of employers to decrease the costs of employment by substituting assessable income with non-assessable fringe benefits. While the Minister did not specifically discuss the clause of the Bill that became s 336N(2) of the Income Tax Act 1976, his comments suggest that s 336N(2) was intended to cover the specific situation of an employer that knowingly seeks to avoid a liability for FBT by arranging for a benefit to be provided to an employee by a third party.

58. Therefore, the Commissioner's view is that the scheme of the FBT rules and the legislative history suggest that s CX 2(2) requires the

determination of the purpose or object of the parties (that is, the employer and the third party) in making the arrangement.

### *Which party's purpose?*

59. It is the parties' purpose or object in making the arrangement that is relevant. Where both the employer and third party share the same purpose, then determining whether s CX 2(2) applies will be straightforward. However, in some situations the employer and third party may each have a different purpose or object in making the arrangement.

60. For example, where the third party agrees to provide the benefit because the employer has stated it will withhold business from the third party unless it does so, arguably the third party has not made the arrangement for the purpose or with the object of providing a benefit to an employee. Instead, the third party arguably made the arrangement for the purpose or with the object of preserving its business with the employer. The issue then arises as to whose purpose should be considered determinative when deciding whether s CX 2(2) applies.

61. The Commissioner's view is that the scheme of the FBT rules supports the employer's purpose being determinative in these situations.

62. A liability for FBT is imposed on benefits provided by employers to their employees. The FBT rules are not, as a rule, concerned with benefits provided to employees by persons who are not their employers. Section CX 2(2) is an exception to this rule. Section CX 2(2) has an anti-avoidance purpose. It seeks to prevent employers from avoiding a liability for FBT by arranging for third parties to provide benefits to their employees.

63. The scheme of the FBT rules supports s CX 2(2) applying where the employer, but not the third party, makes the arrangement with the purpose of providing a benefit to an employee. In such cases, a liability for FBT is avoided where it would have arisen if the benefit had instead been provided by the employer directly. Moreover, the third party is not seeking to avoid its liability for FBT, because it has no liability. At most, the third party might be a knowing participant in the employer's arrangement. More likely, perhaps, the third party would be pursuing their own commercial non-tax objectives and may be ignorant of, or indifferent to, the employer's purpose.

64. By contrast, the scheme of the FBT rules does not support s CX 2(2) applying where the third party, but not the employer, makes the arrangement with the purpose of providing a benefit to an employee. If s CX 2(2) were to apply in such cases because of the third party's purpose, then FBT would be imposed despite the employer not having the purpose of providing a benefit to its employee. The imposition of FBT in these circumstances seems unfair and illogical.

65. In summary, where the employer and the third party each have a different purpose or object in making the arrangement, s CX 2(2) will apply only if the employer's purpose or object in making the arrangement was to provide a benefit to an employee.

### *Objective or subjective test?*

66. The above conclusions combine to show that, for an "arrangement" to be caught under s CX 2(2), the purpose or object of the employer must have

been to provide the employee with a benefit. This part of the commentary considers whether the test should be a subjective or an objective one.

67. In the current context, a subjective test would look at what the particular employer had in mind when the arrangement with the third party was entered into. An objective test, however, would consider what a reasonable person in the position of the employer should have had in mind.

68. Case law, particularly in the area of GST, indicates that the correct test for determining purpose is a mixed test, considering both subjective and objective factors in reaching a conclusion as to a taxpayer's purpose. In several cases, the courts have held that the test for purpose is dependent on the statutory context in which it is found (see, for example, *CIR v Haenga* (1985) 7 NZTC 5,198 (CA)).

69. Therefore, the wording of s CX 2(2) must be looked at closely. Section CX 2(2) does not contain the word "purpose" or "object". It requires that the "arrangement" be "made between" the employer and the third party "for the benefit to be provided".

70. The Commissioner's view is that s CX 2(2) requires a consideration of the reason the employer "made" the "arrangement" with the third party. This means the test to determine the employer's purpose or object in making the arrangement should be subjective, looking at the particular reasons the employer had in mind (see, for example, *G v CIR*). However, the employer's reasons should be tested in light of the surrounding circumstances (*CIR v National Distributors Ltd* (1989) 11 NZTC 6,346 (CA)).

71. For s CX 2(2) to apply, therefore, the reason the employer made the arrangement must have been to provide a benefit to its employee.

### *Which purpose test should be applied?*

72. A number of tests could be used to determine the purpose or object of the employer in making the arrangement with the third party.

73. At one end of the spectrum is a sole purpose test. This test requires that the provision of a benefit to an employee is the sole or only purpose of the employer in making the arrangement. The Commissioner considers this would be an unduly restrictive test for s CX 2(2) because it would not apply in any situation where another purpose existed, no matter how secondary or minor.

74. At the other end of the spectrum, is the test that the section will apply if any one of the purposes of the employer in making the arrangement is that the employee be provided with a benefit. The Commissioner considers this is also an inappropriate test in the context of s CX 2(2). This is because the section would catch all benefits that were provided to employees even if the employer had only an incidental relevant purpose. If the provision of the benefit is truly incidental to the purpose of the employer, then the section should not apply.

75. Between these two extremes are the dominant purpose test and the more than incidental purpose test.

76. The dominant purpose test would require that the main reason the employer made the arrangement with the third party was for the benefit to be provided to the employee. This test would allow the employer to have other purposes in making the arrangement but, for the section to

apply, the main purpose of the employer in making the "arrangement" needs to be the provision of the benefit.

77. Several cases have determined that the word "purpose" used on its own in statutory language without any apparent qualifier means the dominant purpose of the taxpayer; for example, in s CB 4 (Personal property acquired for the purpose of disposal) (and predecessor provisions) and in s 108 of the Land and Income Tax Act 1954 (the former s BG 1).

78. The Commissioner considers it would not be appropriate to apply a dominant purpose test in determining whether s CX 2(2) applies. The words of s CX 2(2) do not indicate that a dominant purpose test is necessary. This can be contrasted with s CB 4, where the section clearly refers to "**the** purpose" [Emphasis added].

79. The final option is a more than incidental purpose test. This test would be similar to the test applied for s BG 1, where the section will apply as long as the purpose of tax avoidance is more than merely incidental to any other purpose in entering the arrangement. In the context of s CX 2(2), this means that if the provision of the benefit is incidental to other purposes of the "arrangement", such as the provision of credit cards to employees or obtaining a good package deal for the employer, then the section would not apply.

80. The use of this test could be seen as supported by s CX 2(2) being an anti-avoidance provision and it being appropriate to have a similar test to other avoidance provisions. Alternatively, it could be argued that a more than incidental test is not appropriate, because the language of s BG 1 explicitly provides for the test of more than merely incidental in the legislation itself, whereas s CX 2(2) does not.

81. Overall, the Commissioner considers that the more than incidental test is the appropriate test to be adopted in s CX 2(2). A more than incidental test means that the purpose of the employer must be significant in order for the benefit to be caught within the section, but does not need to be the most important (or dominant) reason or purpose of the employer in making the "arrangement".

82. If an employer has more than one purpose when they made the "arrangement" with the third party, a significant, but not dominant, purpose of providing a benefit to employees should be caught by the section. If, however, the provision of a benefit is no more than incidental to some other purpose of the employer in making the arrangement with the third party, then s CX 2(2) will not apply.

83. In determining the employer's purpose or object, therefore, the relevant consideration is the subjective purpose or object of the employer in making the "arrangement". For s CX 2(2) to apply, the employer must have, at least, a more than incidental purpose or object of providing a benefit to an employee in making the arrangement.

### *Can s CX 2(2) apply where there is an employee–third party arrangement?*

84. In some cases, where a benefit is provided to an employee by a third party, it might be argued that there are two arrangements "for" that benefit to be provided – one arrangement between the employer and third party and another between the employee and third party. In such cases, the issue may arise whether the presence of an arrangement between the employee and third party for the provision of a benefit means that same

benefit cannot have been provided under an arrangement between the employer and third party.

85. For instance, an employer makes an arrangement with a local gym under which the gym agrees to provide free membership to the employer's employees. To obtain this free membership, employees must undertake the gym's membership process (including agreeing to its standard terms and conditions of use). In this situation, it might be argued that s CX 2(2) cannot apply because the gym membership has been provided through an arrangement between the gym and the employee and, therefore, not through the arrangement between the employer and the gym.

86. The Commissioner's view is that an employee-third party arrangement for a benefit to be provided does not prevent the same benefit from being provided through an employer-third party arrangement to which s CX 2(2) applies. Section CX 2(2) does not expressly or implicitly exclude itself from applying because the benefit concerned may also have been provided through an employee-third party arrangement. Accordingly, s CX 2(2) may apply even if the benefit may also have been provided through an employee-third party arrangement.

### What is the meaning of "benefit"?

87. As noted above, a fringe benefit is defined in s CX 2(1) as "a benefit that… is provided by an employer to an employee in connection with their employment".

88. The term "benefit" is not defined in the Act. Therefore, the ordinary meaning of the word must be considered. The *Concise Oxford Dictionary* relevantly defines the word "benefit" to mean "an advantage or profit gained from something." The meaning of "benefit" is, therefore, very wide.

89. In *Case M9* (1990) 12 NZTC 2,069, Bathgate DCJ considered the meaning of the word "benefit" when considering whether the provision of a motor vehicle was subject to FBT. He stated at 2,074:

> A feature of the definition of "fringe benefit" is the rather involved detail used to specify what is a fringe benefit and what is not a fringe benefit, particularly the latter. A "fringe benefit" is however a "benefit", including the availability for the private use or enjoyment of any person of a motor vehicle, as defined. **The section itself to an extent explains what is a benefit, for the purposes of a fringe benefit; so long as something is provided by an employer to an employee that can be reasonably, practically and sensibly understood as a benefit to the employee in itself and is not expressly excluded, would be sufficient for it to be a benefit for the purposes of the definition of "fringe benefit"** as provided by the section. [Emphasis added]

90. While the legislative provision considered in *Case M9* was a predecessor to s CX 2, the principles remain relevant as the definition of "fringe benefit" still requires that a benefit be provided by an employer to an employee.

91. Based on *Case M9*, a "benefit" is something provided by an employer that can be "reasonably, practically and sensibly understood as a benefit to the employee". Whether a fringe benefit is provided does not depend on whether employees consider that they have received an advantage or benefit. This conclusion is consistent with the analysis on the meaning of "benefit" in QB 12/06 "Fringe benefit tax – 'Availability' benefits" (*Tax Information Bulletin* Vol 24, No 4 (May 2012): 32).

92. Further assistance as to the meaning of the term "benefit" can be obtained from a review of the purpose of the FBT rules. The purpose of the rules can be ascertained from the McCaw report which recommended the introduction of FBT.

93. In setting out the case for taxing fringe benefits, the report states at [6.181] to [6.182]:

> Fringe benefits do not, under existing legislation, generally represent assessable income of the recipient. Some benefits provided in kind, such as accommodation and food, are assessable in terms of the existing tax law. The courts have held that other benefits provided in kind are not assessable unless they can be converted into cash by the recipient. Cash payments are assessable except to the extent that they can be demonstrated to be reimbursement of expenses incurred in gaining or producing assessable income. The Task Force does not consider that such reimbursement allowances constitute a fringe benefit and therefore does not propose any change to the current tax exempt status.
>
> …
>
> **Fringe benefits that reduce an employee's need to meet private outgoings from income clearly increase a taxpayer's capacity to pay in just the same way as does the payment of additional salary or wages in cash**. Those who receive part of their remuneration in this form do not bear their fair share of the tax burden. Furthermore employers who provide non-taxable benefits in lieu of salary or wages are in a favoured position as their total labour cost is reduced.

94. From this, it can be seen that fringe benefits are benefits that provide an economic advantage to an employee because they reduce an employee's need to meet private expenditure from their income. In economic terms, benefits of this type are equivalent to the payment of additional salary or wages in money to the employee.

95. The meaning of "benefit" was also considered in *Case M59* (1990) 12 NZTC 2,339. In *Case M59* Bathgate DCJ stated at 2,343:

> The fringe benefit by way of the provision of the overseas travel and accommodation was provided by the objectors as the employers before 1 April 1985, when they paid the costs of the employees' proposed travel with the travel agents or firms consulted by the employees. Although that benefit may not have been used or enjoyed by the employees until after 1 April 1985, that was not, in my view, a "fringe benefit", because **a fringe benefit as defined by the Act requires two steps and not just one, namely the provision of the benefit by the employer and the use or enjoyment of the benefit by the employee**. The enjoyment of the fact of travel by the employees may well be a benefit, but without the provision of that by the employer it is not a "fringe benefit" for FBT purposes. [Emphasis added]

96. However, *Case M59* was considered in the context of the language used in the Income Tax Act 1976, which defined "fringe benefit" as a "benefit that is used, enjoyed, or received …". The rewritten definition of "fringe benefit" does not include any element of use or enjoyment (by the employee of the benefit provided). In terms of the rewritten definition, all that is required is that the employer has provided a benefit to an employee.

97. Given that s CX 2(2) is an anti-avoidance provision, and essentially treats a benefit provided by a third party to be a fringe benefit provided by an employer, a further issue exists as to whether what the employee receives from the third party needs to be a benefit that the public is unable to receive.

98. The Commissioner considers that, given the conclusion as to the broad meaning of the term "benefit", a fringe benefit can include something the employee could receive on their own account, or that the public could

receive. This conclusion is consistent with "The meaning of 'benefit' for FBT purposes" (*Tax Information Bulletin* Vol 18, No 2 (March 2006): 26), which considers whether an employer provides a benefit where an employee pays for goods or services obtained from their employer, or where the employer also benefits from the employee's receipt of the goods or services.

### What is the meaning of "provided"?

99. Section CX 2(2) requires that a benefit be "provided to an employee through an arrangement". For a benefit to be caught under s CX 2(2), the third party must provide it to the employee. An "arrangement" between the parties for access to the employees is insufficient. The "arrangement" must be for the "provision" of a benefit for s CX 2(2) to apply.

100. The *Concise Oxford English Dictionary* defines the term "provide" as "make available for use; supply".

101. Several cases have discussed the meaning of the word "provide". These cases show that the meaning of "provide" depends on the facts and circumstances of each case (see for example *Ginty v Belmont Building Supplies Ltd* [1959] 1 All ER 414 (QBD) at 422).

102. In *Norris v Syndi Manufacturing Co Ltd* [1952] 1 All ER 935 (CA), an employee had removed the safety guard from a machine to carry out tests. His employer was aware that the employee took the guard off to test the machine and had told him to replace it "after testing and before operation". The employee inadvertently injured himself while working without the guard one day. The Court of Appeal found that the guard had been "provided" by the employer, and that the duty to provide the guard did not require that the employer should have to order the workers to use it. Romer LJ stated at 940:

> **The primary meaning of the word "provide" is to "furnish" or "supply",** and, accordingly, on the plain, ordinary interpretation of s. 119 (1), a workman's statutory obligation is to use safety devices which are furnished or supplied for his use by his employers. [Emphasis added]

103. See also *Tranz Rail Ltd (TIA Interisland Line) v New Zealand Seafarers' Union* [1996] 1 ERNZ 216 (EC), and *Pierce v FCT* 98 ATC 2240 (AAAT).

104. Accordingly, for something to have been "provided" to an employee by a third party in the context of s CX 2(2), it must be supplied, furnished, or made available to that employee.

### Salary sacrifice situations

105. This Ruling does not consider or rule on the taxation implications of salary sacrifice situations. Different considerations may apply to determine the tax treatment. For example, the benefit may have been provided by the employer in such a situation, or there may be other relevant aspects of the arrangement. These considerations may affect whether or not s CX 2(2) will have any application.

106. In the context of the Ruling, salary sacrifice situations include situations where the remuneration given by an employer to an employee is reduced because of a benefit being received by the employee from a third party (or because of the possibility of a benefit being received), or where the remuneration of the employee otherwise takes the receipt of a benefit provided by a third party into account.

## Examples

107. The following examples are included to assist in explaining the application of the law. They consider whether the requirements of s CX 2(2) are satisfied. The examples do not consider whether FBT will be payable on a benefit provided through an arrangement to which s CX 2(2) applies. Section CX 2(2) may apply but FBT will not be payable because of the other provisions in subpart CX or the operation of the valuation rules contained in subpart RD.

108. These examples all assume that there has been no sacrifice of salary by the employee receiving the benefit.

### Example 1

109. ABC Bank wishes to offer the employees of XYZ Ltd a low interest loan facility. ABC approaches XYZ, which agrees to ABC's offer and agrees to pay ABC the difference between the interest rate offered to employees and the current market interest rate.

110. On the facts of this example, the requirements of s CX 2(2) are clearly satisfied. An "arrangement" exists between ABC and XYZ, and the purpose of the employer in making the arrangement is for the provision of a benefit to XYZ's employees. This is evidenced by the fact consideration has been passed between the employer and the third party for the benefit being provided.

### Example 2

111. A credit card company approaches the manager of BCE Ltd, and asks whether BCE would allow it to approach BCE's employees to offer them credit cards (for the employees' personal use). The credit card company proposes that all staff members who choose to receive cards would be allowed to join the credit card company's loyalty scheme (which has no joining fee, but is available only to selected cardholders). BCE agrees to this request, but suggests that the credit card company might wish to provide a slightly discounted interest rate to the employees, so that the offer does not waste the employees' time. The credit card company agrees to this change. BCE provides no consideration to the credit card company. The credit card company is keen to secure BCE employees as customers and is happy to agree to offer the employees the additional benefits.

112. In this example, there is an "arrangement" between the employer and the third party. BCE and the credit card company have agreed to the credit card company undertaking a particular course of action. However, s CX 2(2) will not apply in this situation. The agreement does not include the provision of a benefit, but merely allows the credit card company access to BCE's employees to offer them a benefit. The main purpose of BCE in entering into the arrangement is to allow the credit card company to offer a benefit to BCE's employees that will be of potential interest to the employees. The provision of a benefit, if it is a purpose of BCE, will be incidental to this. Therefore, s CX 2(2) will not apply to this arrangement.

### Example 3

113. A local retailer approaches MNO Ltd and asks permission to display advertising brochures on MNO's premises and for MNO to place an advertisement on the company's intranet. After a cursory inspection of

the brochures and advertisement, MNO agrees. MNO also agrees to allow the retailer to email interested staff with updated specials (staff are given the opportunity not to receive the email updates). The brochures and subsequent email messages invite the employees to join a loyalty programme, which gives them the possibility of receiving rewards.

114. In this example, there will be an "arrangement" between MNO and the local retailer, as they have agreed on a future course of action. However, the arrangement will not be "for" the provision of a benefit. MNO has agreed only to allow the local retailer access to its employees, and this is its main purpose in entering into the arrangement. Any purpose MNO may have of benefiting its employees is incidental to this purpose. The "arrangement" is "for" access to MNO's premises or to allow the local retailer to communicate with the employees directly or by electronic means, not to provide a benefit to employees. Therefore, s CX 2(2) will not apply to this arrangement.

**Example 4**

115. BB Ltd is a large company with several high net worth employees. BB contacts its bank and asks the bank to offer a low interest mortgage facility to BB's employees, which would also permit employees to obtain a mortgage with a smaller deposit than would usually be required. BB believes the bank will agree to this request because BB has a lot of business with the bank. Additionally, it is expected that the bank will get a great deal of business from the employees of BB, because BB has told the bank it is aware of a reasonable number of staff members who would be interested in such a facility. The bank is attracted by the level of business it might achieve with the employees and is also keen to maintain the good relationship it has with BB, so it puts together a proposal, which it presents to BB. BB considers that the proposal is worthwhile, so asks the bank to make the facility available to employees. BB also agrees to help promote the facility by putting up posters and making brochures available in the workplace, and by sending an email message to staff informing them of the facility.

116. In this example, there is an "arrangement" between BB and the bank that is "for" the provision of a benefit to employees. The course of action agreed to by the parties involves the provision of a benefit to employees. BB has not simply entered into the arrangement with the purpose of allowing the bank access to the employees. Rather, BB has entered into the arrangement with a more than incidental purpose of providing employees with a benefit. This is evidenced by the fact BB has an expectation that the bank would comply with its request and because it is aware of staff members who would be interested in the facility. Therefore, s CX 2(2) will apply to this arrangement.

**Example 5**

117. STU Ltd and VWX Ltd are companies in the same group of companies. The group has a widely understood policy that all companies in the group will provide discounted products or services to all employees of companies in the group, although this policy has never been put into writing. STU, therefore, provides interested VWX employees with discounts on its products.

118. In this example, there will be an "arrangement" for the provision of a benefit, and VWX will be liable to FBT on any benefits received by its employees from STU. There is a group policy that each company will

provide the employees of the other companies in the group with benefits. Therefore, there is an understanding between VWX and STU that each will act in a particular way, that understanding extending to the provision of a benefit, and the purpose of the policy is to allow employees to be provided with benefits by STU. Therefore, s CX 2(2) will apply to this arrangement.

**Example 6**

119. DFG, a travel agent, employs several staff and enters into a scheme with YTR, an airline, to strengthen its relationship with YTR. The scheme involves YTR agreeing to give a certain number of free domestic flights per year to employees of DFG who excel in promoting and selling YTR flights. In return, DFG agrees to have its employees promote YTR flights and convert flights to YTR wherever possible. To determine which employees are entitled to free flights, DFG awards its staff with points for outstanding customer service. Once a staff member has accumulated the required number of points, they are entitled to a free flight from YTR. There is no cost to DFG for those flights.

120. In this example, s CX 2(2) will apply. There is an "arrangement" between the parties, as the course of action agreed to by DFG and YTR involves the provision of a benefit to employees. One of the main purposes of DFG in entering into the arrangement is to provide the staff with free flights. Although DFG has another significant purpose in entering into the arrangement, which is to strengthen its relationship with YTR, the purpose of providing a benefit to employees is not incidental to that purpose.

**Example 7**

121. HJK is a large nationwide employer with many staff. A senior manager of HJK approaches LMN, a nationwide chain of retail stores, and suggests that LMN might like to consider offering a discount to HJK employees. LMN agrees to consider this idea and decides to allow a 10% discount to all HJK staff at all of its stores. This is achieved by providing all employees with a discount card. HJK does not give any consideration for this, has made no suggestion that it will do business with LMN if a discount is permitted, and has not been involved in discussions about the level of the discount or any other details of the offer. LMN has decided to offer the employees the discount because it believes LMN will obtain a substantial amount of business.

122. Section CX 2(2) will not apply in this situation. There is no "arrangement" between the parties that encompasses the provision of the benefit, as the only course of action agreed to by the parties is that LMN will consider the idea. HJK has done no more than initiate discussions with LMN, and the decision to offer a benefit to employees was made unilaterally by LMN. Although the purpose of HJK could be argued to be the provision of a benefit, there is no "arrangement" with LMN that is "for" such provision.

**Example 8**

123. An employee works for a company. She obtains a personal credit card and joins its associated points reward scheme. Under that scheme, she can accumulate points as goods and services are charged on the credit card. After the employee accumulates 10,000 points, she can transfer those points, at her option, to any one of several airlines' frequent flyer schemes affiliated to the credit card company's points reward scheme. Once she accumulates a specified number of points on the airline frequent flyer scheme, she can exchange them for free or discounted travel.

124. In the course of the employee's work, she incurs several employment-related charges on the credit card as well as private expenditure. The employee accumulates points on the credit card points reward scheme for both types of expenditure. She soon reaches the specified threshold of points and transfers them to a particular airline's frequent flyer scheme, exchanging them for a free trip to Fiji.

125. Section CX 2(2) will not apply on the facts of this example. The receipt of the points under the credit card company's points reward scheme is because of the contractual arrangement between the credit card company and the employee. There has been no significant contact between the employer and the credit card company. No arrangement exists between the employer and the credit card company to provide the employee with entitlements under its points reward scheme or the associated airline's frequent flyer scheme. It does not matter that some of the points that give the entitlement result from employment-related expenditure.

**Example 9**

126. Following from example 8, in the following year the employee is promoted in the company and receives a corporate charge card on which she is specified as the cardholder. The charge card is from a different company to that which issued her personal card. This particular charge card company also allows cardholders to join its points reward scheme. The employee joins the points reward scheme as an individual member and pays the membership fee personally. The employee's employer is not involved in encouraging the employee to join the scheme. This scheme also allows an accumulation of points as goods and services are charged on the card and a transfer of points, subject to certain conditions, to a participating airline's frequent flyer scheme.

127. Section CX 2(2) will not apply on the facts of this example. There has been no significant contact between the employer and the credit card company. There is no arrangement between the employer and the credit card company to provide entitlements to the employee under the points reward scheme. The employee receives those entitlements because of her contractual relationship with the credit card company.

**Example 10**

128. QRS purchases motor vehicles for business purposes from a motor vehicle dealer. As a result of QRS' substantial custom, the dealer states that it will discount QRS' future purchases. It also informs QRS that the more vehicles purchased, the greater the discount. To increase the discount, QRS asks the dealer to offer the same discount to the employees of QRS. QRS tells the dealer that many of its employees would like to purchase vehicles and it expects that they would be induced to buy vehicles from the dealer if they were offered the same discount. The dealer agrees to offer the employees the same discount as it provides to QRS.

129. In this example, QRS has requested that the dealer provide its employees with a discount on any vehicles they purchase. Because of QRS' substantial custom, the dealer agreed to offer the discount to the employees. There is an arrangement between the dealer and QRS that is for the provision of a benefit (ie the discount) to the employees. Although the dominant purpose of QRS may be to obtain a higher discount on its future vehicle purchases, a significant purpose of it entering into the arrangement is so that the same discount is offered to its employees.

Therefore, s CX 2(2) will apply, because QRS made the arrangement with a more than incidental purpose to provide its employees with a benefit.

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### Expired Rulings

BR Pub 04/05 "The provision of benefits by third parties: fringe benefit tax (FBT) consequences – section CI 2(1)" *Tax Information Bulletin* Vol 16, No 5 (June 2004): 4

BR Pub 09/07 "Provision of benefits by third parties – fringe benefit tax consequences – section CX 2(2)" *Tax Information Bulletin* Vol 21, No 7 (September 2009): 7

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Arrangement
Benefit
Fringe benefit tax
For
Provided
Third party provides benefit

### Legislative references

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Income Tax Act 2007, ss BG 1, CX 2(1), CX 2(2), CX 2(5)(a), GB 31 and the definition of "arrangement" in s YA 1
Interpretation Act 1999, s 5

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