Certifying NZ taxpayer as a taxable person in order to recover VAT refund from European Community

Information needed by Inland Revenue in New Zealand

Summary

This item sets out the details that Inland Revenue needs in order to certify that a taxpayer is a taxable person. A taxpayer will need such a certificate to get a refund for VAT paid on goods and services in countries that are members of the European Community.

Inland Revenue needs these details from a taxpayer who is seeking such a certificate:

- the taxpayer's name
- the nature of the taxpayer's activity
- the address of the taxpayer's establishment, central place of management, or place of abode
- the taxpayer's IRD number.

Background - the European Community Directives

The European Community (EC) has issued a series of directives which cover the taxation of the citizens of its territories. For VAT purposes, the directives require members of the EC to refund VAT to a "taxable person" in other EC member states and in non-member states.

For the purposes of the EC directives, a taxable person is any person who carries on any economic activity in the form of a producer, trader, or supplier of services. These activities include mining and agricultural activities and the activities of the professions.

A taxable person must prove that he or she is a taxable person of a state by producing a certificate or letter from the official tax authority of that state which confirms these details:

- that the person is carrying on an economic activity in that country
- that the person is a registered taxpayer in that country.

A certificate or letter is effective for one year.

European Directive 13 permits European countries to refund VAT to taxable persons who are established in countries outside the EC. This directive deems a person to be established outside the EC if that person does not have any of the following in the territory of the community:

- A business or a fixed establishment from which business transactions are effected
- A permanent address
- A usual place of residence.

Further, in order to qualify these are the only goods or services that the person may supply to the country of the EC:

- transport services and ancillary services
- services on which tax is payable solely by the recipient.

Information taxpayers need to supply to Inland Revenue

If you want a letter from Inland Revenue to confirm that you are carrying on an economic activity, contact Taxpayer Services at your local Inland Revenue office. You will need to supply this information:

- your name
- the nature of your activity
- the address of your establishment, or its central place of management, or your permanent residential address
- your IRD number.

Occasionally, Inland Revenue may have trouble certifying that an economic activity existed during the relevant period. If that happens, we may ask you to provide documents which show that you were running an economic activity, such as cashbooks, bank statements, insurance policies and/or ledgers.

If you need further information on how to get a VAT refund from an EC country, ask your accountant or other tax adviser.

Details to be supplied to Inland Revenue when seeking a deduction for payments to spouse

Summary

This item states the Commissioner's current policy on the information that a taxpayer must supply when he or she seeks to claim a deduction for payments made to a spouse.

All legislative references in this item are to the Income Tax Act 1976.

Legislation

Section 106(1)(d) states that a taxpayer cannot claim a deduction for:

(d) Payments of any kind made by a husband to his wife or by a wife to her husband:

Provided that, with the consent of the Commissioner granted before the deduction is claimed by the taxpayer, and subject to section 97 of this Act, a deduction may be made in respect of any payment made by a husband to his wife or by a wife to her husband where the Commissioner is satisfied that the payment is for services rendered (not being domestic services or services performed in connection with the home) or is otherwise a bona fide payment, and that the payment was exclusively incurred in the production of the assessable income of the husband or wife, as the case may be, for the income year.

In summary, all of these conditions must be met before the Commissioner will allow a deduction for a payment to a spouse:

- The taxpayer must get the Commissioner's permission to claim a deduction before claiming it.
- The payment must not be excessive - section 97 effectively allows the Commissioner to disallow so much of the deduction for wages as he considers exceeds a reasonable amount, having regard to the nature and extent of the services the spouse performs.
- The payment must be for performing non-domestic services by the spouse, or otherwise be a bona fide payment. A deduction may be allowed for domestic services if the taxpayer is a farmer and the spouse cooks for permanent farm employees. Such a deduction will only be allowed if the taxpayer complies with normal employer obligations. See page 5 of TIB Volume Six, No.1 (July 1994) for further information.
- The taxpayer must incur the payment exclusively in the production of assessable income for the year.

Policy

Procedure

To ascertain whether the payment meets the requirements of section 106(1)(d), the Commissioner requires the taxpayer (or agent) to complete and sign a declaration which sets out these details:

- the nature of the business in which the spouse is employed
- precise details of the duties carried out by the spouse
- the hours worked by the spouse during an average week and the number of weeks worked during the year
- details of other labour employed by the taxpayer and amounts paid as wages
- the method of payment to the spouse (e.g. cash at regular intervals or periodically, or by crediting an account)
- the amount of wages to be paid to the spouse.

If you want to find out how to make such a declaration, contact Taxpayer Services at your local Inland Revenue Office.

Method of payment

In most cases there must be an actual payment of wages to the spouse, rather than the crediting of an account. The essential consideration is that the spouse must have a say in the disposal or control of the wages. The crediting of an account will be acceptable if both of these conditions are met:

- The spouse has control over the wages and consents to them being used in a certain way.
- The spouse signs a statement which sets out how the wages will be paid and used, and submits this with the completed declaration (which is otherwise in order).

In some cases the spouse may not be paid until after finishing the work, in order to tie in with cash flows. (This may be the case when the work is seasonal work.) So long as the payer complies with the other requirements relating to the payment of a spouse this will probably not cause a problem.

Excessive payments

To determine whether a payment to a spouse is excessive, the Commissioner uses as a guide the current level of wages paid for comparable services in an arm's length transaction.

When to apply for approval

The taxpayer must apply for approval before claiming for a deduction. The application may be for payments the taxpayer has actually made during the year or for payments the taxpayer will make in the future.

Increase in spouse's wages

If the spouse's wages increase because of an increase in duties or some other similar reason, the taxpayer will need to complete a further application for approval.

However, if the wage increase is because of a general wage increase in the particular occupation, the taxpayer won't need to re-apply for approval. In this situation the taxpayer should note the reason on the return form.

Taxpayer's obligations

The taxpayer must satisfy normal employer obligations if the Commissioner grants approval for the deduction. Specifically, the spouse must complete an IR 12 and the taxpayer must deduct PAYE (including ACC premiums) from the wages, and pay it to Inland Revenue. The taxpayer must actually pay the spouse a genuine wage on a regular basis (in the same manner as payments to other employees).

Example 1

May employs her husband Jim to drive the delivery truck for her furniture business during his weekends. She pays Jim market-rate gross wages of $120 per week. She deducts PAYE and ACC premiums and pays him by cheque at the end of each month. At the end of the income year, before filing her income tax return, May applies to the Commissioner for approval of the deduction of Jim's wages.

This approval is granted for these reasons:

- The services which Jim performs are not domestic services, and May's business incurs the payment exclusively in the production of assessable income.
- May supplies the required details about Jim's employment to Inland Revenue.
- The payment is not excessive compared with the level of wages paid to people who perform similar services in an arm's length transaction.

May deducts the wages of $6,240 ($120 per week) from her income.

Example 2

In the next income year Jim agrees to do the accounts for May's business as well as the deliveries. May increases his gross wages to $800 per week because of the increase in his duties (market wages for the hours and duties performed by Jim are $400 per week). She does not get the Commissioner's approval to deduct the increased payment before furnishing her income tax return.

May deducts the full amount of the payments to Jim in her annual tax return. The extra deduction is not allowed because May did not receive the Commissioner's approval before claiming the deduction.

Even if May had applied for the Commissioner's approval before increasing the payments it is likely that the full increase would not have been approved. This is because May's payment to Jim is well above the market rate paid to an arm's length employee. Section 97 states that the Commissioner can disallow so much of the deduction as he considers is excessive.

GST and debt collection services

Introduction

This item states the Commissioner's current policy on how goods and services tax (GST) applies to services provided by debt collection and other agencies. It deals specifically with these activities:

- debt collection
- credit reporting
- mercantile activities such as process serving, investigations and tracing of debtors, and repossessions.

The item also discusses how GST applies to legal services acquired by debt collection agencies. Such treatment will depend on whether the agency acquires the services as principal or as an agent of the person seeking to recover the debt.

All legislative references in this item are to the Goods and Services Tax Act 1985.

Legislation

Section 14 provides that certain supplies are exempt from GST. Such exempt supplies include (under section 14(a)):

> The supply of any financial services (together with the supply of any other goods and services, supplied by the supplier of those financial services, which are reasonably incidental and necessary to that supply of financial services) ...

Section 3(1) defines the term "financial services" to include:

> (ka) The payment or collection of any amount of interest, principal, dividend, or other amount whatever in respect of any debt security, equity security, participatory security, credit contract, contract of life insurance, superannuation scheme, or futures contract:
>
> (l) Agreeing to do, or arranging, any activities specified in paragraphs (a) to (ka) of this subsection, other than advising thereon.

Policy

Debt collection

Services in relation to agreeing to or arranging the payment or collection of any outstanding debt constitute "financial services" under section 3(1)(ka) and (l), so they are exempt supplies under section 14(a) and not subject to GST.

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Debt collection agencies often use legal services to arrange the collection of outstanding debts. Some debt collection agencies retain their own in-house legal staff. Others engage independent solicitors to undertake the necessary legal work.

If the debt collection agency engages the services of an outside law firm, the debt collection agency generally passes those costs on to the client (that is, the person seeking to collect the debt) as disbursements. These legal services constitute taxable supplies by the law firm in the course of its taxable activity, so they are subject to GST. They are not "financial services" under the section 3 definition and are not exempt from GST. The outside law firm is providing a legal service, not arranging the collection of the debt. The debt collection agency is not the supplier of these services, so it cannot be said that it is supplying services that are "reasonably incidental and necessary" to the supply of financial services under section 14(a).

A debt collection agency can act as agent or principal in acquiring the legal services from the outside law firm. TIB Volume 6, No. 1 (July 1994) at page 5 discusses how the GST Act applies to disbursements made by professional firms on behalf of their clients. The TIB item discusses the treatment of payments made by professional firms as agent and payments made as principal. The same treatment applies to debt collection agencies:

- If the debt collection agency acts as a principal in receiving the supplies from the outside law firm, the debt collection agency cannot claim an input tax credit on the GST relating to the legal services. These services are not acquired for the principal purpose of making taxable supplies. Rather, the services are acquired for the principal purpose of making exempt supplies of debt collection services.
- If the debt collection agency is acting as the agent of its client, section 60(2) applies to deem the supply to have been made to the client. The client may deduct input tax on the supply if the client acquired the legal services for the principal purpose of making taxable supplies.

If the debt collection agency provides its own in-house legal services, the use of those services in collecting debts may form part of the supply of an exempt "financial service". However, if the debt collection agency receives specific instructions to provide legal services, as opposed to the general instruction to collect a debt, the supply of these legal services is subject to GST. This might include the situation in which the agency's legal staff are engaged specifically to take court action in order to recover the debt. This ensures that the same treatment applies to both solicitors and debt collection agencies when only legal services are performed.

Credit reporting

Credit reporting involves the provision of certain financial and credit information upon which creditors assess credit applications. These services are exempt if they are provided to a client in the course of collecting a debt. They are regarded as being reasonably incidental and necessary to the debt collection activity and part of the supply of financial services. However, if the services are undertaken in isolation, they are subject to GST.

Mercantile activities

Mercantile services are services generally undertaken as part of the debt collection process. In some instances, mercantile services do not relate to financial transactions and are undertaken in isolation. Investigation and document servicing in relation to matrimonial or criminal matters are examples. The following commentary discusses mercantile activities in relation to the credit industry.

Process services

This activity involves the serving of notices of legal proceedings on defendants or debtors in actions for the recovery of money. The service of debt recovery notices is a task that debt recovery agencies may either undertake themselves or contract out.

When this activity is undertaken as part of the general debt recovery process (that is a client has engaged the agency to recover a debt) the service is part of a "financial service" and is exempt from GST. The service is considered to be reasonably incidental and necessary under section 14(a) to the supply of financial services (being the collection of the debt).

If the service is performed in isolation (that is, the agency or contractor is only instructed to serve the notice), the activity is taxable and the supply is subject to GST.

Investigations and tracing of debtors

This service involves the location of missing debtors by a person such as a mercantile agent, debt collector, or a licensed private investigator so that debt collection action can be commenced or legal documents served.

When the location of a missing debtor is undertaken as part of the debt recovery process, the service is part of the financial service under section 3(1)(ka) and (l), and is therefore exempt. The service is regarded as being reasonably incidental and necessary to the collection of the debt under section 14(a).

If the search for the debtor is undertaken in isolation (that is the agency is only instructed to locate a person), the service is subject to GST.

Repossessions

Repossessions are seizures by agents of credit cards or of chattels which are security for loan advances; they are generally performed by the agents for the lender or vendor of the chattels.

When a debt collection agency is engaged to repossess property offered as security for a loan, the services constitute taxable supplies and are subject to GST. The services constitute the recovery of goods rather than the collection of debt. They are therefore beyond the scope of the term "financial services" in section 3(1)(ka) and (l). Any ancillary service charges relating to the repossession (such as tracing the debtor etc.) are also subject to GST.

When an agency is engaged to repossess secured assets or chattels, and the debtor instead pays the outstanding debt, the service supplied by the agency is still subject to GST. The primary service provided by the agency is the repossession of the secured assets or chattels, rather than the collection of a payment. In other words, the repossession activity is not something which is reasonably incidental and necessary to the supply of financial services (being the collection of the debt) within the terms of section 14(a). The agency is not arranging or agreeing to collect a debt, but is arranging or agreeing to repossess goods.

Assessability of lump sum and pension payments made to employees and past employees

Summary

This item states the Commissioner's current policy on the tax treatment of lump sum and pension payments that employers make to employees and past employees. The Commissioner's policy is that all of these payments made in respect of employment are assessable, regardless of whether they are made under a contract or voluntarily.

All legislative references in this item are to the Income Tax Act 1976.

Background

Employers may pay pensions or lump sums to current or past employees. Some employers may choose to make payments which they are not required to pay under an employment contract. Employers and employees need to know whether these payments are assessable income.

Legislation

Section 65(2) lists amounts which are included in assessable income. Monetary remuneration is included under section 65(2)(b), and pensions under section 65(2)(j). "Monetary remuneration" is defined in section 2:

> "Monetary remuneration" means any salary, wage, allowance, bonus, gratuity, extra salary, compensation for loss of office or employment, emolument (of whatever kind), or other benefit in money, in respect of or in relation to the employment or service of the taxpayer; ...

"Salary or wages" is also defined in section 2. Amongst other things, it includes:

> (b) A periodic payment by way of superannuation, pension, retiring allowance, or other allowance or annuity in respect of or in relation to the past employment of that person or of any person of whom that person is or has been the wife or husband or a child or dependant; and...
>
> (bb) An ex gratia payment that is a pension within the meaning of section 65(1B) of this Act; ...

The section 65(1B) meaning of "pension" includes any payment which a taxpayer receives from any person for whom the taxpayer (or certain family members of the taxpayer) has rendered past services if, in the Commissioner's opinion, the payment would not have been made if those past services had not been rendered.

Policy

The definitions of "monetary remuneration", "salary or wages", and "pension" within the meaning of section 65(1B) include lump sums and pensions in respect of or in relation to employment. A lump sum or pension payment made by an employer to an employee in respect of or in relation to employment is monetary remuneration or a pension within the definition of those terms, and is assessable to the recipient under sections 65(2)(b) or 65(2)(j) respectively.

The Commissioner's view is that it makes no difference whether the employer pays the lump sum or pension payment voluntarily or under a contract. If the payment is made in respect of or in relation to employment, it is assessable. Similarly, it makes no difference if the employee is a current or past employee, or if the services are provided to someone other than the employer. If an employer makes a lump sum or pension payment in respect of or in relation to an employment relationship, the payment is assessable.

Example

Agnes worked for a church for 20 years. The church rules enable a committee of church members to pay a pension to retired church workers. Pensions are paid at the discretion of the committee and no employee can regard the pension as an entitlement. The committee's rules state that each case is considered on its merits, and payment of a pension to one retired worker does not establish a precedent for any other worker.

When Agnes retired she was granted a pension until death. The committee considered Agnes' length of service made her deserving of a pension.

The pension is assessable. It is monetary remuneration because it is paid in respect of or in relation to Agnes's employment with the church. It makes no difference that the pension was paid at the discretion of the committee.

Revocation of qualifying company election - payment of qualifying company election tax

Summary

This item outlines how the legislation dealing with the revocation of qualifying company status affects the payment of qualifying company election tax (QCET).

Generally, to remove a company's QCET liability, the shareholders or directors of the company must revoke their qualifying company election before the end of the income year in which QCET is payable.

An exception applied when companies became qualifying companies under the transitional provisions in the 1992-93 income year. The transitional provisions allowed such companies to delay paying QCET until the 1993/94 income year. A revocation of qualifying company status made in that income year was too late to remove the QCET liability.

All legislative references in this item are to the Income Tax Act 1976.

Background

The qualifying company regime applies from the 1992/93 income year. It allows closely held companies and their shareholders to be treated in a similar way to partnerships for tax purposes.

Legislation

The legislation governing the qualifying company regime is contained in sections 393 to 393U. The transitional provisions are contained in sections 393S to 393U. We haven't quoted the legislation in this item; our intention is to outline how relevant parts of the legislation apply.

Application

To become a qualifying company, a company must first meet the requirements of the qualifying company regime. (For full details of requirements see the Qualifying Companies Guide - IR 4PB - or items in TIBs Volume Three, No.7 (April 1992) and Volume Four, No.5 (December 1992)).

Secondly, all the directors of the company and all shareholders who are *sui juris* (of legal capacity) must make written elections. The shareholders must also elect to be personally liable for a share of the income tax payable by the qualifying company. However, a majority shareholder can elect that a company becomes a qualifying company (but not a loss attributing qualifying company) on behalf of any minority shareholder and bear that shareholder's liability.

Effective date of election to become a qualifying company

An existing company's election to become a qualifying company takes effect on the first day of the income year following the income year in which the Commissioner receives the election, unless a later income year is chosen in the election.

However, if the election is made in the first income year in which a company is required to file a tax return, the company can choose for the election to take effect from the start of that income year.

Payment of QCET

When an existing company becomes a qualifying company, it becomes liable to pay QCET. Any QCET payable is due by the terminal tax due date for the income year before the income year in which the election to become a qualifying company took effect. This means QCET is payable in the year the company becomes a qualifying company.

QCET is charged at 33% and calculated by applying the QCET formula. (See IR 4PB booklet or TIBs Volume Three, No.7 (April 1992) and Volume Four, No.5 (December 1992) for full details.) The application of the formula is similar to a notional winding up of the company.

Example

Small Co has a 31 March balance date. Small Co's shareholders and directors elect on 4 March 1994 for it to become a qualifying company. The election takes effect from 1 April 1994, the beginning of the company's 1994-95 income year. Any QCET payable is due by 7 February 1995, the terminal tax date for the company's 1993-94 income year.

Voluntary revocation of qualifying company election

If a qualifying company wants to cease being a qualifying company, the initial election made to become a qualifying company has to be revoked. The election can be revoked voluntarily by the directors or the shareholders. A voluntary revocation of an election to become a qualifying company takes effect from the first day of the income year in which the Commissioner receives it (unless a later income year is specified).

Deemed revocation of qualifying company election

A deemed revocation of an election occurs by default if a company no longer meets the qualifying company requirements or there if is a specified change in the ownership structure or status of shareholders. A deemed revocation generally takes effect from the first day of the income year in which the event generating the deemed revocation occurred. However, any deemed shareholder revocation is given a period of grace before it takes effect. The period of grace is 12 months in the case of the death of a shareholder, and 63 days in all other cases. This period gives the shareholders time to take action to prevent the loss of the qualifying company status.

Effect of revocation on QCET liability

A revocation made at any time before the end of the income year in which QCET is payable normally removes a company's QCET liability. This occurs because the effect of the revocation is that the company becomes a non-qualifying company throughout the income year in which the revocation was made. If such a revocation is made after QCET has been paid, the QCET must be refunded.

Example

Small Co became a qualifying company from the beginning of the 1994-95 income year and has to pay its QCET by 7 February 1995. On 13 January 1995 Small Co's shareholders realise the company does not have enough money to pay its QCET and revoke their election. Small Co has its liability for QCET cancelled and is treated as an ordinary company for the 1994-95 income year.

Transitional provisions

The transitional provisions that applied to qualifying companies in the 1992-93 income year allowed elections to take effect earlier and the payment of QCET to be delayed.

Qualifying company elections that were made by 31 March 1993 could take effect from the beginning of the 1992-93 income year, unless a later year was specified.

However, the QCET resulting from an early election did not have to be paid until the 1992-93 terminal tax date (7 February 1994 for most balance dates). Once the 1993-94 income year had started it was, therefore, too late for the directors or shareholders to cancel QCET by revoking their election. Revocations made during an income year can take effect only from the first day of that income year.

Because extra time was allowed for the payment of QCET, interest was charged at the specified rate (6%) from the third 1992-93 provisional tax payment date (7 March 1993 for a March balance date) until the earlier of the date QCET was paid or the 1992-93 terminal tax date.

QCET payable for the 1992-93 income year was also calculated at a concessional rate of 7.5% rather than 33%.

Example

On 10 March 1993 the shareholders and directors of Tight Co elected that it become a qualifying company. This election took effect from 1 April 1992. QCET and interest accrued from 7 March 1993 were payable by 7 February 1994.

On 14 January 1994 the directors realised Tight Co had insufficient money to pay its QCET and revoked their election. However, the revocation could only take effect from 1 April 1993. Tight Co's QCET liability could not be cancelled because it had been a qualifying company during the 1992-93 income year.

Penalties

Unpaid QCET is treated as unpaid terminal tax for the purpose of calculating penalties. An initial penalty of 10 percent applies if QCET is not paid by the due date. A further penalty of 10 percent of the total amount outstanding is added every six months while any amount remains unpaid.

Forms to be filed

To revoke a qualifying company election voluntarily, the directors or shareholders must fill out the IR 4PR "Revocation of Qualifying Company Election" form and return it to the Commissioner.

If a company is a loss attributing qualifying company, the IR 4PA "Revocation of Loss Attributing Qualifying Company Election" form is required instead. To revoke a foreign loss election only, section two of the IR 4PF "Foreign Loss Election/Revocation" form must be returned.

GST general time of supply rules - receipt of deposits

Summary

This item states the Commissioner's current policy on how the Goods and Services Tax Act 1985 applies when a supplier receives a payment for the supply of goods and services. It discusses the correct taxable period in which to account for GST. It also discusses the effect of a deposit being held by a stakeholder. A stakeholder may hold a deposit until it is determined whether the supplier or the recipient of a supply is entitled to finally receive it.

A supply of goods and services is deemed to be made when the supplier or the recipient issues an invoice, or when the supplier receives any payment for the supply, whichever is the earlier. When an invoice has not been issued for the supply, the supply is deemed to be made on the date that the supplier receives any payment. Payment includes the receipt of a deposit. If a stakeholder receives a deposit, this is not considered to be receipt of the payment by the supplier.

All legislative references in this item are to the Goods and Services Tax Act 1985.

Background

We have been asked to clarify the requirement for a supplier of goods and services to account for GST charged on supplies made, when that supplier has received only a deposit for the supply. There is some confusion as to how much GST (if any) should be accounted for when the supplier has not received full payment, or when the supply has not physically been made.

A registered person must charge GST (output tax) on taxable supplies of goods and services made to other people. A recipient of goods and services is charged GST (input tax) on taxable supplies received - for example, purchases and day to day operating expenses.

A registered person must account for the output tax attributable to a taxable period when filing a GST return for that period. Any input tax attributable to that period is deductible from the output tax, provided the goods and services are acquired for the principal purpose of making taxable supplies. The amount of output tax still remaining after deducting any input tax is payable to Inland Revenue by the last working day of the month following the taxable period. If the amount of input tax exceeds the output tax, Inland Revenue will refund the difference.

Legislation

Section 9(1) sets out the general time of supply rule for GST purposes. It states:

> Subject to this Act, for the purposes of this Act a supply of goods and services shall be deemed to take place at the earlier of the time an invoice is issued by the supplier or the recipient or the time any payment is received by the supplier, in respect of that supply.

Subsections (2), (3), (6), and (7) of section 9 set out time of supply rules for special circumstances.

Section 20(4) determines when to account for output tax charged. In summary, persons who use the invoice basis or the hybrid basis must attribute the full output tax on a supply to the taxable period in which the supply is deemed to be made. Persons who use the payments basis must account for output tax on each payment they receive in the taxable period in which they receive it.

Section 20(3) determines when to account for input tax. In summary, persons who use the invoice basis can claim input tax in the taxable period in which the supply is deemed to be made to them. Persons who use the payments basis or the hybrid basis can claim input tax on each payment they make in the taxable period in which they make the payments.

Section 20(3) also contains a proviso which allows a recipient of a supply of goods and services to attribute the input tax deduction to a later taxable period.

Policy

Time of supply

A supply of goods and services is deemed to take place when the supplier or the recipient issues an invoice, or when the supplier receives any payment for the supply, whichever is the earlier. The supply is deemed to be made on this date regardless of when the supply is physically made.

Deposit received by supplier

When the supplier receives a deposit before an invoice is issued, the goods and services are deemed to be supplied in full on that date. Section 9(1) refers to any payment the supplier receives. This includes a part payment of the purchase price by way of a deposit. There is no requirement that the supplier receives all of the purchase price. This principle is supported by the judgments in *Case L67* (1989) 11 NZTC 1,391; *Case N24* (1991) 13 NZTC 3,199; and *Case R11* (1994) 16 NZTC 6,062.

Deposit received by stakeholder

A stakeholder may receive a deposit in terms of a conditional contract between the supplier and the recipient, and hold it until it is determined who is entitled to finally receive it.

A stakeholder can be used in the supply of any type of goods and services, and is particularly common in the buying and selling of real estate. When a stakeholder holds a deposit, the supplier is not considered to have received the payment until it is applied to his or her benefit. The payment is considered to have been applied to the supplier's benefit when any of these events occurs:

- The payment is paid to the supplier.
- The payment is paid to the supplier's agent.
- The payment is credited against amounts owing by the supplier, for example legal fees or real estate agents' commissions.

If the supplier's agent acts as the stakeholder and holds the deposit, payment is considered to have been received by the supplier when the contract becomes unconditional. The Commissioner accepts that the supplier's agent can act as a stakeholder while the contract is still conditional. However, when the contract becomes unconditional, the agent is no longer holding the deposit as stakeholder, but rather as agent for the supplier. The circumstances of each case will determine whether the supplier's agent is acting as a stakeholder.

The Commissioner considers that the supplier of the goods and services cannot act as stakeholder. A stakeholder must be an independent third party.

Example 1

Interior Covers Ltd is a wallpaper retailer and hanger. It is registered for GST on the invoice basis, and files GST returns monthly. The company waits until it has finished hanging the wallpaper before it issues the customer with an invoice. However, a deposit of 10% is required from the customer before work begins.

During July, Interior Covers Ltd receives orders from 10 customers to supply and hang wallpaper to the value of $7,000 each. The total value of the orders is $70,000 including GST. Deposits of $700 each are received from the 10 customers. The wallpaper is not physically supplied during July.

GST Treatment

Supplies of wallpaper to the customers who paid deposits are deemed to be made on the date the deposits are received. As the company is registered on the invoice basis of accounting, it must account to Inland Revenue for the full amount of output tax charged on the supplies.

The company's July GST return must include the following output tax details:

Total value of supplies deemed to have been made: $70,000
GST accountable (one-ninth) $7777.77

Example 2

Reece Eaver repairs home satellite-dishes. He is registered on the payments basis, and files GST returns monthly. During May, Reece agrees to repair Mrs Scott's satellite-dish for a fee of $300. She pays Reece a deposit of $50 on 14 May. Reece completes the job and returns the dish together with an invoice before the end of May, requesting payment of the balance of $250. Mrs Scott pays the balance in full on 20 June.

GST Treatment

When Reece receives the deposit on 14 May, the supply of his repair services to Mrs Scott is deemed to be made. As Reece is registered on the payments basis of accounting, he is only required to account to Inland Revenue for the output tax actually received on the supply. In addition to any other output tax received in May, Reece should include the $5.55 output tax (one-ninth of $50) received from Mrs Scott in his May GST return. Reece should include output tax of $27.78 (one-ninth of $250) received from Mrs Scott in his June GST return.

Example 3

Rob LeBaron develops inner city apartments for sale, and is registered for GST purposes. On 1 November, a conditional contract to supply an apartment for $200,000 is signed between Rob and Graeme, who wants to purchase an apartment as his residence. Graeme pays a deposit of $20,000 to Rob's real estate agent on 1 November. The real estate agent holds the deposit as stakeholder until the contract becomes unconditional on 5 December. No amounts are credited towards the agent's commission before that date. Rob accounts for GST on an invoice basis and files his GST returns monthly. He has asked when he should return the output tax on the sale.

Although the real estate agent is also Rob's agent, the Commissioner considers that the deposit is not applied to Rob's benefit until the contract becomes unconditional on 5 December. Rob is considered to have received the payment on 5 December, as from that point the payment is held by the real estate agent in the capacity of Rob's agent, and not in the capacity of a stakeholder.

As Rob accounts for GST on an invoice basis, he is required to account for the full amount of output tax charged on the supply in his GST return for the month of December. This amounts to one-ninth of $200,000, i.e., $22,222.22.

Gift duty - exemption for maintenance or education of relatives

Section 72, Estate and Gift Duties Act 1968

Summary

This item discusses the general approach that the Commissioner takes when applying section 72 of the Estate and Gift Duties Act 1968. Section 72 provides an exemption from gift duty for gifts made for the maintenance or education of relatives.

The Commissioner must be satisfied that the gift is not excessive in amount, having regard to the legal or moral obligation of the donor to provide the maintenance or means of education. Each particular gift and its surrounding circumstances will be considered when deciding whether section 72 applies. However, the following general points can be made about applying section 72:

- The exemption applies to gifts of money as well as gifts of other property:
- The exemption can apply to gifts made to trusts as well as gifts made directly to a relative. Gifts of single capital amounts to a trust can qualify for the exemption.
- "Maintenance" includes everything a person requires to maintain his or her particular lifestyle. Factors such as the relationship of the parties, their wealth and position, and the environment to which they are accustomed are all relevant.
- "Education" means the process involving the study of certain subjects by way of systematic teaching, training, instruction or research leading to an increase in a person's store of knowledge and/or qualifications.
- "Relative" has a wide meaning and extends to relationships outside of the immediate family.
- Whether a gift is excessive will largely depend on the donor's moral obligations. Whether the donor owes a moral duty to the recipient of the gift depends on such factors as the wealth of the donor, the donor's position in the community, the nature and circumstances of the family, the recipient's age, state of health and financial position, and the character and conduct of the recipient. The moral duty owed to a spouse is different to that owed to children.
- Moral obligations may change over time as social attitudes change. This will influence the application of section 72.

All legislative references in this item are to the Estate and Gift Duties Act 1968 unless otherwise stated.

Legislation

Section 72 states:

Where the Commissioner is satisfied that any gift is made for or towards the maintenance of the wife, husband, or any relative of the donor, or for or towards the education of any such relative, and is not excessive in amount, having regard to the legal or moral obligation of the donor to provide that maintenance or means of education, the gift shall not constitute a dutiable gift.

Background

Section 61 imposes gift duty on every dutiable gift. Section 63 states that a dutiable gift shall include and consist of:

(a) All the property, wherever situated, comprised in any gift made by any donor to any donee, where the donor is domiciled in New Zealand at the date of the gift, or is a body corporate incorporated in New Zealand:

(b) All the property, situated in New Zealand, comprised in any gift made by any donor to any donee, where the donor is domiciled out of New Zealand at the date of the gift, or is a body corporate incorporated out of New Zealand.

Section 72 excludes certain gifts from gift duty even though the gifts would otherwise constitute a dutiable gift.

For a gift to be exempted from gift duty under section 72, the Commissioner must be "satisfied" that certain requirements are met. These requirements are that:

- The gift is made for the maintenance or education of a wife, husband or relative of the donor.
- The gift is not excessive in amount having regard to the legal or moral obligation of the donor to provide that maintenance or means of education.

There are two main points to make about these requirements. Firstly, the donor's legal or moral obligation must be considered. This means that the particular circumstances surrounding each gift must be considered. Whether or not a gift constitutes maintenance depends on the nature of the legal or moral obligations of a particular donor. What may constitute a legal or moral obligation for one donor may not constitute a legal or moral obligation for another donor.

Secondly, the words used in the section, such as "legal or moral obligation" and "excessive in amount", are terms whose meaning changes and develops over time. Section 72 is a "living" piece of legislation. This means that there can be no definitive interpretation of the terms used.

Notwithstanding the above points, some guidance can be provided as to the Commissioner's general approach under section 72. The Commissioner can also provide some indication as to how specific terms will be interpreted and whether particular circumstances fall within the section.

Guidelines

Exemption when gift made to trust rather than directly to relative

The exemption can apply to gifts made to trusts rather than directly to a relative. Section 72 speaks in terms of "any gift made for or toward the maintenance ..." of the relative. The section does not require that the donor make the gift directly to the relative. However, when a gift is made to a trust, it should be clear that the donor's relatives are the beneficiaries and that the gift is for the maintenance or education of these beneficiaries.

Gifts of single capital amounts to a trust can qualify for the exemption under section 72 if the gift is made for or towards the maintenance or education of a relative and the gift is not excessive in amount (having regard to the donor's legal and moral obligations).

Types of gifts to which section 72 applies

"Gift" is defined in section 2(2) as follows:

"Gift" means any disposition of property, wherever and however made, otherwise than by will, without fully adequate consideration in money or money's worth passing to the person making the disposition:

Provided that where the consideration in money or money's worth is inadequate, the disposition shall be deemed to be a gift to the extent of that inadequacy only.

A gift can therefore be any form of property. Money, housing, jewellery, and antiques are all examples of gifts that may qualify for the exemption under section 72.

Meaning of "maintenance"

The Commissioner will take into account the facts of each particular case to determine what is reasonable maintenance in the surrounding circumstances. Maintenance means more than merely what is needed to provide the necessities of life. Maintenance also includes everything that a relative requires to maintain his or her lifestyle. In particular, the Commissioner will consider facts such as:

- the relationship of the parties
- the wealth and position of the parties
- the environment to which the parties are accustomed.

What amounts to maintenance will vary from case to case depending on a consideration of the above factors.

Meaning of "education"

The Commissioner interprets "education" as the process involving the study of certain subjects by way of systematic teaching, training, instruction or research with the aim of increasing a person's store of knowledge and/or qualifications.

Schooling in primary, secondary and tertiary institutions will meet the definition of education. Other methods of gaining education will also meet the definition of education if the methods involve the study of certain areas in a systematic way.

Meaning of "relative of the donor"

"Relative" is not defined in the Estate and Gift Duties Act 1968 and therefore takes on its ordinary meaning. The term has a very wide meaning and can include quite distant relatives and people connected by marriage rather than just blood relatives.

Section 2(3) provides some guidance as to whether people have a relationship with each other, although the term "relative" is not limited to those discussed in that section. Section 2(3) states:

For the purposes of this Act -

(a) Persons are connected by blood relationship if within the fourth degree of relationship:

(b) Persons are connected by marriage if one is married to the other or to a person who is connected by blood relationship to the other:

(c) Persons are connected by adoption if one has been adopted as the child of the other or as the child of a person who is within the third degree of relationship to the other:

(d) Illegitimate relationship shall be equivalent to legitimate relationship.

The term "relative" extends to relationships outside the immediate family, but the greater the "distance" of the relatives the less likely it is that there is a moral obligation on the donor to make a gift. Similarly, there is less likely to be an obligation towards an adult relative compared with a relative who is still "under age".

Meaning of "not excessive in amount, having regard to the legal or moral obligation of the donor to provide that maintenance or means of education"

Legal obligations

Legal duties owed to family members are limited and few. Examples of legal duties owed to provide maintenance and education are:

1. In relation to spouses, section 63(1) of the Family Proceedings Act 1980 imposes a duty for each spouse to maintain the other "to the extent that such maintenance is necessary to meet the reasonable needs of the other party, where the other party cannot practicably meet the whole or any part of those needs" because of the effects of a limited number of circumstances. These circumstances are:
    - The division of marital functions
    - Custodial arrangements for any child of the marriage after the parties cease to live together
    - A physical or mental disability
    - An inability to obtain work
    - The undertaking of a reasonable period of education or training.

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In considering the reasonable needs of each spouse, the standard of living of the household is disregarded, unless there are “special circumstances”.

2. In relation to children, section 152 of the Crimes Act 1961 imposes a legal duty on parents to provide the necessaries for any child under the age of 16. Section 14 of the Children Young Persons and their Families Act 1989 imposes duties on parents, albeit in a negative way, by providing that the State will step in when a certain threshold of harm to a child is reached. Section 20 of the Education Act 1989 imposes a duty on parents to ensure that their children attend school.

3. There appears to be no legislative requirement imposing a legal duty on people (while they are alive) to provide maintenance and education for their parents or any other members of their extended family.

Moral obligations

Determining the moral obligations of a particular donor is a subjective judgment because the duties are unique to each individual.

There is no case law that assists in the interpretation of “moral obligations” in the context of section 72. The Family Protection Act 1955 and related case law does provide some indication as to what constitutes a moral obligation and can be used as a “benchmark” in the context of section 72.

The Family Protection Act 1955 applies when a deceased person does not adequately provide for the proper maintenance and support of certain persons. The Court looks to whether there has been a breach of some moral duty owed by the deceased person.

In *Allardice v Allardice* (1910) 19 NZLR 959, 973, Justice Edwards stated that the Court is required “to place itself in all respects in the position of the testator, and to consider whether or not, having regard to all existing facts and circumstances, the testator has been guilty of a breach of [that] moral duty”.

The courts have identified a number of factors to take into account when considering whether the deceased owed a moral duty to a particular applicant. Considerations relevant to section 72 of the Act include:

- The wealth of the donor (including both income and capital sources) and the donor’s position in the community
- The nature and circumstances of the family, for example, the style of living to which the recipient of the gift is accustomed
- The recipient’s age, state of health and financial position
- The character and conduct of the recipient
- Any special needs of the recipient, such as those associated with a disability.

In addition to the above factors, a donor’s moral obligations could also be influenced by the donor’s ethnic and cultural background.

Note that under the Family Protection Act, the Courts interpret the moral duty of a testator differently depending on whether a spouse or child is involved. The moral duty to spouses stems from their undertaking to support each other when they marry. Therefore, the courts expect a husband or wife to provide for his or her spouse to enable the spouse to live in the style he or she has become accustomed to, without anxiety about present or future needs.

However, the reasoning in relation to children is different. The Courts tend to interpret parents’ moral duty to their children as a duty to nurture and educate them to enable them to become productive members of society. This duty is regarded as ending when children become self-supporting. This will usually be when the children complete their education and no longer look to their parents for financial support. For Family Protection Act purposes, a parent’s moral duty may extend beyond the stage when the child is self-supporting, but this duty relates to an obligation to leave a child a “fair share” of the estate and is not relevant for gift duty purposes. Therefore, it can be concluded that a parent’s moral duty to provide maintenance and education to his or her children ceases when the child becomes financially independent.

Payments excessive in amount

Unless they are providing only for the necessaries of life, most gifts are likely to be excessive in amount if regard is had only to the legal obligations of the donor. Because of the limited extent of legal duties owed between family members, the extent of any moral duty is likely to be the most important consideration in deciding whether a gift is excessive in amount.

Whether a payment is excessive will depend on the extent of the legal and moral obligations and the particular circumstances of a case. A gift of a large capital amount does not in itself mean a gift is excessive in amount. This will depend on the obligations of the donor and the purpose for which the gift is given.

Note that changing social attitudes will influence the existence and extent of moral duties. This in turn will influence what amounts are considered to be excessive.

No part of any gift that is excessive in amount can qualify for the exemption under section 72. The exemption cannot be given for that part of the gift that is not excessive.

GST - zero-rating of goods sold to persons departing NZ

Summary

This item sets out the GST treatment of goods sold in New Zealand to tourists and other persons departing from New Zealand. The item discusses six categories of goods that can be zero-rated:

1. goods sold to departing travellers by any shop operating in the Customs-controlled area of an airport, unless the goods are normally intended to be used within that area
2. goods sold to a customer before the customer leaves New Zealand, when the supplier delivers the goods to the Customs-controlled area of the airport, provided the customer does not take possession of the goods at any time outside the Customs-controlled area
3. goods sold to persons departing by sea, when the purchaser does not have access to the goods at any time before the ship has left the final New Zealand port
4. goods sold by a supplier licensed as an export warehouse, when the supplier has been licensed by the Comptroller of Customs to operate a sealed bag system
5. goods posted or couriered overseas by the supplier
6. goods sold by shops licensed as export warehouses which operate within the Customs-controlled part of an international airport, when the goods are sold to departing travellers who uplift the goods when they return to New Zealand.

In each case the supplier must keep sufficient information, as outlined in this item, to provide evidence for the zero-rating claim.

All legislative references in this item are to the Goods and Services Tax Act 1985 unless otherwise stated.

Background

Generally speaking, a GST registered person must charge GST on all supplies of goods made in New Zealand. This means that the registered person must charge GST on the supply of goods to a purchaser, even though the purchaser may be departing from New Zealand at some time in the near future. Purchasers cannot recover the GST charged on such supplies unless they are registered for GST purposes and the goods are acquired for the principal purpose of making taxable supplies. Purchasers cannot obtain a refund of GST paid on goods purchased in New Zealand when they leave the country.

However, there are some situations in which the supply of goods to persons departing from New Zealand can be charged with GST at the rate of zero percent. The legislative authority for zero-rating the supply of goods in these cases is found in paragraphs (a) to (af) of section 11(1). In each of the cases in which the supply of goods may be zero-rated the supplier must retain sufficient information to support the zero-rating claim.

Legislation

Section 11(1) states:

Where, but for this section, a supply of goods would be charged with tax under section 8 of this Act, any such supply shall be charged at the rate of zero percent where -

(a) The supplier has entered the goods for export, pursuant to the Customs Act 1966, and those goods have been exported by the supplier; or

(aa) The goods have been deemed to be entered for export, pursuant to the Customs Act 1966, and the goods have been exported by the supplier; or

(ab) The supplier has satisfied the Commissioner that the goods have been exported by the supplier to a place outside New Zealand; or

(ac) Subject to subsection (1B) of this section, the supplier will enter the goods for export, pursuant to the Customs Act 1966, in the course of, or as a condition of, making the supply and will export the goods; or

(ad) Subject to subsection (1B) of this section, the goods will be deemed to be entered for export, pursuant to the Customs Act 1966, and exported by the supplier in the course of, or as a condition of, making the supply; or

(ae) Subject to subsection (1D) of this section, the goods are supplied by a supplier licensed, pursuant to section 82 of the Customs Act 1966, as an export warehouse, and -

(i) The supplier has been licensed by the Comptroller to operate a sealed bag system; and

(ii) The goods are supplied in accordance with the sealed bag system; and

(iii)The goods are entered, or are deemed to be entered, for export pursuant to the Customs Act 1966; or

(af) The goods are supplied, by a supplier licensed pursuant to section 82 of the Customs Act 1966 as an export warehouse, to -

(i) An inbound air traveller; or

(ii) An outbound air traveller who uplifts the goods upon returning to New Zealand -

within an area licensed pursuant to section 32 of the Customs Act 1966 as a Customs examining place for the Customs processing of international air travellers at an international airport;

Policy

The supply of goods may be zero-rated in the following circumstances. In every case, it is important that the supplier retains the evidence outlined in this item. If the evidence is not retained, the goods sold will be subject to GST at the standard rate of 12.5 percent.

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1. Goods sold to departing travellers by any shop operating in the Customs-controlled area of an airport, unless the goods are normally intended to be used within that area

The supply of goods can be zero-rated under section 11(1)(ab) if the supplier satisfies the Commissioner that the supplier exported the goods to a place outside New Zealand. Taking a narrow approach, it could be argued that it is the purchaser rather than the supplier who exports the goods because the purchaser physically takes the goods out of New Zealand. However, the Commissioner accepts that the supplier can be said to have exported the goods to a place outside New Zealand if the supplier is selling goods at a place that can only be entered by people who are imminently about to board an aircraft out of New Zealand. In this situation the purchaser has no practical choice but to take the goods out of New Zealand.

To qualify for zero-rating, the shop must be in the area of the airport controlled by Customs ("the restricted area"), i.e. the part of the airport that only those people who have passed through Customs and are about to fly out of New Zealand can enter. A shop that operates in the general public access area ("the unrestricted area") of an international airport is not able to zero-rate goods sold as discussed under this category, although they may be able to zero-rate goods under categories 2 or 5.

If a shop is accessible only to those people who have passed through Customs, the Commissioner accepts that all goods sold can be zero-rated unless the goods are normally intended to be used or consumed within the restricted area. Examples of goods that are normally used or consumed within the restricted area include most food and beverage items sold by fast food outlets, cafes, restaurants, and bars. The Commissioner will allow the zero-rating of items that are reasonably capable of being used or consumed outside New Zealand. Examples of items that are reasonably capable of being used or consumed outside New Zealand include newspapers, camera film and food items such as chewing gum and chocolate bars.

If a shop has a frontage or counter opening into the unrestricted area as well as a frontage or counter opening into the restricted area, only those goods supplied to customers in the restricted area can be zero-rated. In this case the shop must have a system to obtain sufficient evidence to show that a person about to leave New Zealand purchased the goods. For example, it would be acceptable if the supplier obtains a photocopy of the purchaser's airline ticket detailing the purchaser's name, flight number, and destination as well as recording the purchaser's address (whether it is a New Zealand or an overseas address). If the supplier does not keep enough evidence to show that a person about to leave New Zealand purchased the goods, the supplier must account for GST at the standard rate of 12.5 percent.

2. Goods sold to a customer before the customer leaves New Zealand, when the supplier delivers the goods to the Customs-controlled area of the airport, provided the customer does not take possession of the goods at any time outside the Customs-controlled area

The supply of goods can be zero-rated under section 11(1)(ab) if the supplier satisfies the Commissioner that the supplier exported the goods to a place outside New Zealand. The Commissioner accepts that the supplier exports goods for the purposes of section 11(1)(ab) if the supplier delivers the goods to a place which is very close to the departing aircraft, and if the purchaser of the goods has no practical choice but to take the goods out of New Zealand. This place is the restricted area of the airport controlled by Customs.

The customer must not have access to the goods outside the restricted area at any time. If the customer does have access to the goods outside the restricted area, the Commissioner would not be satisfied that the supplier had exported the goods. The goods are subject to GST at the standard rate of 12.5 percent.

The supplier must keep enough evidence to show that the goods were sold to a person departing overseas in the near future at the time of the sale. An example of such evidence is a photocopy of the purchaser's airline ticket detailing the purchaser's name, flight number and destination as well as a record of the purchaser's address (whether it is a New Zealand or an overseas address).

The supplier must also have proof that the goods were delivered to the Customs-controlled part of the airport, for example, a courier invoice or some documentation obtained from Customs. If the supplier does not keep this evidence, the vendor is liable for the GST at the standard rate of 12.5 percent.

3. Goods sold to persons departing by sea, when the purchaser does not have access to the goods at any time until the ship has left the final New Zealand port

The supply of goods may be zero-rated under section 11(1)(ab). The supplier must have an evidence-keeping system which shows that the supplier sold goods to a person departing from New Zealand, and that the person did not have access to the goods until the ship had sailed from the final New Zealand port. For example, it would be acceptable if the supplier records the purchaser's name and address (whether it is a New Zealand or an overseas address) and the ship's name and departure date as well as obtaining a written undertaking from the ship's purser that the purchaser will not have access to the goods purchased until the ship has left the final New Zealand port. The undertaking may be in a form produced by the supplier and then signed by the purser, or in a form produced by the purser.

4. Goods sold by a supplier licensed as an export warehouse, when the supplier has been licensed by the Comptroller of Customs to operate a sealed bag system

Section 11(1)(ae) provides for the zero-rating of goods under a sealed bag system. This section applies only to a supplier licensed as an export warehouse under section 82 of the Customs Act 1966, and when these three conditions are met:

- The supplier has been licensed by the Comptroller of Customs to operate a sealed bag system.
- The goods are supplied in accordance with the sealed bag system.
- The goods are entered, or deemed to be entered for export pursuant to the Customs Act 1966.

Section 11(1)(ae) only applies in the circumstances outlined above. A supplier cannot zero-rate goods using sealed bags if it is not licensed as an export warehouse and/or is not licensed to operate a sealed bag system by the Comptroller of Customs.

It has come to Inland Revenue's attention that some suppliers who are not licensed export warehouses are zero-rating the supply of goods under "unofficial" sealed bag systems. The suppliers are selling goods to customers and providing the goods to customers in a sealed bag that is taken by the customer through Customs. The supplier cannot zero-rate the supply of goods when the customer has access to the goods, even if in a sealed bag, outside of the restricted area of the airport. In this case it is the customer rather than the supplier who is the exporter of the goods.

Suppliers who are not licensed export warehouses and/or who do not sell goods in the restricted part of an international airport can, of course, still zero-rate the supply of goods when they are sold in situations that fall within categories 2, 3 or 5 of this item

5. Goods posted or couriered overseas by the supplier

A supplier may undertake to post or courier goods sold to a person at an overseas address. In this case the supply of the goods can be zero-rated either under section 11(1)(ac) or (ad).

Suppliers must keep one of the following types of evidence to show that they posted or couriered the goods to a person at an overseas address:

- a copy of the numbered declaration prepared by Customs (the Customs export entry) if the goods have a value of $1,000 or more and are required to be entered for export under the Customs Act 1966
- a copy of an international parcels customs declaration supplied by New Zealand Post and stamped by the postal officer when the parcel is posted, or a New Zealand Post invoice for the overseas postage
- a copy of the courier's invoice.

A copy of any registration and/or insurance papers could also be used as further evidence to show that certain goods were posted overseas by the supplier.

6. Goods sold by shops licensed as export warehouses which operate within the Customs-controlled area of an international airport, when the goods are sold to a departing traveller who uplifts the goods upon returning to New Zealand

Section 11(1)(af) provides for the zero-rating of the supply of goods in this situation. Only those suppliers licensed as export warehouses under section 82 of the Customs Act 1966 that operate within the Customs controlled area of an international airport can zero-rate goods in this situation.

Enquiries

If you need more information about zero-rating goods under section 11, contact your local Inland Revenue office. However, you will need to contact New Zealand Customs if your enquiry concerns any of these matters:

- entering goods for export
- obtaining a licence to operate an export warehouse
- obtaining a licence to operate a sealed bag system.

Application date

The policy outlined in categories 1, 2 and 3 listed above applies from the date of publication of this item. Categories 4, 5 and 6 restate existing policy.

Depreciation rates - dispenser fittings

The Commissioner has issued Determination DEP 7: Tax Depreciation Rates General Determination 7, which applies to various dispenser fittings. It is reproduced below.

Determination DEP 7: Tax Depreciation Rates General Determination Number 7

This determination may be cited as "Determination DEP 7: Tax Depreciation Rates General Determination Number 7".

1. Application

This determination shall apply for the 1994/95 and subsequent income years to the asset classes listed below. It applies to assets acquired on or after 1 April 1993.

2. Determination

Pursuant to section 108C of the Income Tax Act 1976 I hereby amend the general basic economic depreciation in Determination DEP 1 (as previously amended by DEP 2 to DEP 6) by:

- deleting, from the "Building Fit-out" asset category, the following asset class and general depreciation rate:

Asset Class	Estimated Useful Life (years)	DV Banded Depn Rate (%)	SL Equiv Banded Depn Rate (%)
Towel cabinets	3	50	40

- inserting, into the "Building Fit-out" asset category, the following asset classes and general depreciation rates:

Asset Class	Estimated Useful Life (years)	DV Banded Depn Rate (%)	SL Equiv Banded Depn Rate (%)
Hand soap dispensers	2	63.5	63.5
Paper towel dispensers	2	63.5	63.5
Toilet roll dispensers	2	63.5	63.5

3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax Act 1976.

This determination is signed by me on the 21st day of November 1994.

Murray McClennan
Manager (Rulings - Tax Policy)

Depreciation - new asset classes and rates for medical equipment, medical laboratory equipment, and scientific and general laboratory equipment

The Commissioner has issued a new general depreciation determination called "Determination DEP8: Tax Depreciation Rates General Determination 8".

The determination applies for the 1994/95 and subsequent income years, to assets which are acquired on or after 1 April 1993.

The determination makes these three changes:

1. It deletes the "Scientific, Medical and Laboratory Equipment" asset category and all the asset classes and depreciation rates listed under it.
2. It inserts a new industry category called "Medical and Medical Laboratory Equipment". This new category contains the following:
   - Twenty-six **new asset classes** and depreciation rates. These new asset classes are:

Medical, veterinary, dental, optical, chiropractors, funeral directors (excluding casket making machinery), and medical laboratory plant and equipment (default class)
Analysers
Beds (domestic type)
Beds (Hi-Lo)
Beds (standard)
Blood warmers
Chiropractors couches
Dialysis / By-pass machines
Fibre optic scopes
Fitness equipment
Infusion pumps (and the like)
Laparoscopic equipment
Linear accelerator / simulator
Linen
Saunas
Solarium beds
Solarium lamps
Spa pools
Treatment planning system (radiotherapy)
Ultrasonic diagnostic equipment
Ultrasonic scanners (used outdoors by veterinarians)
Vaporisers / absorbers
Washer Decontaminators
Weighing equipment (for patients - electronic)
Weighing equipment (for patients - mechanical)
X-ray cassettes

   - Two **asset classes** that have had the wording altered or transposed from the asset classes listed under the previous "Scientific, Medical and Laboratory Equipment" category. The Commissioner made these changes to correct a spelling error, or so the asset classes may be easily found in an alphabetical listing. The altered asset classes are:

Gamma cameras
Irradiation plant

   - Eighteen **higher general depreciation rates** for asset classes which were listed under the previous "Scientific, Medical and Laboratory Equipment" category. The asset classes that have higher rates are:

Medical, veterinary, dental, optical, chiropractors, funeral directors (excluding casket making machinery), and medical laboratory plant and equipment (default class)
Crutches
Defibrillators
Diathermy equipment
Electro-diagnostic equipment
Electrosurgical equipment
Flow measuring equipment
Gamma cameras
Humidifiers
Infant incubators
Operating tables
Patient monitoring equipment
Radiation detection equipment
Splints
Tools (power)
Ventilators
Wheel chairs (non-powered)
Wheel chairs (powered)

3. It inserts a new asset category called "Scientific and Laboratory Equipment (excluding equipment used in a medical laboratory)". This new category contains the following:
   - Five **new asset classes** and depreciation rates. The new asset classes are:

Scientific and laboratory equipment (excluding medical laboratory equipment) (default class)
Analysers
Linear accelerator/simulator
Washer decontaminators
X-ray cassettes

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- One asset class that has had the wording altered from the asset classes listed under the previous "Scientific, Medical and Laboratory Equipment" category to correct a spelling error. The altered asset class is:

Irradiation plant

- Two **higher general depreciation rates** for asset classes which were listed under the previous "Scientific, Medical and Laboratory Equipment" category. These asset classes are:

Flow measuring equipment
Radiation detection equipment

Depreciation Determination DEP8

This determination may be cited as "Determination DEP8: Tax Depreciation Rates General Determination 8".

1. Application

This determination shall apply to the asset classes listed under the "Medical and Medical Laboratory Equipment" industry category, and the asset classes listed under the "Scientific and Laboratory Equipment (excluding equipment used in a medical laboratory)" asset category. This determination shall apply for the 1994/95 and subsequent income years where the assets are acquired on or after 1 April 1993.

2. Determination

Pursuant to section 108C of the Income Tax Act 1976 I hereby:

- Delete the asset category "Scientific, Medical and Laboratory Equipment" and all the asset classes, estimated useful lives and depreciation rates listed under that category.
- Insert the industry category "Medical and Medical Laboratory Equipment" with the following asset classes, estimated useful lives, diminishing value depreciation rates and straight line equivalent depreciation rates:

Medical and Medical Laboratory Equipment	Estimated Useful Life (years)	DV Banded Depn Rate (%)	SL Equiv Banded Depn Rate (%)
Medical, veterinary, dental, optical, chiropractors, funeral directors (excluding casket making machinery), and medical laboratory plant and equipment (default class)	8	22	15.5
Alarms (for patients)	5	33	24
Anaesthesia equipment	10	18	12.5
Analysers	8	22	15.5
Audiometers	8	22	15.5
Autoclaves	20	9.5	6.5
Baths (water)	12.5	15	10
Beds (domestic type)	8	22	15.5
Beds (Hi-Lo)	10	18	12.5
Beds (standard)	15.5	12	8
Blood warmers	10	18	12.5
Breathing apparatus	10	18	12.5
Centrifuges	10	18	12.5
Chambers (vacuum)	10	18	12.5
Chiropractors couches	15.5	12	8
Chromatographs	8	22	15.5
Crematoriums	25	7.5	5.5
Crutches	1	100	100
Cylinders (gas)	5	33	24
Defibrillators	6.66	26	18

Medical and Medical Laboratory Equipment (continued)	Estimated Useful Life (years)	DV Banded Depn Rate (%)	SL Equiv Banded Depn Rate (%)
Dental chairs	15.5	12	8
Dental units	8	22	15.5
Dialysis / By-pass machines	8	22	15.5
Diathermy equipment	6.66	26	18
Drill bits, saw blades and the like		expense	expense
Electrical test meters	8	22	15.5
Electro-diagnostic equipment	6.66	26	18
Electrocardiographs	8	22	15.5
Electronic balances	8	22	15.5
Electrosurgical equipment	6.66	26	18
Fibre optic scopes	5	33	24
Fitness equipment	5	33	24
Flasks (vacuum)	10	18	12.5
Flow measuring equipment	6.66	26	18
Freezers	10	18	12.5
Fume cabinets	15.5	12	8
Furnaces	15.5	12	8
Furniture (fixed)	20	9.5	6.5
Furniture (loose, laboratory)	10	18	12.5
Furniture (loose, medical)	10	18	12.5
Gamma cameras	8	22	15.5
Hoists (for patients)	10	18	12.5
Humidifiers	5	33	24
Hydrocollators	10	18	12.5
Incinerators (pathological)	20	9.5	6.5
Incubators (laboratory)	12.5	15	10
Infant incubators	8	22	15.5
Infusion pumps (and the like)	5	33	24
Instruments (hand held)	5	33	24
Invalid scooters	8	22	15.5
Irradiation plant	25	7.5	5.5
Lamps (for treatment)	8	22	15.5
Laparoscopic equipment	4	40	30
Laser surgical and dental equipment	5	33	24
Lighting (examination)	12.5	15	10
Lighting (operating theatre)	12.5	15	10
Linear accelerator/simulator	10	18	12.5
Linen	3	50	40
Mannequins	10	18	12.5
Microscope equipment	10	18	12.5
Microtomes	10	18	12.5
Operating tables	15.5	12	8

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Medical and Medical Laboratory Equipment (continued)	Estimated Useful Life (years)	DV Banded Depn Rate (%)	SL Equiv Banded Depn Rate (%)
Optical equipment	10	18	12.5
Orthopaedic appliances	3	50	40
Oscilloscopes	8	22	15.5
Ovens	12.5	15	10
Patient monitoring equipment	6.66	26	18
Physiotherapy equipment	10	18	12.5
Radiation detection equipment	8	22	15.5
Recorders	8	22	15.5
Refrigerators	8	22	15.5
Respiration apparatus	10	18	12.5
Resuscitators	8	22	15.5
Saunas	15.5	12	8
Scanners	10	18	12.5
Skeletons	10	18	12.5
Sluicers	10	18	12.5
Solarium beds	5	33	24
Solarium lamps	5	33	24
Spa pools	10	18	12.5
Spectrophotometers	8	22	15.5
Splints	1	100	100
Sterilisers	20	9.5	6.5
Surgical implant instrument sets (orthopaedic)	3	50	40
Tools (power)	8	22	15.5
Treatment planning system (radiotherapy)	6.66	26	18
Trusses	3	50	40
Ultrasonic diagnostic equipment	5	33	24
Ultrasonic equipment	8	22	15.5
Ultrasonic scanners (used outdoors by veterinarians)	4	40	30
Vaporisers/absorbers	10	18	12.5
Ventilators	8	22	15.5
Vessels (vacuum)	10	18	12.5
Walking frames	3	50	40
Washer Decontaminators	8	22	15.5
Weighing equipment (for patients - electronic)	12	18	12.5
Weighing equipment (for patients - mechanical)	20	9.5	6.5
Wheel chairs (non-powered)	8	22	15.5
Wheel chairs (powered)	6.66	26	18
X-ray cassettes	5	33	24
X-ray equipment (except as shown elsewhere)	10	18	12.5
X-ray equipment (mobile)	8	22	15.5
X-ray processors	8	22	15.5
X-ray viewers	12.5	15	10

- Insert the asset category "Scientific and Laboratory Equipment (excluding equipment used in a medical laboratory)" with the following asset classes, estimated useful lives, diminishing value depreciation rates and straight line equivalent depreciation rates:

Scientific and Laboratory Equipment (excluding equipment used in a medical laboratory)	Estimated Useful Life (years)	DV Banded Depn Rate (%)	SL Equiv Banded Depn Rate (%)
Scientific and laboratory equipment (excluding medical laboratory equipment) (default class)	10	18	12.5
Analysers	8	22	15.5
Autoclaves	20	9.5	6.5
Baths (water)	12.5	15	10
Callipers	8	22	15.5
Centrifuges	10	18	12.5
Chambers (vacuum)	10	18	12.5
Chromatographs	8	22	15.5
Compasses	8	22	15.5
Cylinders (gas)	5	33	24
Drill bits, saw blades and the like		expense	expense
Electrical test meters	8	22	15.5
Electronic balances	8	22	15.5
Flasks (vacuum)	10	18	12.5
Flow measuring equipment	6.66	26	18
Freezers	10	18	12.5
Fume cabinets	15.5	12	8
Furnaces	15.5	12	8
Furniture (fixed)	20	9.5	6.5
Furniture (loose, laboratory)	10	18	12.5
Hardness testers and the like (laboratory)	15.5	12	8
Incubators (laboratory)	12.5	15	10
Instruments (hand held)	5	33	24
Irradiation plant	25	7.5	5.5
Linear accelerator/simulator	10	18	12.5
Meteorological equipment	10	18	12.5
Micrometers	8	22	15.5
Microscope equipment	10	18	12.5
Microtomes	10	18	12.5
Navigational equipment	8	22	15.5
Oscilloscopes	8	22	15.5
Ovens	12.5	15	10
Radiation detection equipment	8	22	15.5
Recorders	8	22	15.5
Refrigerators	8	22	15.5
Respiration apparatus	10	18	12.5
Spectrophotometers	8	22	15.5
Sterilisers	20	9.5	6.5

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Scientific and Laboratory Equipment (excluding equipment used in a medical laboratory) - continued	Estimated Useful Life (years)	DV Banded Depn Rate (%)	SL Equiv Banded Depn Rate (%)
Surveying equipment	8	22	15.5
Surveying equipment (electronic)	4	40	30
Telescopes (optical)	25	7.5	5.5
Telescopes (radio)	25	7.5	5.5
Ultrasonic equipment	8	22	15.5
Vessels (vacuum)	10	18	12.5
Washer Decontaminators	8	22	15.5
X-ray cassettes	5	33	24
X-ray equipment (except as shown elsewhere)	10	18	12.5
X-ray equipment (mobile)	8	22	15.5
X-ray processors	8	22	15.5
X-ray viewers	12.5	15	10

3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax Act 1976.

This determination is signed by me on the 22nd day of November 1994.

Murray McClennan
Manager (Rulings - Tax Policy)

Specified superannuation contribution withholding tax (SSCWT) - correction

Deductibility of employer contributions to employee superannuation schemes

In TIB Volume Six, No.1 (July 1994) there was an item on SSCWT. This item incorrectly stated that "employer contributions to superannuation schemes are only deductible if they are made to a scheme that is a superannuation fund". There are exceptions.

A superannuation fund is any superannuation scheme registered under the Superannuation Schemes Act 1989.

An employer contribution to an employee superannuation scheme that is not a registered superannuation scheme is deductible under section 150(2A) of the Income Tax Act 1976 if the superannuation scheme is deemed to be a company (as required by section 150(2B)). This means an employer contribution to a non-registered superannuation scheme that is defined as a unit trust under section 211 (and therefore deemed to be a company) is deductible. However, an employer contribution is not deductible if it is made to a non-registered superannuation scheme that is not a company, such as a non-contributory scheme that is fully funded by the employer.

The deductibility of employer contributions to superannuation schemes is governed by section 150 because deductibility under section 104 is precluded by section 106(1)(m).

Calculating SSCWT payable

Some readers found the example used in the item confusing. The example assumed that the employer was obligated only to make a gross superannuation contribution that matched the employee's contribution. The net contribution was less than the employee's contribution because SSCWT was deducted from the gross contribution.

If an employer is obligated to make a contribution to a superannuation scheme that is equal in net terms (i.e. after deducting SSCWT) to that made by an employee, the employer's contribution will have to be increased by the amount of SSCWT payable. In this situation the SSCWT payable can be calculated from the employer's desired net contribution by using the formula:

$$\text{SSCWT} = \frac{a}{1 - a} \times b$$

In this formula:

a is the SSCWT deduction rate

b is the employer's net contribution

Example

If an employer wishes to make a net contribution of $1,000 to an employee superannuation scheme, the SSCWT payable in addition to the net contribution is calculated as follows:

$$\frac{33}{67} \times \$1{,}000 = \$492.53$$

To calculate the employer's gross superannuation contribution, the net contribution will therefore have to be increased by $492.53 to $1,492.53. This will ensure that $1,000 still remains to be contributed to the scheme after SSCWT is deducted at 33 cents per dollar.

Fidelity fund levies - GST implications clarified

Summary

This item explains when to claim input tax deductions for payments to the New Zealand Law Society (NZLS) fidelity fund. It applies to practitioners who account for GST on the payments basis or hybrid basis, and who have elected to pay the fidelity fund levy ("the levy") in instalments. In such cases, the deduction available for each instalment is limited to the tax fraction, i.e., 1/9th, of the amount actually paid. Practitioners who have overstated their deduction should advise their local Inland Revenue office, setting out the amendments required.

All legislative references in this item are to the Goods and Services Tax Act 1985.

Background

In 1992 the NZLS imposed a one-off levy of $10,000 plus GST on practising members. The NZLS gave practitioners the option of paying the levy in five equal annual instalments. At the beginning of 1993, district law societies issued tax invoices on behalf of the NZLS for the full amount of the levy. In the case of the instalment option, the NZLS required the full amount of GST to be paid with the first instalment. Some confusion has arisen regarding the correct GST treatment for practitioners who account for GST on the payments basis or hybrid basis, and who have elected to pay the levy in instalments.

Policy

TIB Volume Four, No.7 (March 1993) sets out the application of GST to the levy.

Application

The time of claiming the corresponding GST input tax deduction depends on the accounting basis of the individual practitioner. Practitioners who use the invoice basis may claim the input deduction at the earlier of being invoiced or making any payment. Those registered on a payments basis or hybrid basis may claim the input deduction based only on the actual amount paid for the supply in each period. For these practitioners this means upon payment of the levy or part of the levy, regardless of whether a part or all of the GST component is paid at that time.

GST on levy paid in instalments - practitioner on payments or hybrid basis

The correct treatment is:

	Levy	GST Output Tax	Total	Input Deduction
Instalment 1 (Jan 1993)	$2,000	$1,250	$3,250	$361.11
Instalment 2 (Jan 1994)	$2,000	-	$2,000	$222.22
Instalment 3 (Jan 1995)	$2,000	-	$2,000	$222.22
Instalment 4 (Jan 1996)	$2,000	-	$2,000	$222.22
Instalment 5 (Jan 1997)	$2,000	-	$2,000	$222.22
	$10,000	$1,250	$11,250	$1,250.00

Practitioners who have overstated the deduction available for the first instalment payment (i.e., claimed an input tax credit of $1,250 rather than $361.11) should advise their local Inland Revenue office. They should detail the adjustments required for that return (i.e., a reduction in the available input tax deduction of $888.89) and the consequent amendment for the return for the period in which the second instalment was paid (i.e., an available input tax deduction of $222.22). No penalty or additional tax will be imposed, provided these steps are taken to amend the over-statement.

Questions we've been asked

This section of the Tax Information Bulletin sets out the answers to some day-to-day questions that people have asked. We have 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.

Income Tax Act 1976

"New Zealand" does not include Ross Dependency

Section 2 - Interpretation of "New Zealand": An Australian resident was employed by a private company in the Ross Dependency in Antarctica. He has asked whether his employment income, earned solely in the Ross Dependency, is subject to New Zealand income tax.

This will depend on whether his employment income, under section 243(2)(c), is income "earned in New Zealand" and whether the Ross Dependency is part of New Zealand for income tax purposes. (This question raises similar issues under sections 243(2)(o) and (r) of whether the employment income is income derived from contracts made or wholly or partly performed in New Zealand or income derived directly or indirectly from any other source in New Zealand.)

The "New Zealand" definition in section 2 does not cover these questions. New Zealand in the definition refers only to the limits of the continental shelf as defined in section 2 of the Continental Shelf Act 1964 and certain water and airspace above the continental shelf. However, the definition is not exhaustive (being only inclusive). The definitions of "New Zealand" in section 4 of the Acts Interpretation Act 1924 and section 2 of the New Zealand Boundaries Act 1863 do not include the Ross Dependency. Accordingly, the definition of New Zealand for income tax purposes does not include the Ross Dependency.

The Australian resident is not subject to New Zealand income tax on employment income sourced from the Ross Dependency.

Note that a New Zealand income tax resident who derives employment or other income from the Ross Dependency would be subject to New Zealand tax. Section 242(a) imposes income tax on income of New Zealand residents, whether it is derived from New Zealand or from elsewhere.

Deductibility of expenses incurred in selling a business

Section 106(1)(a) - Certain deductions not permitted - Capital: A partnership is about to file its final IR 7 partnership tax return after closing its business. One of the partners has asked if legal and real estate agents' fees incurred in selling the business can be claimed as a deduction for income tax and GST purposes.

Section 106 lists certain non-deductible types of expenditure. One of these is capital expenditure. The Commissioner's view is that legal expenses and real estate agents' fees incurred in the sale of a business are capital in nature and not deductible.

For GST purposes, under section 6(2) of the Goods and Services Tax Act 1985:

"Anything done in connection with the commencement or termination of a taxable activity shall be deemed to be carried out in the course or furtherance of that taxable activity."

If the partnership is registered for GST and tax invoices are available, it can claim an input tax deduction for the GST element of any expenses incurred in the sale of the business.

Deductibility of domestic mortgage interest against rental income

Section 106(1)(h) - Deductibility of interest: A taxpayer has recently purchased a house in Wellington with the aid of a mortgage. The house is to be used as her private residence. She has rented out her former home in Auckland, and wants to know if the mortgage interest that she pays on her Wellington home is deductible against income from the rental property.

Section 106(1)(h)(i) allows an interest deduction in so far as the interest is payable in gaining or producing assessable income.

The Commissioner will consider the use of the capital for which the interest is paid to determine whether there is sufficient nexus between the interest and the gaining or producing of assessable income to meet the test for deductibility. Interest will be deductible to the extent that both of these conditions are met:

- In the period in which the interest deduction is claimed, the related capital is used to produce assessable income.
- No identifiable part of the capital is used for private or domestic use, or a use that produces exempt income.

In this particular case, the interest paid on the mortgage on the Wellington property is not deductible as is does not satisfy the test in section 106(1)(h)(i). The interest payable is not used in gaining or producing assessable income. It is expenditure of a private or domestic nature and prohibited from deduction under section 106(1)(j).

A full statement setting out the Commissioner's policy on interest deductibility and his interpretation on several leading cases on the subject has been published in TIB Volume Three, No.9 and its appendix.

Agent must deduct non-resident withholding tax if not already deducted at source

Section 312 - Deduction of Non-Resident Withholding Tax: A tax practitioner was acting as agent for a client who is no longer a New Zealand resident for taxation purposes. The practitioner has received payments of non-resident withholding income (dividends) for this client.

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The company which paid the dividends did not know whether it should deduct RWT or non-resident withholding tax (NRWT), so it deducted neither. The practitioner wants to know who is now responsible for deducting the NRWT.

An agent acting for a non-resident has a responsibility to see that NRWT is deducted from non-resident withholding income. Under section 312(2), if an agent receives income on behalf of a non-resident, and no (or insufficient) NRWT has been deducted from the income, the agent must deduct the shortfall and pay it to Inland Revenue.

For more information on this subject, see Inland Revenue's NRWT Payers Guide (IR 291). You can get a copy from any Inland Revenue office.

Effect of income spreading on Family Support entitlement

Section 374B(1) - Determination of assessable income (for Family Support Credit of Tax): A taxpayer has sold a right to take timber. She is considering applying for a spread of the proceeds under section 81A, and has asked how this would affect her Family Support entitlement.

Section 81A allows a taxpayer who sells timber or a right to take timber to apportion income received between the income year of sale and any number of the three preceding income years. To apportion this income, the seller must apply in writing to Inland Revenue within 12 months after the end of the income year in which the timber was sold.

Under section 374B(1)(d)(i), income which may be spread under the terms of section 81A is included as assessable income in the year in which the income is actually derived. For the purpose of calculating Family Support entitlement, section 374B(1)(e)(ii) excludes this income from the year to which the income was spread.

If the taxpayer applies to spread this income for income tax purposes, her Family Support entitlement in the year the income was derived will be based on the income received before the spread took place.

Assessability of provisional tax use of money interest

Section 413A - Interest on overpaid provisional tax: A taxpayer has asked whether a payment of "use of money interest" from Inland Revenue is taxable income.

Section 413A provides for the payment of interest (known as use of money interest) to a provisional taxpayer who overpays provisional tax. Whether or not the interest is taxable depends on the year of the provisional tax overpayment. The rule is:

- Interest paid on overpaid 1994 (and earlier income years') provisional tax - not taxable.
- Interest paid on overpaid 1995 (and subsequent income years') provisional tax - taxable.

For the 1994 and earlier income years, use of money interest is not taxable because section 61(13A) deemed such interest exempt from tax.

However, section 61(13A) was repealed with effect from the 1994-95 income year onwards. In addition, from the 1994-95 income year, section 413A(8)(b) provides that use of money interest:

> "... shall be deemed to be interest derived by the person for the purposes of Parts IV and IXA of this Act."

Section 65(2)(j), a section within Part IV of the Act, deems payments of interest to be assessable income. This means that use of money interest earned in 1995 or any later income year is taxable income. Inland Revenue will deduct resident withholding tax when we pay the interest.

Goods and Services Tax Act 1985

Credit notes - how to complete GST return

Section 25 - Credit and Debit notes: A GST registered person has asked if she must reduce the output tax figure on her return when she issues a credit note, or whether she is allowed to increase the input tax figure.

When the consideration for a taxable supply is altered, the GST portion of the transaction also needs to be adjusted. If a tax invoice was issued for that supply, a credit (or debit) note that complies with section 25(3) must be issued.

A registered person has the option of accounting for an altered consideration by either reducing the output tax, or claiming a deduction of input tax. The effect of either method is the same.

Example

A seller invoices goods to a buyer for $1,000. The buyer pays the seller $900, as some of the goods were found to be damaged when they were received. The seller issues a credit note for $100.

The seller’s GST return will include $1,000 in Box 5 (sales), and a $100 claim in Box 12 (purchases). This is the method most likely to be used when the sale is accounted for in one taxable period and the credit note is issued in another.

The seller could have shown the net amount of $900 in Box 5 instead. This is usually the method used when the invoice and the credit note are issued in the same taxable period.

Stamp and Cheque Duties Act 1971

Is stamp duty payable on a franchise agreement?

Section 10 - Stamp duty payable: A taxpayer asked whether stamp duty is payable on franchise agreements.

Before 17 March 1988, section 10 provided that stamp duty was payable on every instrument executed after 1 January 1972. “Instrument” was defined for the purposes of the Act in such a manner that franchise agreements could fall within that definition and be held liable for stamp duty.

The Stamp and Cheque Duties Amendment Act (No 2) 1988 amended the definition of “instrument of conveyance”, so that stamp duty is no longer payable on franchise agreements. The Act also amended section 10, so that for instruments executed after 17 March 1988, stamp duty is payable only if the instrument conveys or leases land (other than certain residential land), or conveys shares in a flat- or office-owning company.

Legal decisions - case notes

This section of the Tax Information Bulletin sets out brief notes of recent tax decisions made by the Taxation Review Authority, the High Court, the Court of Appeal and the Privy Council.

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.

Contents

Previously-published cases - appeal notes

TIB Volume Six, No.2

Newman v CIR AP 83/92: The taxpayer is appealing this decision to the Court of Appeal.

TIB Volume Six, No.4

Coveney and others v CIR: Inland Revenue is appealing this decision to the Court of Appeal.

Whether purchase of land for subdivision qualifies for conveyance duty exemption

Rating: • • •

Case: I.C. Baillie v Commissioner of Inland Revenue, M.464/94

Act: Stamp and Cheque Duties Act 1971 - section 24(1)(b)

Keywords: *Conveyance duty, residential land, dwellinghouse, subdivision into residential sections*

Summary: The High Court held on the facts that the objector was not eligible for the conveyance duty exemption under section 24(1)(b) of the Stamp and Cheque Duties Act 1971. The land was purchased for the purpose of subdivision and not that of erecting dwellinghouses.

Facts: The objector and his company Village Heights Limited ("VHL"), were regarded by the Court as synonymous. The objector purchased an area of undeveloped land that was zoned residential. VHL (as nominee for the objector) then entered into various contracts to contour the land and install roading and utilities to enable subdivision of the land into vacant residential sections under the Resource Management Act 1991. VHL entered into sale and purchase agreements with sub-purchasers on "builder's terms". Under the "builder's terms" each sub-purchaser had to settle in full on the first anniversary of the date of possession (five working days after notification that title was available) or upon settlement "of the sale of the proposed dwelling on the said land", whichever was the earlier.

The issue was whether the exemption from conveyance duty in section 24(1)(b) can apply if the purchaser seeking the exemption does not itself intend to erect a dwellinghouse nor to obtain a binding commitment from a sub-purchaser to erect a dwellinghouse "as soon as practicable".

Decision: The High Court found the scheme and purpose approach to statutory analysis argued by the objector was of limited assistance. The Court preferred to focus on the words of the section themselves. His Honour found that the case turned on the phrase "for the purpose of having a dwellinghouse erected on it", and that the relevant purpose must be that of the person who is acquiring the land under the instrument of conveyance for which the exemption is sought.

Justice Blanchard held that although a sub-purchaser purchased the vacant section with the purpose of building a dwellinghouse on it, that fact is not relevant to the first conveyance if the person to whom the property is conveyed under the first instrument does not meet the criteria for the conveyance duty exemption. An exemption may be available to a sub-purchaser who has the purpose of erecting a dwellinghouse, but the exemption would apply to the conveyance to the sub-purchaser, not the conveyance to the objector.

On the facts, Justice Blanchard found that the objector's purpose was to carry out a subdivision of the land into residential sections and to make those sections available to purchasers. It was a matter of relative indifference to the objector whether the dwellinghouse was built.

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

Whether transfer of land was part of a taxable activity

Rating: • • •

Case: TRA No. 91/69

Act: Goods and Services Tax Act 1985 - sections 5, 6, 51.

Keywords: *Taxable activity, supply under matrimonial property agreement, supply to trust, subdivision*

Summary: Two transfers of land, one under a matrimonial property agreement and one to a family trust, were not in the course or furtherance of a taxable activity. The taxable activity of land development had ceased before the transfers took place.

Facts: In 1973 the objector purchased two blocks of land (2B and 2E) for retirement and lifestyle purposes. There was no road access to block 2B. The objector hoped to use the blocks for farming but soon realised that they were not an economic unit. He considered dividing block 2B into smaller blocks so that he could sell them.

From about 1978 to the time when he sold the land the objector had tried to get road access to block 2B but was unsuccessful. From about 1978 to 1987 the objector also tried to get approval to subdivide block 2B. All his applications were

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rejected until 1987 when the district scheme was reviewed and multiple cross-leased housing on one title was permitted subject to approval of a management plan.

The objector submitted a draft plan which was approved. However, this plan was not carried out as it was intended to be a feasibility study only. The objector tried once more in 1988 to sell the land but was unsuccessful.

During this period the objector and his wife had separated. In 1988 they entered into a matrimonial property agreement to subdivide the property. A half share in block 2B was transferred to the wife and then both the husband and the wife transferred their half shares in block 2B to two family trusts. These trusts later formed a partnership to sell block 2B. These transfers took place in February 1989.

Decision: The TRA found that the objector was engaged in the taxable activity of land development before the time of transfer but the transfer of block 2B under the matrimonial property agreement and to the trust were not supplies made in the course or furtherance of the taxable activity. The reason for this is that although the objector's activities were intended to lead to subdivision the taxable activity had failed by February 1989. Therefore, the supplies were made in the course of a matrimonial settlement and also technically in the course of farming.

Although it did not affect the decision, Judge Barber agreed with the Commissioner that if the taxable activity of property development had been in existence in February 1989 then the supplies could have been part of that activity and not within the proviso (c) to section 51(1). This proviso states that a person is not liable to register for GST if the total value of supplies exceeds $30,000 only "as a consequence of any cessation of, or any substantial and permanent reduction in the size or scale of any taxable activity carried on by that person."

Comment: Inland Revenue is not appealing this decision.

Alienation of income from partnership

Rating: • • • • •

Case: TRA No. 92/16

Act: Income Tax Act 1976 - section 75
Matrimonial Property Act 1976 - section 21

Keywords: *Law partnership, alienation of income, personal exertion*

Summary: Partners in a law firm entered into agreements under the Matrimonial Property Act 1976. The partners claimed that the effect of the agreements was that a portion of the law firm income which would previously have been taxable in the hands of the partners was income of the partners' wives. This income was therefore taxable in the wives' hands. The TRA addressed two preliminary issues, then decided that although the matrimonial property agreements were valid, for tax purposes they did not make the income assessable to the wives rather than to the partners in the law firm.

Facts: Partners in a law firm entered into agreements under section 21 of the Matrimonial Property Act. They were equal partners and entitled to equal shares in the law firm's net profits. The matrimonial property agreements transferred one half of each partner's shares in the capital of the partnership. The main issue before the TRA was whether the partners could split their partnership income for tax purposes on the basis that the sums paid to the wives of the partners were a return on the wives' ownership of a capital stake in the partnership.

Decision:

Before the TRA addressed the substantive issue, it addressed two preliminary matters. The first preliminary matter related to objections by the partners to assessments for the 1989-1991 income years. The Commissioner had applied to the High Court for an order that a case stated in respect of the partners' objection be stated directly to the High Court. The partners submitted that under regulation 5(1) of the Taxation Review Authority Regulations 1974, the Commissioner must file a case stated within six months of receiving the objections. The Commissioner had not done this, so the partners submitted that the TRA should therefore allow their objections. The Commissioner submitted that under the proviso to regulation 5, a case stated need not be filed with the TRA until six months after the date on which the High Court refuses the application; otherwise the High Court would deal with the 1989 to 1991 assessments.

Judge Barber found that, as the High Court had not yet (at the date of the TRA hearing) dealt with the Commissioner's application, the Commissioner was not out of time for filing a case stated. Judge Barber dismissed the partners' application to allow the objections for the 1989 to 1991 years. After the TRA hearing, Justice Penlington (High Court, Hamilton, M280/94) decided that the partners' objections for the 1989 to 1991 income years should be referred directly to the High Court.

The second preliminary matter related to the assessments for the 1986 to 1988 income years. This issue was whether the Commissioner had stated his grounds of assessment and disallowance of the partners' objections so narrowly that the Commissioner was restricted to making an argument on section 75 of the Income Tax Act 1976 only. Section 75 deems income to be derived by a taxpayer even though the income is not actually paid to or received by the taxpayer. If the argument was restricted to section 75, the Commissioner could not put forward an argument based on the general legal principle that income earned from personal activities cannot be effectively assigned for tax purposes. The partners argued that the Commissioner was now seeking to change the basis of his assessment and that principles established by the Court of Appeal in *CIR v Farnsworth Ltd* [1984] 1 NZLR 428 prevented him from doing so.

Judge Barber stated that *Farnsworth* limits the Commissioner to the basis on which he arrived at an assessment and at the hearing he cannot rely on a different provision on which the parties have not joined issue. Judge Barber found that the Commissioner had not changed his ground or approach. Rather, the Commissioner had changed his emphasis without in any way creating surprise or prejudice to the partners. The Commissioner was not restricted to making an argument based on the application of section 75 only.

The substantive issue before the TRA was whether the income assigned for the 1986 to 1988 income years should be regarded, for tax purposes, as income of the partners or of their wives. Judge Barber found that the partners could not assign the income for tax purposes. Judge Barber found that the partners' legal partnership was a normal professional legal partnership and that the income generated by it was, as a matter of fact, predominantly generated by the personal exertion of the partners. The rule that income earned from personal exertion cannot be assigned for tax purposes has been conclusively determined by the Court of Appeal and Privy Council in *Hadlee & Sydney Bridge Nominees Ltd v CIR* [1991] 3 NZLR 517 and *Hadlee v CIR* [1993] 2 NZLR 385. This rule cannot be overcome by the Matrimonial Property Act 1976. The matrimonial property agreements do not take effect for income tax purposes until after the income is derived by the partners.

Judge Barber found that nothing turns on the fact that the shares in the partnership were described as being disposed of by way of transfer as opposed to an

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assignment. Any distinction drawn on the basis of the method used to dispose of the interest does not change the principle that disposition of the interest itself is ineffective for tax purposes.

Comment: We do not know if the taxpayers are appealing this decision.

Whether sale of Government stock by a finance company is assessable income

Rating: • • •

Case: AA Finance Limited v CIR CA 204/93

Act: Income Tax Act 1976 - section 65(2)(a)

Keywords: *Gains derived from business, capital v income, Government stock*

Summary: The Court of Appeal upheld the High Court decision finding that the acquisition and holding of Government stock was a necessary incident of operating as a finance company. Accordingly, any gain from the sale or realisation of Government stock was assessable income.

Facts: The taxpayer is a finance company. The appeal concerned the assessability of gains derived by the taxpayer on dealings in Government stock over the income years 31 March 1984 to 1987 inclusive. Up until 1985 the taxpayer was subject to investment regulations that required it to hold Government stock. During the period in question, certain parcels of Government stock were sold or matured realising a gain over their acquisition price. In most instances the taxpayer had purchased the stock at a discount.

The taxpayer's trust deed contained borrowing restrictions, including limits linked to the lesser of market value or cost price of its Government stock. During the relevant period, the market value of its Government stock fell below its cost price. To avoid a possible breach of the trust deed, the taxpayer entered into a number of transactions involving the sale of Government stock, at a price in excess of cost. The taxpayer achieved this by selling stock, and then immediately purchasing securities having similar interest rates and maturity dates to the previously disposed of stock. These transactions were loosely described as "swap transactions" and recorded in the taxpayer's accounts as having given rise to a gain. They were designed to ensure that the value of the taxpayer's remaining Government stock could be demonstrated to be at least equivalent to its cost price.

The Commissioner treated the difference between acquisition cost and the recorded price on the maturity or sale of all Government stock during the relevant period as assessable income. This was as income derived from any business under section 65(2)(a), interest under section 65(2)(j) and income from any other source under section 65(2)(l). The taxpayer objected and a case was stated to the High Court. The High Court held that gains had been made. The gains were assessable income being profits or gains derived from the taxpayer's business, and income from any other source.

Decision: The Court of Appeal considered the primary argument related to the application of section 65(2)(a). The crucial questions were whether the realisation transactions were on revenue account, and if so, in relation to the swap transactions, whether the taxpayer derived any gains on those realisations.

As to whether gains produced in a business are revenue or capital, the Court of Appeal was not persuaded that Justice Heron had erred in what it considered to be essentially a factual assessment. As a finance company the taxpayer derived its income from the borrowing and lending of money. Money is the stock in trade of a finance company. The holding of Government stock was a necessary incident of operating as a finance company. There was nothing special in the taxpayer's business to derogate from that conclusion. There was no basis in fact for the argument that Government stock represented an investment separate from, and unconnected with, the taxpayer's ordinary trading activities. The Government stock dealings formed part of the totality of the business.

The Court dismissed the taxpayer's contention that, in respect of the Government stock involved in the swap transactions, it had only swapped securities for securities, not for cash. The Court looked to the legal arrangements entered into and carried out, and not the end economic result. It noted that the transactions were not constructed as an exchange of securities. The taxpayer's accounts recorded the transactions as sales for cash, yielding cash gains and reflected the taxpayer's intentions. The Court considered that the taxpayer "must live with the fiscal consequences of the way in which the transactions were structured".

The Court of Appeal thought it unnecessary to consider the possible application of sections 65(2)(j) and 65(2)(l).

Comment: The taxpayer is not appealing this decision.

Whether GST inputs credits claimable on development of a retirement village

Rating: • • •

Case: Norfolk Apartments Limited v Commissioner of Inland Revenue HC Auckland M 296/94

Act: Goods and Services Tax Act 1985 - section 14, 20(3), 21(5)

Keywords: *Retirement village, principal purpose, common areas, dwelling, apportionment*

Summary: The High Court decided the Commissioner acted correctly in disallowing Norfolk Apartments Limited's ("NAL") objections to an assessment. The assessment disallowed claims for input tax credits or refunds of GST associated with the acquisition of land and the expenses involved in constructing a retirement village on that land.

Facts: NAL purchased land with local authority consent to build a retirement village. NAL entered into a contract for the construction of a retirement village. The facility was constructed on the basis that residents would have exclusive transferable occupation licences to occupy an apartment and garage, and an ancillary right to enjoy common areas. Under the occupation licence the right to use the common areas was on the basis that an apartment service fee was paid. The fee was payable to an associated company, Norfolk Apartments Management Limited, for providing the service of running and administering the apartments.

NAL contended that its principal purpose in acquiring the land and constructing the premises was to carry on a taxable activity. On this basis NAL claimed that the GST on the purchase of the land and the GST on the construction materials were deductions for which it was entitled to obtain a credit.

Decision: Justice Robertson held that NAL's principal purpose in purchasing, developing and constructing apartments on the land was to supply accommodation to residents in a retirement village. This is an exempt supply under section 14. There was an associated supplementary intention to carry on a taxable activity by providing additional services, but this was an ancillary or incidental purpose. Justice Robertson also held that the building was not a commercial dwelling.

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Because the principal purpose of acquiring and developing the land was to make exempt supplies, no apportionment was available under section 21(5). Adjustments can only be made if there is a subsequent application for the purpose of making taxable supplies.

Comment: The taxpayer is appealing this decision.

Upcoming TIB articles

In the next few months we'll be releasing policy statements on these topics in the Tax Information Bulletin:

- Income tax treatment of overseas teachers and researchers deriving income in New Zealand
- Fringe benefits granted to employees of overseas branches
- The application of GST to gaming machines
- Expenses incurred in pollution control
- Depreciation claims usually mandatory
- Residential property exempt from conveyance duty
- Tax treatment of payments made for part-time domestic work
- Persons eligible to apply for a certificate of exemption for resident withholding tax
- When Inland Revenue can grant relief from payment of tax in cases of financial hardship
- Meaning of terms "own" and "acquired" for depreciation purposes
- GST and rates apportionment

We'll publish these statements as soon as we've finished consulting with commentators outside Inland Revenue.

Due dates reminder

January 1995

5 Large employers: PAYE deductions and deduction schedules for period ended 31 December 1994 due.

7 Provisional tax and/or Student Loan interim repayments: first 1995 instalment due for taxpayers with September balance dates.
Second 1995 instalment due for taxpayers with May balance dates.
Third 1995 instalment due for taxpayers with January balance dates.

1994 end-of-year payments of income tax, Student Loans and ACC premiums due for taxpayers with February balance dates.

Non-IR 5 taxpayers: annual income tax returns due for taxpayers with September balance dates.

QCET payments due for companies with February balance dates with elections effective from the 1995 income year.

(We will accept any payments received on Monday 9 January 1995 as in time for 7 January 1995.)

15 GST return and payment for period ended 30 November 1994 due. *(We will accept payments received on Monday 16 January as on time.)*

20 Large employers: PAYE deductions and deduction schedules for period ended 15 January 1995 due.

Small employers: PAYE deductions and deduction schedules for period ended 31 December 1994 due.

FBT return and payment for quarter ended 31 December 1994 due.

Gaming machine duty return and payment for month ended 31 December 1994 due.

RWT on interest deducted during December 1994 due for monthly payers.

RWT on dividends deducted during December 1994 due.

Non-resident withholding tax (or approved issuer levy) deducted during December 1994 due.

31 GST return and payment for period ended 31 December 1994 due.

February 1995

5 Large employers: PAYE deductions and deduction schedules for period ended 31 January 1995 due. *(We will accept any payments received on Tuesday 7 February as in time.)*

7 Provisional tax and/or Student Loan interim repayments: first 1996 instalment due for taxpayers with October balance dates.
Second 1995 instalment due for taxpayers with June balance dates.
Third 1995 instalment due for taxpayers with February balance dates.

1994 end-of-year payments of income tax, Student Loans and ACC premiums due for taxpayers with March-September balance dates.

QCET payments due for companies with March-September balance dates, for elections effective from the 1995 income year.

20 Large employers: PAYE deductions and deduction schedules for period ended 15 February 1995 due.

Small employers: PAYE deductions and deduction schedules for period ended 31 January 1995 due.

Gaming machine duty return and payment for month ended 31 January 1995 due.

RWT on interest deducted during January 1995 due for monthly payers.

RWT on dividends deducted during January 1995 due.

Non-resident withholding tax (or approved issuer levy) deducted during January 1995 due.

28 GST return and payment for period ended 31 January 1995 due.

Contents continued - questions and legal case notes

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Legal decisions - case notes (pages 28-35)

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