Fidelity Fund Levies - Income Tax and GST Implications

Summary

This article deals with the income tax and GST implications of payments to the New Zealand Society of Accountants (NZSA) and the New Zealand Law Society (NZLS) fidelity funds.

These levies are fully deductible for income tax in the income year in which practitioners incur them. This is regardless of whether payment is made in one sum or by instalments over a number of income years.

The full GST liability occurs at the earlier time of payment or when the service is invoiced.

Background

Both the NZSA and the NZLS make annual levies on practising members to supplement their respective fidelity funds. In the last year each society has made a larger than normal levy.

Income Tax Policy

Paying the levy is a prerequisite for issue of a practising certificate. A solicitor must have a practising certificate to practise on his/her own account (Sections 56, 57, and 167 of the Law Practitioners Act 1982).

Although the Accountants' Society does not issue certificates of practice annually, annual payments to the fidelity fund are linked to an accountant's ongoing eligibility to practice (Section 14A of the New Zealand Society of Accountants Act 1958, and section 11 of the New Zealand Society of Accountants Amendment Act 1963).

This means the respective levies are a cost of doing business for practising accountants or solicitors. The levies are deductible under section 104 of the Income Tax Act 1976 (the ITA).

These levies meet the requirements of section 104 of the ITA whether they are made in full or in instalments. The cost has been incurred as the total payment has either been made, or is owing and will be made.

The timing of the deduction depends on individual practitioners' balance dates. The cost is deductible in the income year in which the practitioner first incurs the liability. For the special levies this is:

- Accountants - the income year in which May 1992 falls;
- Solicitors - the income year in which December 1992 falls.

For most practitioners this will be the income year ended 31 March 1993.

GST Policy

The term "services" has a broad meaning in the Goods and Services Tax Act 1985 (the GST Act). Both the NZLS and the NZSA provide many services to their members, one of which is the provision of a fidelity fund. Therefore, the levies are payments for services.

The levies are not financial services or an other exempt supply. They are a supply by the NZLS or the NZSA to their respective practising members. The levies are neither fines nor penalties on individual practitioners. Each practising member is liable to make payment by virtue of being a practising member. Nor are the levies gifts or donations. They are a prerequisite for obtaining a practising certificate for a solicitor and retention of a certificate of practice for an accountant, so they lack the voluntary nature of a gift or donation. (*NZSA v CIR*, *NZLS v CIR* (No.2) [1986] 8 NZTC 5,205). The levy is a taxable supply, thus GST is payable.

Section 9 of the GST Act deems the supply to have occurred at the earlier time of invoice or payment. Only one invoice is issued for the levy, even where the payer elects to pay by instalments. Therefore, the full amount of GST is payable at that time.

The timing of the corresponding GST input credit depends on the circumstances of the individual practitioner. Section 20(3) of the GST Act determines this. Those registered on an invoice basis may claim the input at the earlier of being invoiced or payment. Those registered on a cash or hybrid basis may claim the input on an actual payments basis. In either case, the practitioner must hold a tax invoice.

A practitioner who is below the threshold for GST registration and who has not registered voluntarily may not claim any GST input credits. Instead the full (GST inclusive) amount of the levy is deductible for income tax purposes as discussed above.

References: HO 10.D.1.1
HO GST L.1.1

Employee or Independent Contractor?

We've published this article to help taxpayers work out their employment status for tax purposes; it does not introduce any policy changes. It describes the tests for determining whether taxpayers are employees or independent contractors, and discusses the recent Employment Court decision in *TNT Worldwide Couriers v Cunningham* (1992).

A taxpayer's tax obligations differ according to his/her employment status, so it is important to know if s/he is an employee or not. On a related matter, Inland Revenue is warning taxpayers against "opting out" of the PAYE system by calling themselves independent contractors when they are essentially still employees.

Sometimes it isn't easy to tell if a taxpayer is an employee. Changes in regulations and work practices may also cause the employment status of some workers to change. Court cases like *Challenge Realty Limited and Ors v CIR* (which judged commission real estate salespersons to be employees) and *TNT* (which judged owner driver couriers to be employees) show that even a long accepted status might not meet the legal requirements for that status.

Background

In *TNT* the Employment Court found that an owner-driver courier for TNT was an employee and not self employed. *TNT* wasn't a tax case, but it has tax implications because the general law determines employment status for tax purposes.

In *TNT*, the courier:

- provided his own vehicle and was responsible for its maintenance and upkeep
- was responsible for all his own tax and ACC payments
- claimed deductions as if he were self employed, and
- had an employment contract with TNT that said he was an independent contractor.

However the Court found the courier actually had a contract of service with TNT because the employer's actions showed it treated the courier as its employee. In particular it:

- exercised strong control over the volume, type, quality and location of his work
- supervised him closely
- restricted him from carrying freight for anyone else
- had all ownership rights over the business and goodwill
- could regulate his income (by controlling where and how much he worked).

Relevance of Employment Status

A worker's employment status has important consequences for tax purposes:

Payments to *employees* from their employer are salary or wages, which must have PAYE deducted at source.

Employees cannot register for or charge GST for services they supply as employees.

Independent contractors

- may deduct certain expenses incurred in deriving assessable income
- must account to Inland Revenue for tax and ACC earner and employee premiums for themselves and any employees; and
- must meet all the requirements of the GST Act if the services they supply are a taxable activity, and they are registered (or liable to register) for GST.

Types of Employment Arrangement

Employment status depends on whether a worker's employment contract is a "contract of service" or a "contract for services".

A *"contract of employment"* includes an unwritten arrangement. A written contract is neither necessary nor conclusive as to the existence of any particular type of employment relationship (although it can show the sort of work relationship the parties intended to have). Employment contracts often change as the work relationship evolves (e.g., a worker takes on more duties). The Courts consider how the parties actually work together when they determine what sort of employment contract the parties have.

Employees have a *"contract of service"* with their employer. Contracts of service evolved from the old concept of a master-servant relationship. This required an employee to be continuously available for service and to accept a high degree of control by the employer.

A *"contract for services"* applies to the relationship between an independent contractor and a principal. It emphasises the nature of goods or services to be provided by the worker rather than his or her availability to work as directed.

Employment Status and Revenue Law

Tax law relies on the terms "contract of service" and "contract for services", but doesn't define them. Therefore their meanings depend on the general law - i.e., contract law developed by the Courts and any statutes that apply to a particular kind of work.

A person will have the same employment status for tax purposes as s/he has under the general law. If Inland

Revenue needs to determine a worker's status, we will use the current general law tests.

Tests of the Employment Relationship

The law uses five tests to determine what type of contract exists.

Cases may not be clear-cut and the tests overlap (e.g., whether a worker can work for other employers is a component of both the control and independence tests). This means the results of the various tests must be weighed to find the predominant factors which will determine the relationship.

Here are the five tests:

1. Control

This looks at the degree of control the employer exerts over the way the work is done. The greater the extent to which the principal/employer:

- supplies the equipment, premises and materials used;
- specifies work content, hours and methods;
- can choose, pay, regulate and dismiss workers;

the more likely it is that the worker will be an employee.

In *TNT*, the Court said this was a very important test. The fact that TNT exercised a high degree of control in all these areas (except it did not supply the courier's vehicle) was the main reason for determining that there was a contract of service.

2. Independence

A worker who can exercise the following types of powers or responsibilities is unlikely to be an employee:

- work for other people or clients;
- work from his/her own premises;
- supply his/her own (specialised) tools/equipment;
- have direct responsibility for the profits and risks of the business;
- hire/fire whoever s/he wishes to help do the job;
- advertise and invoice for the work;
- pay/account for taxes and government and professional levies.

This is the inverse of the Control test - a high level of independence is inconsistent with a high level of control. For example, although the TNT courier driver supplied his own vehicle and did his own tax and accounts, he had little or no other independence.

On the other hand, when some independent contractors do work for someone, they agree not to work for a competitor or give away trade secrets. This alone won't make the worker an employee (it actually emphasises that the worker is usually entitled to work for others).

3. Organisation/Integration

A job is likely to be done by an employee if it is:

- integral to the business organisation;
- the type of work commonly done by "employees";
- continuous (not a "one-off" or accessory operation);
- for the benefit of the business rather than the worker.

E.g., courier drivers are essential to the continuous operation of most courier businesses and are usually clearly identified with their courier firm.

4. Intention

This looks at the label the parties themselves and any outside authorities apply to the relationship:

- The employment contract treats them as employees;
- Payment is at regular intervals, at a set rate and PAYE is deducted;
- The worker previously worked as an "employee" for the same employer;
- If a statute treats the relationship as one or the other type of contract.

This is a strong, but not conclusive indication of the type of relationship. If the actual facts point to an employment relationship, then simply labelling it an independent contract will not alter the actuality. This happened in *TNT*. In a clause which purported to override all other aspects of the agreement, the written contract stated that the courier was an independent contractor. However the Employment Court found that the actual conduct of the relationship showed that TNT imposed a high level of control and supervision of its staff that was altogether inconsistent with any independence or initiative on their part.

The influence of a statute is shown in the Real Estate Agents' Amendment Act 1992. This was a consequence of the *Challenge* Court case and allows real estate sellers to agree with their licensee that they will be independent contractors rather than employees.

5. Economic Reality

This test looks at aspects such as:

- whether the type of business or the nature of the job justifies or requires using an independent contractor;
- the behaviour of the parties before and after entering into the contract;
- if there is a time limit for completing a specific project;
- whether the worker can be dismissed;
- who is responsible for correcting sub-standard work;
- who is legally liable if the job goes wrong.

Usually, an independent contractor agrees to be responsible for his/her work. S/he cannot usually be "dismissed", although the contract can be terminated if it is broken.

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Consequences of a Change in Status

Taxpayers may consider that they have not been using the correct employment status in their tax returns. If you want more information about correcting this, including the requirements for a different status, contact your nearest Inland Revenue Office.

The *TNT* case is being appealed. If the appeal decision indicates that some couriers and carriers should change their employment status for tax purposes, Inland Revenue will not seek to recover back taxes from them if we have previously accepted their returns made on the basis of the old status. We will also issue more detailed guidance on couriers' and carriers' tax obligations under the different employment relationships.

References:
Challenge Realty Limited and Ors v CIR (1990) 12 NZTC 7,212
TNT Worldwide Couriers v Cunningham (1992) EC Wellington, WEC 31D/92; 23/12/92
TIB 4.1; 3.8; 3.4; 3.1.

GST and Compensation to Maori Organisations

Summary

This item confirms that GST is not payable on compensation payments that the Government makes to the Maori people for the confiscation of land and the destruction of goods and chattels.

History

Government Commissions of Inquiry over the years have resulted in compensation payments being made to various Maori organisations. These payments were for the confiscation of land and the loss and destruction of goods and chattels. The payments for land confiscation are payable on an annual basis in perpetuity, but those for loss of property were one-off payments. The question has arisen whether these compensation payments are subject to GST in the same way as Government grants to various organisations are treated.

GST Treatment

A supply must take place before GST is payable. In the case of a Government grant to a GST registered organisation, GST is payable because the grant is deemed to be consideration for the supply of goods or services by the organisation in the course of its taxable activity. This situation comes under section 5(6D) of the Goods and Services Tax Act 1985, which was inserted by the Goods and Services Tax Amendment Act (No 3) 1991 to reinforce Inland Revenue's policy on these grants. The recipients of these grants are supplying services to the Government through the use to which they put the grant money they receive.

Compensation payable by the Crown to the Maori organisations is payable under statute. It is not consideration for the supply of goods or services as no supply has taken place. GST is therefore not payable on these payments.

Reference: HO: GST Govt M.1.
Technical Rulings Chapter 108

Livestock Valuation - New Self-Assessed Cost Guidelines

The Government set up the Livestock Valuation Consultative Committee to review the way livestock is valued for tax purposes.

In its report, the Committee recommended that farmers be able to value livestock using their own costs of production. The new scheme will be known as the Self Assessed Cost (SAC) scheme, and farmers can use it for 1991-92 and future income years.

Inland Revenue has produced a set of guidelines for determining the self-assessed cost for individual farmers. These are contained in Appendix A to this TIB.

There is more information about the other proposed livestock valuation options in TIB Volume Four, No.2 of September 1992.

Livestock Valuation Changes

Questions Raised During Recent Seminars

During a recent series of seminars on the proposed livestock valuation changes we were asked several questions that had common themes. Based on those questions, the following information will be of interest to livestock owners and tax practitioners involved with the farming community.

This information is based on Government decisions on the recommendations of the Livestock Valuation Consultative Committee (the Committee). Legislation for the changes is in the Tax Reform Bill (No. 6) introduced in the House on 17 December 1992. The Bill is due to become law before the end of March 1993.

Removing three year spread of revaluation income when moving livestock to the Herd Scheme

The three year spread gave tax relief to farmers moving stock from any other scheme to the herd scheme, and to farmers who were increasing herd scheme numbers from homebred sources. Under the rules applying up to the 1992 income year all animals of a type and/or all mature animals of a livestock type had to be included in the herd scheme if the farmer had adopted that option for that livestock type.

Under the proposed changes the requirement to include all mature livestock of a type in the herd scheme will be removed. Farmers, especially those who are increasing livestock numbers, can select any number of the additional animals they wish to be valued under the herd scheme in any income year. Those animals not in the herd scheme can be valued at any of the other valuation options such as National Standard Cost (NSC), Self Assessed Cost (SAC), market value, etc.

Example

Present rules

A farmer decides to increase the number of sheep by retaining 200 home bred ewe hoggets. All sheep are currently valued under the herd scheme. Because of the present requirement to include all these animals in the herd scheme, their value would be assessable income in the income year the farmer retained them. If the farmer so elects some revaluation income could be spread over three income years.

Proposed Rules

Under the proposed herd scheme rules the farmer could decide to move only 50 of the ewes to the herd scheme in the first year. The other 150 could be valued under another scheme in the first year and moved to the herd scheme in whole or in part in subsequent years. There will be no restriction of the number of livestock moved to the herd scheme, nor the number of years it takes to move all the additional ewes to that scheme.

The proposed herd scheme rules will allow farmers the flexibility to move livestock to the herd scheme when and how they wish. The tax impact of increasing livestock numbers in the herd scheme can be spread over any number of years. The current three year spreading provisions are no longer necessary.

Delaying the announcement of National Average Market Values (NAMVs) until June each year

The current method of setting NAMVs involves a national survey of sale prices conducted for the twelve month period ending on 31 March each year. The Committee considered that this system is unsatisfactory as it does not accurately reflect the value of livestock on hand at balance date. For example, the major cattle and deer sales are conducted between March and May. A survey of prices up to March misses current year sales but picks up prices from sales in the previous March to May period. This methodology can cause serious distortions as happened with mixed-age dairy cows last year.

The Committee recommended a “snapshot valuation” by livestock valuers at 30 April for sheep, goats and pigs and 15 May for cattle and deer. The weighted national average values would reflect the value of good quality stock “on farm” at those dates.

The Government has agreed that the system recommended should be trialled for a year in parallel with a national survey using livestock sales data over the main sales period. For most stock this will be January to May. After the trial an assessment will be made on the valuation method to be adopted.

Whichever system is used for 1993 and future years the values will not be available until mid June each year.

With the repeal of the trading stock scheme only the herd values will be released each June. Farmers on the herd scheme with static herd numbers will not have a taxable component if herd values increase. The late release of the values will not unduly affect their income calculations. Those who have increased herd numbers during any year will need to wait until the release of the values to calculate their annual income.

Farmers wishing to re-estimate provisional tax at the third instalment date could use the previous year's national average market values or current market values. Alternatively, farmers may decide to value the additional livestock under the National Standard Cost scheme. These figures will be available in January/ February each year.

Correcting Minor Errors in GST Returns

Tax Practitioners have asked for a ruling from Inland Revenue for cases where they notice errors in their clients' GST returns. They asked whether they should:

- file an amended return(s) for the period(s) in which the error was made, or
- make a one-off correcting adjustment in the next available return.

For all cases of this type, the following ruling will apply:

If correcting the error(s) will result in less than $50 of tax to pay (per period), it can be corrected in the next available GST return. If the correction will mean tax to pay of more than $50 in a period, the practitioner must file an amended GST return for the relevant period(s).

If a practitioner files amended back returns, additional tax will be imposed automatically, though we will consider remission on a case-by-case basis, depending on the nature of the error(s).

Practitioners must keep detailed working papers in all cases, which must be available to Inland Revenue on request.

Tax Information for Employers

Inland Revenue is sending out information packs to over 160,000 employers to tell them about changes in tax administration from 1 April 1993. These packs contain samples of new PAYE forms, and information about the Student Loans Scheme and Child Support.

We have redesigned these forms to make it as easy as possible for employers to make PAYE deductions (and student loan repayment deductions, where appropriate), as well as to supply other tax information. Before we did this we researched employers' needs in a nationwide survey, and we have incorporated as many of their suggestions as possible into the forms.

Since last year employers have been making Child Support deductions from some employees' wages, and supplying information about the dates when employees start and finish working. From 1 April 1993, some employers will also have to make student loan repayment deductions on behalf of some employees.

More Child Support Deductions being made

Inland Revenue's Child Support Agency is now deducting child support payments from almost half of the liable parents who have been issued assessments. We are making deductions from the incomes or bank accounts of approximately 41,000 liable parents, who make up almost half of all the liable parents for whom we have issued assessments.

Of these 41,000 people, about 27,000 are beneficiaries, who have their child support payments deducted before they receive their benefits. A further 8,500 are having money deducted from their salary or wages, and the remaining 5,500 are having money deducted from their bank accounts.

While many of these 41,000 people have asked for automatic deductions to be made, there has recently been a sharp increase in compulsory deductions as part of the Agency's compliance activity. As a result, the number of automatic deductions has doubled from 7,000 in November to 14,000 in January. This represents a significant step forward in ensuring that all parents meet their financial responsibility to their children, which is the fundamental objective of the Child Support scheme.

By the end of January, the Agency had collected $33.7 million since July. This is 55% of all child support payments owing at 31 December, excluding default assessments. Overall, by 30 June 1993 the Agency aims to collect 64% of the amount owing for this financial year.

In total, there are 87,750 parents whom we have assessed with a child support liability (excluding default assessments). 55,000 (63%) of these parents are making some contribution towards their liability.

Payments made under Restraint of Trade Agreements

This statement replaces the item entitled "Payments made under restraint of trade agreements" in Public Information Bulletin (PIB) No 138 of September 1985.

Background

Under a restraint of trade agreement (also known as a restrictive covenant), in return for payment an employee agrees not to compete with his/her former employer after leaving his/her employment. A restraint of trade agreement can take many forms, such as:

- Agreement not to compete with a former employer within a certain time frame,
- Agreement not to compete with a former employer within a certain geographical area,
- Agreement not to use secret knowledge concerning industrial/scientific processes obtained whilst working for the former employer,
- Agreement not to approach a former employer's customers

The general rule taken by the Courts is that restraints of trade are contrary to public policy and therefore void. These types of agreements are only considered valid where the restraint is justified by the special circumstances of the particular case, and the restraint imposed is reasonable.

In PIB 138 we stated that we would only accept that a payment made under one of these agreements is capital and not assessable if the payment was made under a valid restraint of trade agreement. Our reason for this is that where a contract is unreasonable and therefore a nullity, the character of the payment cannot be determined by the nature of the agreement as there is no agreement.

Discussion

We have reviewed our policy in view of the decision in Case L23 (1989) 11 NZTC 1,147. In this case the Taxation Review Authority (TRA) had to consider whether a payment made to a specialist underwater diver under a restraint of trade agreement was capital, or assessable income under section 65(2)(b) "monetary remuneration" or section 65(2)(l) "other income", of the Income Tax Act 1976 ("the Act"). The TRA rejected the Commissioner's submission that a payment made under an invalid agreement automatically loses the character of capital and is therefore assessable under section 65(2). The TRA found that the practical and business purpose of the payment and the legal rights and duties intended to be created coincided. It was held that the payment did not cease to be capital in character because the agreement turned out to be ineffective.

Section 8 of the Illegal Contracts Act 1970 gives civil Courts the power to give effect to a contract containing a restraint of trade clause by modifying or deleting the offending provision. The TRA does not have this ability. In Case L23, the Authority found that classification of the payment as income or capital did not turn on the issue of validity.

Policy

Inland Revenue accepts that assessability does not turn on the validity of restraint of trade agreements. The assessability of a payment under a void agreement must be found from the intentions of the parties in the same way as the assessability of a payment under a valid agreement. In deciding whether or not payments of either type are assessable, we will apply the general principles expressed in *Buckley & Young Limited v. CIR* [1978] 2 NZLR 485, (1978) 3 NZTC 6,271.

A payment made under a restraint of trade agreement which is treated as a capital receipt will generally not be deductible to the payer, as section 106(1)(a) prohibits the deduction of capital expenditure.

Example

Mr X is a specialist horse trainer in Matamata. His father and grandfather were well know race horse trainers in the Waikato Region. In 1992 Mr X was offered a job as the chief horse trainer of racehorses at Follyfoot Farm. Mr X's employer had an employment contract drawn up setting out his conditions of employment. The employment agreement contains a clause stating that in exchange for the sum of $50,000, for 12 months from termination of the agreement, Mr X will not engage in or have an interest in any racehorse training business within a 100 kilometre radius of Follyfoot Farm.

The classification of the payment as income or capital does not turn on the validity of the contract. Where Inland Revenue is satisfied that the agreement is genuine and observed and is not a sham, the payment will be capital in nature and non-assessable under section 65. The payment will not be deductible to Mr X's employer as it is payment of capital.

Reference: PIB No 138 (1985)
Technical Rulings 56.9.17

Motor Racing Expenditure - Apportionment

Taxation Review Authority Decision

Introduction

This item confirms Inland Revenue's policy on the appropriate basis for apportioning expenditure between business and private use, when an asset has a dual purpose. This is despite a recent Taxation Review Authority decision which allowed the costs in a particular case as a business deduction.

Background

The Taxation Review Authority recently issued a decision on the above matter. The decision has been reported as case P16 (1992) 14 NZTC 4,107.

In the case, a national courier company and its two shareholders were the subject of a tax investigation. The key issue in dispute concerned the deductibility of depreciation claimed by the company for a Jaguar racing car and related parts, and motor racing expenses. The Commissioner disallowed the depreciation and expenses claimed, and deemed the expenses to be dividends in the hands of the shareholders. The taxpayers objected and a case was stated to the Taxation Review Authority.

Before the hearing, the Commissioner accepted that the company should be entitled to deduct one-third of the depreciation and related expenses, and that the shareholders' deemed dividends should be reduced in proportion.

Counsel for the taxpayers submitted that there was a nexus between the expenditure incurred and the gaining or producing of assessable income, which was sufficient to warrant deduction under both limbs of section 104 of the Income Tax Act 1976. The taxpayers participated in national motor racing in order to make the company's name better known nationally and to induce potential customers to associate the company's name with speed and efficiency.

A Jaguar XJS saloon was purchased and taken immediately into the company's books as a racing car. One of the taxpayers participated in driving the car at racing events in order to become an element in the promotion and take advantage of any commercial opportunities arising. Company morale was enhanced and there was a spectacular increase in turnover. The depreciation claimed was deductible as the Jaguar was modified for circuit racing and was not registered or warranted for road use. It fell within the exclusion set out in paragraph (e) of the definition of "motor vehicle" in section 2 of the Transport Act 1962.

The Commissioner submitted that the purpose of the expenditure was to race the car and that racing of the car served two separate purposes; promoting the business and facilitating the taxpayer's personal enjoyment of motor racing. The Commissioner sought to have the expenditure apportioned on that basis. One-third of the expenditure had already been allowed as advertising and promotional expenditure.

The Taxation Review Authority decided in favour of the taxpayers in respect of the depreciation and expenses claim.

On the facts, the Authority found that there was only one purpose for which this expenditure was incurred; that of advertising and promoting the taxpayer's business.

Comment

Inland Revenue is not appealing this Taxation Review Authority decision. The facts of this case represent an unusual situation, which should be seen as an exception to the general rule.

Policy

Where an asset has a dual purpose, business and private, Inland Revenue will continue to apply its existing policy of apportionment of expenditure between business and private on an appropriate basis.

Reference 10.A.3.1

Accrual Determinations

Robin Adair, Inland Revenue's Deputy Commissioner (Legislation), recently signed three accrual determinations. A short explanation of each is provided below. The full determinations appear in Appendix B to this TIB.

Determination 5B: Mandatory Conversion Convertible Notes

This determination rescinds and replaces Determination G5A: *Mandatory Conversion Convertible Notes*, made on 7 November 1991.

This determination differs from Determination G5A by prescribing a method for allocating coupon interest payments between seller and purchaser when a note is sold part way through an interest period. The seller is to allocate interest that has accrued before the date of sale on a straight-line basis. This amount is treated as part of the buyer's acquisition price.

Determination G7C: Futures and Options Markets

This determination rescinds and replaces Determination G7B: *New Zealand Futures and Options Markets* and Determination G18: *International Futures and Options Markets*, both made on 4 December 1989.

The determination differs from Determinations G7B and G18 by:

(a) amalgamating the two existing determinations;

(b) updating the terminology used in relation to the New Zealand Futures and Options Exchange and its members;

(c) adding to the list of approved markets on the New Zealand Futures and Options Exchange;

(d) adding to the list of approved overseas futures and options markets;

(e) modifying the approved sources of information in respect of those overseas markets; and

(f) substituting more relevant and up-to-date examples.

Determination G26: Variable Rate Financial Arrangements

Determination G26 applies to variable rate financial arrangements on which interest is paid at least annually. Any income or expense relating to a variable rate financial arrangement must be accrued. Determination G26 sets out two alternative methods by which this should be done, and explains the circumstances in which each should be used.

A variable rate arrangement may be a floating rate arrangement or a reviewable rate arrangement.

The income or expense in relation to a variable rate arrangement could consist of:

(a) Periodic or coupon interest payments as determined from time to time;

(b) A premium or discount on the issue or face value of the arrangement;

(c) Fees paid or received in relation to the arrangement.

These amounts must be accrued.

The methods provided in the determination separately accrue:

(a) Periodic coupon interest on a daily basis over the income year to which it relates;

(b) Any discount or premium and fees over the term of the arrangement, on either a straight line basis (Method A) or a yield to maturity basis (Method B).

The critical factor in deciding whether Method A or Method B applies to an arrangement is the size of the premium or discount (including fees) relating to the arrangement.

(a) Method A applies to financial arrangements where there is a small (or no) discount or premium. These are arrangements where the discount or premium and fees (non-contingent fees with a limit of 2% of the core acquisition price, plus contingent fees) are less than 2% of the average amount of principal outstanding over the term of the arrangement.

(b) Method B is of general application, and may be applied to any variable rate financial arrangement within the scope of the determination.

Method A permits the spreading of fees and premium or discount over the term of a financial arrangement on a straight line basis, in proportion to the principal outstanding. The simplest case of Method A occurs where the principal is fixed throughout the term. In that case, the premium or discount and fees are spread on a straight line basis over the term of the arrangement.

Method B can be applied regardless of the amount of fees and premium or discount. It requires the fees and premium or discount to be spread on a yield to maturity basis. Since the future cashflows are not known, the actual yield to maturity rate cannot be calculated, but must be estimated. This is done by using the initial interest rate (or price or index) and assuming that this rate will apply throughout the term of the financial arrangement.

The spreading of fees and premium or discount may be done on either a per period basis or a per income year basis. To calculate the yield to maturity, Method B uses either Determination G3: *Yield to Maturity Method* or Determination G10B: *Present Value Calculation Methods* and G11A: *Present Value Based Yield to Maturity Method*.

Interest is calculated separately for each period (or income year) depending on the actual interest rate applying in the period (or the periods within that income year).

Questions We've Been Asked

This section of the Tax Information Bulletin sets out the answers to some day-to-day questions that we've received. We've published these as they may be of general interest to readers.

These items are based on letters we've received. A general similarity to items in this package will not necessarily lead to the same tax result. Each case will depend on its own facts.

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Income Tax Act 1976

Effect of Charitable Trusts Act

Section 61(25) - Charity: A trustee of a trust registered under the Charitable Trusts Act 1957 asked whether the fact that the trust was "charitable" under that Act meant that it was also charitable for taxation purposes.

There is a tax exemption under section 61(25) of the Act for income derived by a trust or organisation carried on for charitable purposes. For taxation purposes, section 2 defines "charitable purpose" to include the relief of poverty, the advancement of education or religion, or any other matter beneficial to the community.

The definition of "charitable" in the Charitable Trusts Act 1957 differs from the definition in the Income Tax Act 1976. Therefore, Inland Revenue makes a separate determination about whether a body qualifies for charitable status for taxation purposes. Even if an organisation has charitable status under the Charitable Trusts Act, it must get separate approval from Inland Revenue before it can become an approved charity for tax purposes.

Inland Revenue is currently producing a booklet that deals with charities, donee organisations and tax exemptions. This will be available from Inland Revenue offices later in 1993.

Reference: HO.TPAH111

Promotional Travel Prizes

Section 65 - Items Included in Assessable Income: A retailer, who was offered a promotion by a product distributor, asked whether a travel prize received under the promotion was taxable. The distributor had offered travel prizes to retailers who purchased a particular brand of product during a certain period. The winners could exchange the travel prizes for cash.

All profits or gains derived from carrying on a business are assessable under section 65(2)(a) of the Act. Therefore, the value of promotional prizes received in the course of carrying on a business is generally included in assessable income. However, prizes will not be assessable income where they are given in kind and cannot be converted into cash.

In this case, as the retailer can convert the prizes into cash, the travel prizes are assessable as business profits.

Reference: HO.TPAH107

Tax Treatment of Annuities

Section 65 - Items Included in Assessable Income: A taxpayer asked whether a ten year annuity offered by a life insurer was assessable for income tax purposes.

Annuities are deemed to be included in assessable income by section 65(2)(j), or under section 65(2)(jb) as accrual income. However, section 61(59) provides an income tax exemption for annuities paid under life insurance policies offered or entered into in New Zealand by a life insurer, or offered or entered into outside New Zealand by a New Zealand resident life insurer. Section 61(59) applies to annuities paid from 1 April 1990.

In this case, the taxpayer's annuity will be exempt from income tax provided that it is paid under a life insurance policy in accordance with section 61(59). If the annuity does not qualify for exemption, the annuity payments will be assessable under section 65(2)(j) or section 65(2)(jb).

Reference: HO.TPP086

Rural Subdivisions

Section 67(9) - Subdivided Farm Lots: A farmer asked about the tax implications of selling a farm property which was subdivided into four economic farming units as part of a subdivision scheme.

Profits or gains from land subdivision schemes are assessable under section 67(4)(e) and 67(4)(f) of the Act. However, section 67(9) provides that section 67(4)(e) and (f) will not apply to the sale of subdivided farm land where:

- The taxpayer used the land in the business of farming immediately before selling it; and

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- The Commissioner is satisfied that the subdivided land is capable of being worked as economic units as farming or agricultural businesses; and
- The Commissioner is satisfied that the land was sold primarily and principally for the purpose of use in a farming or agricultural business.

In this case, profits arising from the subdivision of the farm land will not be assessable provided that the transaction meets the section 67(9) conditions. The Commissioner must be satisfied that the land was subdivided for farming purposes and that the subdivided units are actually capable of being worked as economic units.

Reference: HO.TPA072

Use of Public Service Mileage Rates by Shareholder-Employees

Section 73 - Power to Exempt Employees' Allowances: A tax practitioner asked why shareholder-employees who travel more than 2,000 km annually were not given the same concession as other employees to use Public Service Mileage Rates ("PSMRs") to calculate the reimbursement of motor vehicle expenses. He also enquired about the meaning of "factual, verifiable basis" in TIB Volume 4, No.2 (article on page 2).

Inland Revenue introduced PSMRs as a concession for employees who don't use their cars for work on a daily basis. Shareholder-employees whose work-related travel exceeds 2,000 km annually cannot use this concession. For these people, reimbursement of expenses must be made on a "factual, verifiable" basis. This means that the shareholder-employee must keep records of the vehicle's use for business purposes i.e., records, logbooks and receipts.

Other employees may use PSMRs regardless of the annual distance they travel. Employees and shareholder-employees are treated differently for these purposes because employees are generally subject to control by their superiors with regard to the use of the vehicles. Shareholder-employees are often not subject to the same control.

Reference: HO.TPAH103

Deductibility of Speeding Fine

Section 104 - Expenditure or Loss Incurred in Production of Assessable Income: A farmer who incurred a speeding fine while on a work-related trip asked whether the fine was deductible from his assessable income.

Section 104 of the Act permits the deduction of a loss if it is incurred in the production of assessable income, or necessarily incurred in carrying on a business for the purpose of gaining or producing assessable income. Each case must be examined on its facts to determine whether the loss is sufficiently linked to the taxpayer's income-earning process. In this case, the speeding fine is not deductible as the fine is not sufficiently connected with the farmer's business activities.

Reference: HO.TPAH125

Deduction of PAYE by Home Help Workers

Section 338 - Tax Deductions to Be Made By Employers: An employer asked about the tax implications of payments made to "private domestic workers".

Section 338 of the Act requires employers to make tax deductions from source deduction payments made to employees unless the employees are "private domestic workers". "Private domestic workers" are workers employed, not on a regular full-time basis, to work in the home or grounds of an employer. Private domestic work must not relate to any business of the employer.

Where an employer does not deduct PAYE from source deduction payments, section 355 requires the employee to deduct it. Since their employers do not have to make deductions, private domestic workers must deduct and account for their own PAYE directly to Inland Revenue. They do this by filing an IR 56 form. Inland Revenue will issue an IR 12 showing gross earnings and PAYE for each income year.

Reference: HO.TPA070

Goods and Services Tax Act 1985

Donations to Childcare Centre

Section 2 - Interpretation: A non-profit childcare centre asked about the GST implications of contributions received from parents. The centre asked parents to make a suggested donation reflecting the length of each child's attendance at the centre. However, attendance was not conditional on the receipt of the payment.

Section 2 of the Act defines "unconditional gift" as a voluntary payment to a non-profit body where the person who makes the payment does not receive any benefit in return. For GST purposes, unconditional gifts are not treated as consideration for supplies of goods and services. Therefore, GST does not apply to payments made as unconditional gifts.

In this case, a child's attendance at the childcare centre is not conditional on the parent's donation. The contributions to the centre are unconditional gifts and there is no GST. However, GST would apply if attendance at the childcare centre was dependent upon payment of a fee.

Reference: HO.TPA050

GST on Grants

Section 5(6D) - Payment in the Nature of a Grant or Subsidy: An organisation asked about the GST consequences of receiving a Crown grant. The organisation also asked whether a body which receives grant money on another body's behalf and passes that money on was liable for the GST on the grant.

Section 5(6D) of the Act provides that a grant or subsidy that the Crown or a public authority makes to a person in respect of his/her taxable activity is consideration for a supply of goods and services in the course of the taxable activity. This means that such a grant or subsidy is subject to GST.

If the recipient of the payment is registered or liable to be registered for GST, s/he must account to Inland Revenue for one-ninth of the payment as GST output tax. If the grant is made to a person who is not GST registered (or liable to be so registered), that person does not have to account for GST.

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A body which receives grant money (and passes it on) on another's behalf is not liable to account for GST. The actual recipient of the grant must account for one-ninth of the payment as GST output tax if section 5(6D) applies to the grant.

Reference: HO.TPAH120

Time of Supply of Real Estate

Section 9 - Time of Supply: A vendor of farm land asked whether the time of supply of the farm land (and liability to account for GST) was triggered by the payment of a deposit to his solicitor. The solicitor held the deposit as a stakeholder until the sale contract became unconditional.

Section 9(1) deems a supply to take place at the earlier of the time that an invoice is issued, or the time payment is received for the supply. Where payment is made before the issue of an invoice, a real estate supply is deemed to take place at the time of the payment.

Payment occurs when a deposit is applied for the benefit of the vendor of the real estate (for example, if the deposit is invested in the solicitor's trust account for the vendor's benefit, or paid towards the estate agent's fees). However, where a real estate agent or any other person holds the deposit as a stakeholder only, the deposit is not applied for the benefit of the vendor.

In this case, as the solicitor held the deposit as a stakeholder only, the time of the supply was not triggered by payment of the deposit. The vendor was not required to account for GST at this time. The time of supply will be triggered later when the deposit is applied for the vendor's benefit or an invoice is issued for the supply, whichever is the earlier.

Reference: HO.TPAH123

Temporary Import of Goods for Servicing and Maintenance

Section 12 - Imposition of Goods and Services Tax on Imports: A company asked for an explanation of the GST implications of exported goods that are temporarily returned to New Zealand for repairs and maintenance. The company exported goods which were returned to New Zealand for repairs and maintenance. The goods were sent back to the overseas recipient within 6 months of their arrival in New Zealand.

The GST treatment of imported goods is contained in section 12 of the Act, which the Customs Department administers. The Customs Department have advised that this case would come within section 181 of the Customs Act 1966, which provides that if goods are brought into New Zealand for less than 12 months they are treated as temporarily imported. In these cases, a deposit equal to the sum of GST and duty payable on the value of the goods imported must be paid to the Customs Department. If the goods are removed from Customs Control within the 12 month period after their arrival, the deposit will be refunded.

Any further enquiries should be directed to the Customs Department at the port where the goods are expected to arrive.

Reference: HO.TPA059

GST on Imported Goods

Section 12 - Imposition of Goods and Services Tax on Imports: A taxpayer asked for an explanation of the GST implications of importing a motor vehicle into New Zealand from Australia.

Section 12 of the Act imposes GST on the importation of goods into New Zealand. GST charged under section 12 is levied and collected by the Customs Department.

In this case, GST will be levied at 12.5% of the value of the imported motor vehicle. The value of the vehicle is determined in accordance with section 12(2) as the sum of:

(i) The value of the goods determined in accordance with the Customs Act 1966;

(ii) The amount of duty and tax payable under the Customs Act 1966 and the Dumping and Countervailing Duties Act 1988; and

(iii) The amount paid or payable to transport the goods to New Zealand and to insure the goods.

Reference: HO.TPP091

GST on Garage Sale Items

Section 51 - Persons Making Supplies in Course of Taxable Activity to be Registered: A taxpayer asked whether a person regularly holding garage sales was required to register for GST.

Section 51 of the Act provides that a person carrying on a taxable activity and who has made (or expects to make) supplies with a value exceeding $30,000 in any 12 month period must register for GST. A person carrying on a taxable activity may voluntarily register for GST even if his/her turnover does not reach this level. A taxable activity involves the supply of goods or services on a continuous or regular basis.

Garage sales are usually one-off events held by private individuals to clear unwanted possessions. These sales are not taxable activities as they do not involve regular or continuous supplies of goods. However, if a person holds garage sales on a regular basis, s/he must register for GST if the 12 month turnover exceeds the $30,000 threshold, and can choose to register if the turnover is below this level.

Reference: HO.TPAH110

Stamp and Cheque Duties Act 1971

Conveyance Duty on GST Inclusive Price of Factory Purchase

Section 41 - Valuation GST-Inclusive: A taxpayer who purchased an empty factory asked whether conveyance duty should be charged on the GST inclusive or exclusive value of the factory.

Section 41 provides that the value of property for the purposes of the Act is GST inclusive. Section 41 is based on the premise that conveyance duty is payable on the total amount of consideration paid to induce the vendor to sell. This amount includes GST.

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In this case, the vendor of the factory was registered for GST and the consideration for the sale included GST, so conveyance duty was charged on that GST inclusive amount. Because the purchaser was also GST registered, he could claim an GST input tax credit.

If the sale of the factory had qualified for zero-rating as a supply of a taxable activity as a going concern, conveyance duty would be chargeable on the amount of consideration including GST at zero percent.

Reference: HO.TPAH109

Child Support Act 1991

Child Support Liability when Caring for Invalid

Section 87 - Amendment of Assessments: A liable parent asked whether his child support payments could be reduced to take into account the fact that he cares for his sick elderly mother.

The Child Support Act 1991 contains a formula to calculate the amount of child support that a liable parent must pay. This formula only recognises spouses, de facto partners and children as dependants for this purpose. The Family Court is the only body which can reduce child support liability to take into account special circumstances, such as financial hardship. In this case, the liable parent may apply to the Family Court for an order to depart from the formula assessment contained in the Child Support Act 1991.

Reference: HO.TPAH114

Legal Decisions - Case Notes

Welcome to the second Case Notes column.

We have given each case a rating as a reader guide to its potential importance.

- • • • • •   Important Decision
- • • • •   Interesting Issues Considered
- • • •   Application Of Existing Law
- • •   Routine
- •   Limited Interest

We've given full references to each case, including the citation details where it has already been reported. Details of the relevant Act and section will help you to quickly identify the legislation at issue. Short case summaries and keywords deliver the bare essentials for busy readers. The notes also outline the principal facts and grounds for the decision. Where possible, we have indicated if an appeal will be forthcoming.

These case reviews do not set out Inland Revenue policy, nor do they represent our attitude to the decision. These are purely brief factual reviews of decisions for the general interest of our readers.

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Income Tax Act 1976

Case: TRA No 94/92 Case Q5 (1993) NZTC 5,044

Rating: • • •

Act: Income Tax Act 1976 - Sections 65 and 106

Keywords: *Share trading loss, business of share dealing, circulating capital*

Summary: In circumstances where taxpayers are in the business of share dealing, share trading losses are deductible.

Facts: The objectors sought to deduct share trading losses from other taxable income.

Decision: One of the objectors had accumulated experience and skill in money management with a history of similar acquisitions and sales of assets for the purposes of capital gain. The change to investing in publicly listed shares was accompanied by actions that showed that this objector had approached the activity in a businesslike manner. The objectors studied the background of the leading directors and kept notes of the performances of each company in which they had an interest. They also kept graphs and charts of what they took to be market trends. Before embarking on the scheme, the parties discussed it with the Commissioner. The objectors were told that tax would be payable on gains, and losses made would be deductible.

Judge Willy decided that the objectors were engaged in the business of share dealing. He referred to the business discussion in *CIR v Stockwell* (1992) 14 NZTC 9,1809 (CA) and the circulating capital asset discussion in *CIR v Inglis* (1992) 14 NZTC 9190.

Comments: Inland Revenue has not decided whether to appeal this decision.

References: Technical Rulings 12.9.5; 12.9.5.1; 12.9.5.2; 12.9.5.3; 12.9.6.

Case: TRA No. 91/159 Case Q9 (1993) 15 NZTC 5,055

Rating: • • •

Act: Income Tax Act 1976

Keywords: *restraint of trade agreement, capital*

Summary: Payment was made to an actor under a restraint of trade agreement in respect of two television commercials. The actor agreed not to endorse or promote any other type of competitive product. The payment was capital and non assessable.

Facts: The objector was an actor. He entered an agreement with an advertising agency to make two television commercials for a client of the agency. He received $25,000 for the first year the commercials were shown on television and $17,500 for the second year the commercials were used. In return for these two payments, the actor agreed to a restraint of trade clause. He would not be associated with the promotion in New Zealand of any product or brand of good which was similar to, or in competition with, the type of good he had advertised.

Decision: Judge Willy found that the advertising agency and client wished to obtain the actor's services for two years clear of competition from any other manufacturer of a similar product. The Judge held that the restraint of trade clause was the fullest possible restraint which the client sought to obtain from the objector. The Judge referred to Public Information Bulletin No 138 and held that the payment, less $5,000 acting fee, was clearly capital in nature.

Comments: Inland Revenue is appealing this decision.

References: Technical Rulings Chapter 56.9.17

Case: Brierley Investments Ltd v Bouzaid & Henry
HC Wellington CP 352/89 - McGechan J

Rating: • • • • •

Keywords: *administrative law, judicial review, fairness, legitimate expectations*

Summary: Brierley Investments Ltd applied unsuccessfully on grounds of administrative "unfairness" for judicial review. They sought review of Inland Revenue's decision to re-examine the use of their longstanding tax accounting formulae. The Court held that there were circumstances in which judicial review could be available. It held that BIL had failed to prove unfairness or error on the facts.

Facts: The Respondents represent the Commissioner of Inland Revenue, ("CIR"). The Applicant, Brierley Investments Limited, ("BIL"), alleged that formulae relating to deductibility and capital/revenue apportionment were agreed with the Commissioner, (or at least that the Commissioner accepted their use), and BIL relied upon them as future guidelines. The Commissioner contended that any agreement related to specific income years only. The Commissioner wished to review the use of the formulae before 1990, and to determine a suitable future basis for assessment.

In 1969 BIL consulted extensively with Inland Revenue. An "agreed basis" was reached for determining the deductibility of interest and other expenditure for the income years between 1963-1967. BIL has continued to rely on this basis since 1969.

An investigation between 1970-73 led to a decision by Inland Revenue to use a further "agreed basis" to determine capital and income on the disposal of shares. Inland Revenue issued amended assessments for the years 1964-1970, applying this formula. BIL objected, but did not ultimately pursue the objection.

Between 1975 and 1986 BIL used both formulae for tax accounting purposes. There was no critical examination of the returns. Contact between BIL and Inland Revenue took place at a purely administrative level, and was routine and low-key. In 1987, an inspector made an investigation of BIL aimed at other specific issues. While some discussion of the formulae took place, it was not the focus of the inspector's inquiry, and she did not confirm the validity of the general approach to deductibility questions.

In 1988, Inland Revenue notified BIL of their intention to investigate the company. In 1989 they confirmed unrestricted investigations would be carried out over the years before 1990. The investigations would include a review of the use of the formulae. BIL objected to the scope of the investigations, including the review of the formulae, which they claimed they were entitled to use before 1990.

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Decision: BIL argued, principally on the basis of administrative "fairness" that the Commissioner could not reopen the question of the right to use those formulae. BIL considered that they had consistently applied the formulae approved by the Commissioner. The Commissioner had acted inconsistently with representations made, and it was "unfair" that the Commissioner was attempting to deprive BIL of the expectation that the formulae would continue to be applied for the years before 1990. BIL accepted that the investigation could examine the proper application of the formulae in those years.

Mr Justice McGechan held that the remedy of judicial review could be available in the course of reaching an assessment where discretion were being exercised. He drew the distinction between challenging the use of discretion, (powers), in the pre-assessment process, where judicial review is available; and the assessment situation, where judicial review is not available and the Commissioner is acting under a mandatory statutory duty. He held that the Commissioner's duty to act fairly may well extend beyond the area of breach of contract or breach of representations, to the defeat of legitimate expectations.

After reviewing the facts, His Honour held that BIL had failed to prove that there was an agreed basis or representation establishing either formula. The Commissioner made no clear statement to BIL, nor was there such a representation. There was no basis for constructing a legitimate expectation. BIL failed to prove unfairness or error. BIL chose to take a business risk not to obtain a written confirmation of its assumptions. That risk came home.

The findings of fact meant that the authorities relating to judicial review in cases of "unfairness" did not need to be explored. His Honour referred to a number of cases in which the need for both full disclosure by a taxpayer, and a clear or explicit ruling by Inland Revenue were required before a binding commitment would arise.

Comments: The taxpayer will be appealing this decision.

Goods and Services Tax Act 1985

Case: TRA No. 89/230

Rating: • • •

Act: Goods and Services Tax Act 1985 Sections 2,6,8,9,10,14,20,24,26

Keywords: *GST liability for consultant's commission*

Summary: The objector was liable for GST on his commission on consultancy services for assisting in the sale of a rural landfill property.

Facts: The objector arranged convoluted transactions for the sale of a rural landfill property at a price of $4,922,700. He had paid $160,000 for the property less than a year earlier. The process of arranging the sale transaction continued for at least 3 months.

On settlement, the objector became entitled to a "commission" of $500,000: $50,000 in cash, and a sub-mortgage of $450,000 against the vendor's second mortgage over the property. He never received the $450,000.

Decision: The major issue was whether the objector was liable to GST on this service of arranging the sale. Judge Barber decided the objector was liable.

Judge Barber rejected the objector's argument that his involvement in the sale was not a taxable activity. The services were carried on continuously or regularly over an appreciable period, and involved several steps and arrangements.

He also rejected the argument that as the services were carried out under a written contract of service they were exempt under section 6(3)(b). Instead of finding any evidence of a contract of employment or service, he found that the objector was retained as some type of consultant or commission agent.

He also rejected the argument that the arrangements comprised an exempt financial transaction under section 14, as a supply of financial services. He found that the objector received the commission for arranging the sale, not for arranging finance for the purchase.

The fact that the objector did not receive the $450,000 balance of his commission was not relevant, as the sub-mortgage for that amount comprised part of the consideration for his services.

The objector could not obtain a bad debt deduction for the $450,000 as he had not fulfilled the requirements of section 26. He had not furnished a return or accounted for the output tax as required, nor proved that he had written off the amount as a bad debt. He had capitalised the debt at settlement, so it was a capital loss, and not a bad debt. The Commissioner's assessments were also largely confirmed in relation to the lesser issues. The objector had not complied with the invoicing requirements of section 24, and was unable to prove that various amounts were not part of a taxable activity.

Comments: The taxpayer is appealing this decision.

References: Technical Rulings Chapter 107.9

Case: TRA No. 91/140

Rating: • • •

Act: Goods and Services Act 1985 - Sections 2 and 5(6D)

Keywords: *GST on grants, Public Authority, lodgement of objection*

Summary: This case concerns the retrospective application of section 5(6D) to grants made by the Departments of Social Welfare and Education.

Facts: The taxpayer is a branch of a Christian church. The taxpayer operates a childcare centre for which it receives grants from the Education Department and the Department of Social Welfare. The childcare centre operated on a break even basis and the taxpayer set the fees to achieve this aim.

The Government grants originally subsidised the staff wages. However from February 1990 the grants changed to an all-encompassing subsidy for the general operation of the childcare centre and for the upgrading of the facilities.

The taxpayer considered such grants were exempt of GST. Inland Revenue disagreed and issued assessments for the periods ending 31 October 1986 to 31 August 1990. The taxpayer objected to the assessments on 21 December 1990.

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The Goods and Services Tax Amendment Act (No.3) 1991 amended section 5 by inserting section 5(6D). Before this amendment, there was no GST liability on governmental grants or subsidies to a non profit body for the supply of goods and services to others. Section 5(6D) now imposes a liability for GST on governmental grants or subsidies paid to non profit bodies, where they carry on a taxable activity in supplying goods and services to others. This section deems the grants and subsidies to be consideration for the supply of goods and services.

This new section had no effect on any taxable period for which a taxpayer had lodged an objection before 19 December 1990.

Decision: Barber DJ concluded that the Departments of Education and Social Welfare were clearly "Public Authorities" within the meaning of the Act, and that section 5(6D) applied to the grants received by the taxpayer.

The date an objection is lodged with Inland Revenue is the date on which Inland Revenue receives the objection. In this case, we received the objection after the prescribed date so section 5(6D) will apply.

Comments: We do not know whether the taxpayer will be appealing this decision.

References: Technical Rulings Chapter 108.10

Child Support Act 1991

Case: B v C of IR (1993) 15 NZTC 10,015

Rating: • • • •

Act: Child Support Act 1991 Section 105

Keywords: *Special circumstances, commitments of the parent necessary to support herself, unjust and inequitable*

Summary: This was an appeal against a Family Court judgment which declined an application for a departure from the formula assessment by the CIR under the Act. The High Court dismissed the appeal.

Facts: The applicant was assessed to pay child support of $297.10 per month, under section 29 of the Act. She sought a departure order under section 106 to reduce her contribution to the minimum figure prescribed by section 29, $520 per annum. The applicant owns the former family home. The property is worth $165,000 and there is a mortgage on the property for $38,000. The applicant gave evidence that although she lived modestly and worked two jobs she was unable to make ends meet. She incurred a weekly deficit of $35.

The Family Court Judge stated that he was unable to conclude that "special circumstances" existed or that the applicant had made out either of the grounds in s105(a)(iii) (A) or (c)(i). The Judge held that the necessary commitments of the applicant did not significantly reduce her capacity to provide financial support. The commitments towards the house were not wholly necessary in the sense that the applicant did not require a property of that scale. The Judge also held that the formula assessment did not result in an unjust and inequitable determination of the level of financial support to be provided by the applicant. This was because the house was costing the applicant more than was required to provide

her with a reasonable level of accommodation. Alternatively, the house could be used as a source of additional income.

Decision: The applicant argued that the Family Court Judge had misinterpreted or misapplied the special circumstances requirements and that he had misdirected himself as to the objects of the Act. The High Court dismissed the appeal. The High Court agreed with the Family Court Judge's interpretation of the legislation and held that one of the objectives of the legislation is to induce parents to alter their priorities. The High Court held that where income is insufficient to meet outgoings, unless there is something more to take the case out of the ordinary, this will not fulfil the requirements of "special circumstances".

Comments: We do not know whether the taxpayer will appeal this decision.

References: Technical Rulings Chapter 64

Estate and Gift Duties Act 1968

Case: Estate R.E. Turner v CIR High Court M43/92

Rating: • •

Act: Estate & Gift Duties Act 1968 - Sections 7, 26, 92

Keywords: *Dutiable estate; Passing of property; Contingency; Jersey customary law*

Summary: A widow was the sole beneficiary and administrix of her husband's estate. She claimed that the Commissioner should have deducted the value of her dower rights over her husband's land on the island of Jersey from the dutiable estate.

Facts: Under Jersey law, there is a customary dower right. Under this right, the widow has a right to the life enjoyment of one third of her husband's real property owned at the time of his death. The Commissioner assessed the husband's estate for estate duty on the whole value of land on the island. The widow objected on the basis that the value of her dower rights should not have been taken as part of the dutiable estate.

Decision: Under the legislation, the dutiable estate of a deceased person includes all property that passes under his/her will or intestacy. The Court held that the property that passed in this case included the deceased's interest in the land on Jersey, but subject to the widow's customary dower right under the Land Law of Jersey. An opinion from Jersey solicitors was tendered by the administrix (and accepted by the Commissioner and the Judge) as evidence that the Law of Jersey treated such a dower right as a legal (or equitable) interest in property. This right arose on the deceased's death, was quantified in law and protected by a legal charge.

The appeal was allowed. It was held that the Commissioner should deduct the value of the widow's right from the dutiable estate.

Comments: Inland Revenue has not decided whether to appeal this decision.

References: Technical Rulings 69.10

Due Dates Reminder

March

5 PAYE deductions and IR 66ES for last 13 days of February 1993 due - "large" employers only.

7 First instalment of 1994 Provisional Tax due for taxpayers with November balance dates.

Second instalment of 1993 Provisional Tax due for taxpayers with July balance dates.

Third instalment of 1993 Provisional Tax due for taxpayers with March balance dates.

Annual income tax returns due for non-IR 5 taxpayers with balance dates from 1 to 30 November 1992.

20 RWT on Interest deducted during February 1993 due for monthly payers.

RWT on Dividends deducted during February 1993 due.

Non-Resident Withholding Tax (or Approved Issuer Levy) deducted during February 1993 due.

PAYE deductions and IR 66ES for first 15 days of March 1993 due - "large" employers only.

PAYE deductions and IR 66ES for February 1993 due - "small" employers only.

Gaming Machine Duty return and payment for month ended 28 February 1993 due.

31 GST return and payment for period ended 28 February 1993 due.

April

5 PAYE deductions and IR 66ES for last 16 days of March 1993 due - "large" employers only.

7 First instalment of 1994 Provisional Tax due for taxpayers with December balance dates.

7 Second instalment of 1993 Provisional Tax due for taxpayers with August balance dates.

Third instalment of 1993 Provisional Tax due for taxpayers with April balance dates.

First 1994 Student Loan interim repayment due for periodic payers with December balance dates.

20 PAYE deductions and IR 66N/IR 66W for first 15 days of April 1993 due - "large" employers only. *(Please note that from this payment date onwards, student loan repayment deductions and child support deductions may be due at the same time.)*

PAYE deductions, IR 66N and IR 66ES for March 1993 due - "small" employers only.

Completed Deduction Certificates for year ended 31 March 1993 should have been distributed to all employees.

RWT on Interest deducted during March 1993 due for monthly payers.

RWT on Interest deducted from 1 October 1992 to 31 March 1993 due for six-monthly payers.

RWT on Dividends deducted during March 1993 due.

Non-Resident Withholding Tax (or Approved Issuer Levy) deducted during March 1993 due.

FBT return and payment for quarter ended 31 March 1993 due.

Annual Nil FBT return (1 April 1992 to 31 March 1993) due for employers who pay no fringe benefits.

Gaming Machine Duty return and payment for month ended 31 March 1993 due.

30 GST return and payment for period ended 31 March 1993 due.

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