

## TECHNICAL DECISION SUMMARY > ADJUDICATION

## WHAKARĀPOPOTO WHAKATAU HANGARAU > WHAKAWĀ

# Deductions and shortfall penalties

Decision date | Rā o te Whakatau: 17 February 2025

Issue date | Rā Tuku: 8 May 2025

TDS 25/12

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## Subjects | Kaupapa

Whether the Taxpayer was entitled to input tax deductions it claimed. Whether the Taxpayer was required to return GST output tax on refunds. Whether the Taxpayer was liable for shortfall penalties.

## Taxation laws | Ture tāke

All legislative references are to the Goods and Services Tax Act 1985 (GSTA) unless otherwise stated.

## Summary of facts | Whakarāpopoto o Meka

1. The Taxpayer was a company registered for GST on a payments basis. The Taxpayer had one shareholder and two directors. The Taxpayer purchased land and began to set up a business.
2. There was another company (Y Co) with the same shareholder and the same two directors as the Taxpayer.
3. After a while, the Taxpayer sold the business to Y Co. The purchase price for the business was inclusive of GST and included an amount reimbursing the Taxpayer for business related set up costs (set up costs).
4. The Taxpayer filed GST returns for two periods (which included the period in which the sale took place). In those returns the Taxpayer claimed a range of inputs for which Customer and Compliance Services (CCS) argued:
  - The Taxpayer failed to provide receipts or other documents requested to support the input tax deductions.
  - The Taxpayer failed to keep tax invoices.
  - The Taxpayer had not satisfied the onus of proving that the input tax deductions were in relation to the Taxpayer's taxable activity and were not private or exempt in nature.
5. In its GST returns the Taxpayer included GST outputs on:
  - refunds from suppliers, and
  - the consideration for the transfer of the business to Y Co.

6. CCS argued that the output tax in relation to the refunds were not true outputs and had been accounted for by adjusting the underlying input claims in the respective periods.
7. CCS argued that no GST output tax was required on the portion of the sale price of the business that related to the set up costs. This was because:
  - The set up costs related to the Taxpayer's operation of the business and had been claimed as inputs by the Taxpayer.
  - The sale of the business by the Taxpayer to Y Co was the supply of a going concern.
8. CCS proposed to assess the Taxpayer with shortfall penalties for gross carelessness under s 141C of the Tax Administration Act 1994 (TAA) in relation to the tax positions taken. In the alternative, CCS proposed shortfall penalties for not taking reasonable care under s 141A of the TAA.

## Issues | Take

9. The issues considered in this dispute were:
  - Whether the Taxpayer was entitled to the GST input tax deductions claimed in the periods in dispute.
  - Whether the Taxpayer was required to return GST output tax on refunds and set up costs in the periods in dispute.
  - Whether the Taxpayer was liable for shortfall penalties for gross carelessness in taking its tax positions (s 141C of the TAA). Alternatively, whether the Taxpayer was liable for shortfall penalties for not taking reasonable care in taking its tax positions (s 141A of the TAA).
10. There was also a preliminary issue on the onus and standard of proof.

## Decisions | Whakataau

11. The Tax Counsel Office (TCO) decided:
  - It could not be definitively concluded which input tax deductions claimed by the Taxpayer in the GST periods in dispute were valid. However, not all of the input tax deductions claimed by the Taxpayer were valid.
  - The adjustments proposed by CCS to output tax for the refunds should be made.

- The adjustment proposed by CCS to output tax for the set up costs should not be made.
- The Taxpayer was liable for the gross carelessness shortfall penalties proposed by CCS.

## Reasons for decisions | Pūnga o ngā whakatauranga

### Preliminary issue | Take tōmua: Onus and standard of proof

12. Except for proceedings relating to evasion or similar act or obstruction, the onus of proof is on the taxpayer to show that an assessment is wrong, why it is wrong, and by how much it is wrong.<sup>1</sup> However, if the taxpayer proves, on the balance of probabilities, that the amount of an assessment is excessive by a specific amount, the taxpayer's assessment must be reduced by the specific amount.<sup>2</sup>
13. The standard of proof required is the balance of probabilities.<sup>3</sup>
14. It is appropriate that the same onus and standard of proof be applied in the disputes process as in challenge proceedings. TCO considered whether the Taxpayer has discharged the onus of proof in the context of the issues raised by the parties in the dispute, based on the documentary evidence put before it.

### Issue 1 | Take tuatahi: GST input tax deductions

15. The input tax deductions claimed were not valid because the expenditure was private in nature and/or the Taxpayer did not provide sufficient business records to support the deductions. CCS had provided details of input tax deductions which the Taxpayer was not entitled to claim. The Taxpayer had not satisfied the onus of proof.
16. The effect of s 138P(1B) of the TAA was that the Taxpayer may be entitled to some of the input tax deductions claimed if it could provide sufficient evidence to support its

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<sup>1</sup> Section 149A(2) of the TAA. See also *Case V17* (2002) 20 NZTC 10,192, *Accent Management Ltd v CIR* (2005) 22 NZTC 19,027 (HC), and *Vinelight Nominees Ltd v CIR (No 2)* (2005) 22 NZTC 19,519 (HC).

<sup>2</sup> Section 138P(1B) of the TAA.

<sup>3</sup> *Yew v CIR* (1984) 6 NZTC 61,710 (CA), *Case Y3* (2007) 23 NZTC 13,028, and *Case X16* (2005) 22 NZTC 12,216.

entitlement to those deductions. However, no such evidence had been produced by the Taxpayer.

## Issue 2 | Take tuarua: GST output tax

17. The adjustments to output tax for the refunds reduced the Taxpayer's output tax and accordingly were in the Taxpayer's favour.
18. The amount paid by the Y Co to the Taxpayer was consideration for the sale of the business in the relevant GST period. That the invoice issued by the Taxpayer referred to set up costs and/or the purchase price for the business was calculated with reference to (and sought to recover) costs incurred by the Taxpayer did not change this conclusion.
19. The zero-rating provision in s 11(1)(m) did not apply in this case because:
  - All the requirements of s 11(1)(m) must be satisfied before a transaction can be zero-rated. Even if it could be established that the supply was of a going concern, there was no evidence that the Y Co and the Taxpayer agreed the supply was of a going concern and recorded their agreement in a document.
  - Y Co's tax agent's description of the transaction as the sale of the "business, lock, stock and barrel" was not sufficient to support the view that the Y Co and the Taxpayer agreed that the supply was of a going concern and recorded their agreement in a document.

## Issue 3 | Take tuatoru: Shortfall penalties

20. The Taxpayer took the tax positions by filing tax returns.
21. The Taxpayer's tax positions were not correct and there were tax shortfalls.
22. The Taxpayer was grossly careless when it took the tax positions for the following reasons:
  - The Taxpayer's director was an experienced business person with accounting experience. The director had previously dealt with IR in relation to the deductibility of expenses similar in nature to those considered here.
  - At the time the tax positions were taken, the Taxpayer's director (on behalf of the Taxpayer) was aware of the type of expenses able to be claimed as GST inputs, the need to apportion business expenses that contained a private component and to have records to support the treatment of expenses.

- Taking tax positions without records to support those positions created a high risk of tax shortfalls. The risk was a serious and obvious one that would have been foreseen by a reasonable person in the circumstances. The Taxpayer's director (on behalf of the Taxpayer) had a complete or high level of disregard for the consequences by taking the tax positions.
23. The requirements for shortfall penalties for not taking reasonable care were also met. However, the shortfall penalty for gross carelessness applied because it was the higher penalty (s 149(2) and (3) of the TAA).
24. The resulting shortfall penalties were reduced by 50% under s 141FB(2) of the TAA.