

TAX INFORMATION BULLETIN NO.11

JUNE 1990

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TIME-SHARE APARTMENTS - PROFITS ON SALE SUBJECT TO TAX

SUMMARY

This item corrects a statement made in Public Information Bulletin No.179 concerning the circumstances under which the profit on sale of a time-share unit would be taxable.

BACKGROUND

Public Information Bulletin No.179 contained an item (page 17) dealing with the income tax implications of time-share apartments. That item included the following statement:

“Sale of the Unit

Only where the person selling the unit is in the business of selling properties would the sale of the unit be taxable under section 67 of the Income Tax Act 1976.”

This statement is incorrect.

RULING

Profits from the sale of time-share apartments can be taxable under either section 65(2)(a) or sections 65(2)(f) and 67 of the Income Tax Act 1976, as follows:

Section 65(2)(a) -

This section would include as income for tax purposes, the profit on sale or disposal of any time-share unit where it is derived by the vendor from the business of dealing in land.

Sections 65(2)(f) and 67 -

1. The interest acquired in a time-share apartment by a purchaser usually takes the form of an interval lease relating to the weeks of the year which have been purchased, registered against the separate title of the apartment. Each apartment has a composite title which records that each purchaser has a share in the freehold (calculated as the number of weeks purchased as a fraction of a year), plus an estate as a lessee for the particular weeks purchased.
2. The interest of the purchaser, either in the freehold, or under the interval lease, is an interest in “land” as defined in section 67(1) and all the provisions of section 67 could apply to any sale or disposition of a time-share apartment.

3. The most likely situations in which section 67 and section 65(2)(f) would include any profits or gains derived from the sale of interests in time-share apartments in a person’s assessable income, are as follows:

- (a) Where the time-share apartment was acquired for the purpose or intention (or included the purpose or intention) of selling or otherwise disposing of it.
- (b) Where the vendor, or any person associated with the vendor, carried on the business of dealing in land at the date the time-share apartment was acquired, and
 - * the apartment was acquired for the purpose of the land-dealing business; or
 - * the apartment was sold within 10 years of acquisition.

- (c) Where the vendor sells the time-share apartment within 10 years of acquisition and, in the Commissioner's opinion, at least 20 percent of the profits or gains were due to such factors as land zoning changes, or any other changes or occurrences of a similar nature (including the likelihood of any such changes or occurrences).

4. Whether the section 67(5)(b) exemption for dwellinghouses acquired and occupied primarily and principally as a residence for the vendor, would apply to time-share apartments, depends on the facts of each case. The requirements of this exemption have been held not to be satisfied where occupation as a residence was merely incidental to another purpose such as holding the property pending resale. In establishing this, the period a property is occupied during the year is not, by itself, a conclusive test of whether the property is primarily and principally used as a residence. The exemption also does not apply where the vendor has engaged in a regular pattern of transactions involving acquisition and subsequent sale or disposition of dwellinghouses.
5. The application of the section 67(6) exemption in cases falling within paragraph 3(c) above, would also be a question of fact because, although the exemption applies to “land” rather than a dwellinghouse, it requires that the vendor acquired and used (or intended to use) the land primarily and principally as a residence.

Reference: H.O. 10.T.5.2

LIVESTOCK FARMING REGIME

The Income Tax Amendment Act (No 4) 1989 made several changes to the livestock valuation regime.

Application of Section 86: 3 Year Write-Down Provisions

Section 11, subsections (1) and (2), provides that the 3 year write-down rules only apply to non-specified livestock. This is effective from the income year commencing 1 April 1989.

Where specified livestock purchased in previous years are still being written down, the balance of the write-down may be deducted in full in the income year commencing 1 April 1989.

High-Priced Livestock: Application of \$100 Minimum.

A new definition of the term "high priced livestock" was introduced by section 13 and applies from 1 April 1990. Animals purchased for less than \$100 are not to be included in the high-priced livestock scheme. Such animals may be included in any of the other valuation schemes available for specified livestock.

The wording of the amended definition is broad enough to allow animals purchased prior to 1 April 1989 for less than \$100 which are currently in the higher-priced scheme to be removed. This livestock may be included in any of the other livestock schemes.

IN SPECIE DISTRIBUTIONS

Appendix A to this bulletin deals with the implications under various Inland Revenue Acts of an in specie distribution to shareholders upon the liquidation or dissolution of a company.

ACCIDENT COMPENSATION LEVY RECLASSIFICATIONS

Employer and Self Employed Accident Compensation Levy rates are set annually by way of the Levies Order. The 1989 Order set 24 classes, effective from 1 April 1990.

The Accident Compensation Employer and Self Employed Persons Levies Order 1989 Amendment No 1 made three changes to the 1989 Order, as follows:

Industrial Activity Class	Old Rate	Old Class	New Rate	New Class
Customs, shipping and forwarding agency (without transport operations), business of	40	2.35	43	1.30
Pottery (hand crafted), manufacture, selling	33	2.95	36	1.30
Travel agency, business of	40	2.35	43	1.30

LEGISLATION - INCOME TAX AMENDMENT ACT 1990 AND THE ESTATE AND GIFT DUTIES AMENDMENT ACT 1990

The Taxation Reform Bill 1990 was introduced into the House on 21 March 1990 and passed through all stages under urgency. The Bill was enacted as the Income Tax Amendment Act 1990 and the Estate and Gift Duty Amendment Act 1990. These Acts comprise various provisions which were required to be enacted prior to 1 April 1990. Certain of the provisions in these Acts were transferred from the Taxation Reform Bill (No.7) 1989.

Issues covered by the Income Tax Amendment Act 1990:

- (i) Donations made to the Cyclone Ofa Relief Fund to qualify as a rebate for tax purposes.
- (ii) Taxation treatment of local authority companies and port companies.
- (iii) Dividends payable by building societies on withdrawable shares are "interest" for Resident Withholding Tax purposes.
- (iv) The 20th of each month is reinstated as the date by which PAYE must be paid by small employers.
- (v) The trust regime is amended to make it clear that pensions from a superannuation fund are exempt from income tax.
- (vi) The rates of income tax and excess retention tax for the 1989/90 year are confirmed.

The Estate and Gift Duties Amendment Act 1990 provides for:

- (i) The charitable succession exemption to be raised from \$25,000 to \$100,000.
- (ii) Transfers of property made in accordance with the Waikato Electricity Authority Act 1988 to be exempt from gift duty.

A detailed commentary is provided in Appendix B to this TIB.

GST TREATMENT OF DAMAGES AND OUT OF COURT SETTLEMENTS

1. Summary

This item is to clarify the correct treatment for GST purposes of Court awards and settlements made out of Court.

2. Court Awarded Damages

A Court may rule that specified and/or general damages must be paid by one party to another party where the first party has not satisfied its obligations under a contract. The original contract may have involved a taxable supply, exempt supply or zero-rated supply for the purposes of the Goods and Services Tax Act 1985. Alternatively, no supplies may have occurred where for example, a contract has not been performed.

Certain questions now arise as to the correct treatment for GST purposes of some of the situations that may arise. These questions and the treatment to be applied are as follows:

- (a) Should the GST consequences of damages payments be analysed under each head of claim?

Yes. The nature of the transaction to which the damages claim relates will indicate the liability or otherwise to GST.

- (b) In the case of specified damages in relation to previous taxable supplies, does GST apply? If so, should the amount claimed by the aggrieved party include sums of GST where applicable?

If supplies are made and losses are incurred by the recipient as a result of these supplies due to poor workmanship or an inferior product, any damages awarded in respect of these losses would not be subject to GST. The damages awarded would be in respect of the losses and not the supply of the goods or services.

On the other hand if losses were incurred by the supplier due to non-payment for goods and services and a Court award is subsequently made, then a GST liability would arise. The damages in this situation are in respect of the supply of goods or services.

In the event of a GST liability arising it would be up to the parties concerned and the Courts to decide whether an amount of GST should be included in the payment. Regardless of what is decided in this instance, the amount to be

accounted for in respect of GST would be the tax fraction of the amount awarded.

- (c) In the case of specified damages for loss of profits, where a contract has not been performed, does GST apply?

No. There must be a supply of goods or services before GST can apply.

- (d) What are the GST consequences of general damages?

Here again, the treatment for GST will depend on the nature of the original transaction, e.g., did a supply occur? Was it exempt or zero-rated or a combination of both?

3. Out of Court Settlements

Parties in a dispute may decide to settle out of Court. This may involve a payment to the aggrieved party for a particular claim, or there may be a global compensation covering a variety of claims.

Questions raised and the relevant treatment to be applied are:

- (a) Where there is an out of Court settlement and all or part of the settlement can be connected back to the original taxable supplies, does GST apply? If so, how is the GST calculated?

The proportion of the settlement connected to the supply of the original taxable supplies would be subject to GST.

GST is calculated as the tax fraction of the settlement.

- (b) Where there is an unscheduled global payment in full and final settlement of prior legal proceedings it may not be possible to connect this back to the original supply. Does GST still apply?

Details of the facts of each particular case would need to be examined to ascertain whether a GST liability exists. If it is established that part of the payment relates to the original supply an apportionment may be required if the amount relating to the supply is not specified.

- (c) Where there were no taxable supplies in the first instance, does GST apply to the settlement?

No. There must be a supply of goods or services before GST can apply.

4. Calculation of GST

In the instances discussed above, where GST does apply the aggrieved party should return the tax fraction of the amount involved as output tax with the payer of the amount allowed the same amount as a deduction for input tax.

Reference: HO: GST Govt J. 1
GST Technical Manual Chapter 1.

OFFICIAL INFORMATION COPY: TECHNICAL RULINGS MANUAL

The format of the Department's Technical Rulings has been reviewed and all chapters are being rewritten.

As each chapter is completed it will be allocated a new number, and its availability for purchase will be advertised, together with the cost.

The following chapters are available now:

Chapter 53 - Charities/Donee Organisations. This replaces the previous Chapter 17. The GST-inclusive cost of chapter 53 is \$30.00

Chapter 58 - Resident Withholding Tax (Interest/Dividend PAYE) This is a completely new Chapter. The GST-inclusive cost is \$8.50

Chapter 73 - Unclaimed money. This replaces the previous Chapter 14. The GST-inclusive cost of Chapter 73 is \$5.00

GST Manual-This has also been updated, to incorporate Legislative Amendments arising from the GST Amendment Act (No 2) 1989. The pages of the Manual that are affected have been reprinted, rather than reproducing the entire edition. The cost of the additional pages is \$12.70. These pages will only be available as a separate item from the Manual for a limited time.

Any complete copies of the GST Manual that are purchased from now on will include the new pages, and will cost \$81.30, being the original cost of \$68.60 plus the cost of the new pages.

If you wish to purchase any of these chapters under section 15 of the Official Information Act please forward payment, together with your name and address, to

Inland Revenue Department
Manual Sales Section
PO Box 2198
WELLINGTON

RECENT DETERMINATIONS MADE BY THE COMMISSIONER

Two determinations were issued by the Commissioner on the 23rd of April 1990. Below is a short explanation of each. The full determinations are printed in Appendix C to this TIB.

Determination G6B

This determination replaces Determination G6A, made by the Commissioner on 21 November 1988. Determination G6B differs from G6A by replacing the definition of "authorised foreign exchange dealer" with the definition "approved foreign exchange dealer".

The definition of "authorised foreign exchange dealer" set out in clause 5(1) of Determination G6A refers to persons designated as such by notice in the Gazette for the purposes of the Exchange Control Regulations 1985. Those regulations were revoked from 1 February 1990 by the Reserve Bank Act 1989.

Determination G10A

This determination replaces Determination G10, made by the Commissioner on 21 November 1988. It amends the interpretation of the number of days in a period calculated on a 360 day basis to that used by Hewlett Packard Business Calculators.

INCOME TAX (WITHHOLDING PAY- MENTS) REGULATIONS 1979 - AMEND- MENT NO. 8

Amendment No 8 to the Income Tax (Withholding Payments) Regulations 1979 inserted a new subparagraph (ab) into the definition of "contract activity". The full text of this item is in Appendix D to this T.I.B.

The purpose of the item is to provide a background to the recent amendment, a description of the amendment and an explanation of the effects and extent of the regulations subsequent to the amendment.

Please note that the item is concerned only with Non-Resident Contractors' Withholding Tax. Non-Resident Withholding Tax applies only to payments of interest, dividends and royalties.

- Partnerships
- Estates and Trusts
- Clubs and Superannuation Funds

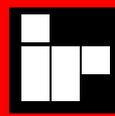
DUE DATES REMINDER

- June 5 PAYE Tax Deductions for last 16 days of May 1990 - "Large" employers only
- 7 First instalment of 1991 Provisional Tax due for taxpayers with February Balance Dates
- Second instalment of 1991 Provisional Tax due for taxpayers with October Balance Dates
- Third instalment of 1991 Provisional Tax due for taxpayers with June Balance Dates
- Tax Returns (IR 5) due for salary and wage earners
- 14 Interest PAYE deducted during May 1990 due for monthly payers
- Dividend PAYE deducted during May 1990 due
- Non-Resident withholding Tax deducted during May 1990 due
- 20 PAYE Tax Deductions for first 15 days of June 1990 - "Large" employers
- PAYE Tax Deductions for May 1990 due "Small" employers
- July 1 GST Return and payment for period ended 31 May 1990 due
- 5 PAYE Tax Deductions for last 15 days of June 1990 - "Large" employers only
- 7 First instalment of 1991 Provisional Tax due for taxpayers with March Balance Dates
- Second instalment of 1991 Provisional Tax due for taxpayers with November Balance Dates
- Third instalment of 1991 Provisional Tax due for taxpayers with July Balance Dates
- Tax Returns due for:
- Provisional Taxpayers
 - Companies
 - Maori Authorities

with balance dates 1 October to 7 May inclusive. (For balance dates between 8 May and 30 September, returns are due two months after balance date)

- 14 Interest PAYE deducted during June 1990 due for monthly payers
- Dividend PAYE deducted during June 1990 due
- Non-Resident withholding Tax deducted during June 1990 due
- 20 PAYE Tax Deductions for first 15 days of July 1990 due - "Large" employers
- PAYE Tax Deductions for June 1990 due "Small" employers
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TAX INFORMATION BULLETIN



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THIS IS AN INLAND REVENUE DEPARTMENT SERVICE
TO PEOPLE WITH AN INTEREST IN THE TECHNICAL ASPECTS
OF TAXATION IN NEW ZEALAND.