

# T AX INFORMATION BULLETIN

Volume Ten, No.7

July 1998

## Contents

### Legislation and determinations

Hydrogen manufacturing unit and hydrocracker catalysts (DEP37) .....	3
Woven reflective mulch (DEP38) .....	4
Crayfish (baby) – peurulus traps (PROV7) .....	4
Farm and fishing vessel ownership savings accounts .....	5
1998 deemed rate or return announced for foreign investment fund regime .....	5
Electricity revenue and data logging terminals – depreciation .....	6
Bird netting – depreciation .....	7

### Interpretation statements

Available subscribed capital – consequences of deemed reregistration .....	8
--	---

### Interpretation guidelines

Computer software – payment to non-resident for use (PIB article withdrawal) .....	11
--	----

### Questions we've been asked

Answers to enquiries we've received at Inland Revenue, which could have a wider application.  
See the inside front cover for a list of topics covered in this bulletin .

### Legal decisions - case notes

Notes on recent cases heard by the Taxation Review Authority, the High Court, the Court of Appeal and the Privy Council. See the inside front cover for a list of cases covered in this bulletin.

### General interest items

Due dates reminder .....	16
Public binding rulings and interpretation statements: your chance to comment before we finalise them .....	17

*This TIB has no appendix*



Inland Revenue  
*Te Tari Taake*

ISSN 0114-7161

This is an Inland Revenue service to people with an interest in New Zealand taxation.

## Contents continued - questions and legal case notes

### Questions we've been asked (pages 11-12)

Child support – shared custody .....	11
--------------------------------------	----

### Legal decisions - case notes (pages 13-15)

Chatham Islands Trust taking over former Government activities – whether limited to “financial transaction” for GST purposes .....	13
Enterprise Trust v CIR	
Auckland Harbour Board v CIR Business transferred from harbour board to port company – deductions disallowed .....	14
TRA 96/104 Farm land subdivided and sold – whether GST taxable activity .....	14
Roma Properties Ltd v CIR Employee status of company directors .....	15
TRA 91/134 Shares issued as part of purchase – whether payment made .....	15

## Get your TIB sooner by internet

This Tax Information Bulletin is also available on the Internet, in two different formats:

### Online TIB (HTML format)

- This is the better format if you want to read the TIB on-screen (single column layout).
- Any references to related TIB articles or other material on our website are hyperlinked, allowing you to jump straight to the related article. This is particularly useful when there are subsequent updates to an article you're reading, because we'll retrospectively add links to the earlier article.
- Individual TIB articles will print satisfactorily, but this is not the better format if you want to print out a whole TIB.
- All TIBs from January 1997 onwards (Volume Nine, No.1) are available in this format.

Online TIB articles appear on our website **as soon as they're finalised** – even before the whole TIB for the month is finalised at mid-month. This means you can read the first of any month's TIB articles on our website in the last two weeks of the previous month.

### Printable TIB (PDF format)

- This is the better format if you want to print out the whole TIB to use as a paper copy – the printout looks the same as this paper version.
- You'll need Adobe's Acrobat Reader to use this format – available free from their website at <http://www.adobe.com>
- Double-column layout means this version is better as a printed copy – not as easy to read on-screen.
- All TIBs from July 1989 (the start of the TIB) are available in this format.

The printable TIB appears on our website at mid-month, at the same time as we send the paper copy to the printers. This means you can get a printable TIB from our website about two weeks before we can post you a paper copy.

### Where to find us

Our website is at <http://www.ird.govt.nz>

It also includes other Inland Revenue information which you may find useful, including any draft binding rulings and interpretation statements that are available, and many of our information booklets.

**If you find that you prefer the TIB from our website and no longer need a paper copy, please let us know so we can take you off our mailing list. You can e-mail us from our website.**

## Legislation and determinations

This section of the TIB covers items such as recent tax legislation, accrual and depreciation determinations, livestock values and changes in FBT and GST interest rates.

### Hydrogen manufacturing unit and hydrocracker catalysts

#### Depreciation Determination DEP37

In TIB Volume Ten, No.4 (April 1998) at page 41, we published a draft general depreciation determination for hydrogen manufacturing unit (HMU) catalysts or hydrocracker catalysts (either rechargeable or non-rechargeable). These assets are used in the oil refining industry. No submissions were received on this draft and

the Commissioner has now issued the determination. It is reproduced below and may be cited as "Determination DEP37: Tax Depreciation Rates Determination general Determination No. 37". The determination is based on the estimated useful lives (EUL) as set out in the determination and residual values of 13.5%.

#### General Depreciation Determination DEP37

This determination may be cited as "Determination DEP37: Tax Depreciation Rates General Determination Number 37".

#### 1. Application

This determination applies to taxpayers who own the asset classes listed below.

This determination applies to "depreciable property" other than "excluded depreciable property" for the 1995/96 and subsequent income years.

#### 2. Determination

Pursuant to section EG 4 of the Income Tax Act 1994 I hereby amend Determination DEP1: Tax Depreciation Rates General Determination Number 1 (as previously amended) by:

- Inserting into the "Oil and Gas Industry" industry category the general asset classes, estimated useful lives, and diminishing value and straight-line depreciation rates listed below:

Oil and Gas Industry	Estimated useful life (years)	DV banded dep'n rate (%)	SL equivalent banded dep'n rate (%)
Hydrogen Manufacturing Unit (HMU) Catalyst	5	33	24
Hydrocracker Catalyst – non-rechargeable	2	63.5	63.5
Hydrocracker Catalyst – rechargeable	4	40	30

#### 3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax Act 1994.

This determination is signed by me on the 12th day of June 1998.

Martin Smith  
General Manager (Adjudication & Rulings)

---

## Woven reflective mulch

### Depreciation Determination DEP38

---

In Tax Information Bulletin Volume Ten, No.4 (April 1998), we published a draft general depreciation determination for woven reflective mulch and invited readers to make submissions on the proposed depreciation rate. No submissions were received and the Commissioner has now issued the determination.

The determination is reproduced below and may be cited as “Determination DEP38: Tax Depreciation Rates General Determination No.38”. The determination is based on an estimated useful life of 3 years and a residual value of 13.5%.

---

### General Depreciation Determination DEP38

This determination may be cited as “Determination DEP38: Tax Depreciation Rates General Determination Number 38”.

#### 1. Application

This determination applies to taxpayers who own the asset classes listed below.

This determination applies to “depreciable property” other than “excluded depreciable property” for the 1997/98 and subsequent income years.

#### 2. Determination

Pursuant to section EG 4 of the Income Tax Act 1994 I hereby amend Determination DEP1: Tax Depreciation Rates General Determination Number 1 (as previously amended) by:

- Inserting into the “Agriculture, Horticulture and Aquaculture” industry category the general asset class, estimated useful life, and diminishing value and straight-line depreciation rate listed below:

Agriculture, Horticulture and Aquaculture	Estimated useful life (years)	DV banded dep'n rate (%)	SL equivalent banded dep'n rate (%)
Woven Reflective Mulch	3	50	40

#### 3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax Act 1994.

This determination is signed by me on the 25th day of June 1998.

Martin Smith  
General Manager (Adjudication & Rulings)

---

## Crayfish (baby) – peurulus traps

### Provisional Depreciation Determination PROV7

---

The Commissioner has issued Determination PROV7: Tax Depreciation Rates Provisional Determination Number 7, which applies to Peurulus (baby crayfish) traps. The determination is reproduced below.

---

### Provisional Depreciation Determination PROV7

This determination may be cited as “Determination PROV7: Tax Depreciation Rates Provisional Determination Number 7”.

#### 1. Application

This determination applies to taxpayers in the fishing industry category.

This determination applies to “depreciable property” other than “excluded depreciable property” for the 1996/97 and subsequent income years.

## 2. Determination

Pursuant to section EG 10(1)(b) of the Income Tax Act 1994 I hereby amend Determination DEP1: Tax Depreciation Rates General Determination Number 1 (as previously amended) by:

- Inserting into the “Fishing” industry category the provisional asset class, estimated useful life, and diminishing value and straight-line depreciation rate listed below:

Fishing	Estimated useful life (years)	DV banded dep'n rate (%)	SL equivalent banded dep'n rate (%)
Peurulus (baby crayfish) traps	1	100	100

## 3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax Act 1994.

This determination is signed by me on the 23rd day of June 1998.

Martin Smith  
General Manager (Adjudication & Rulings)

# Farm and fishing vessel ownership savings accounts

## Withdrawals without payment of withdrawal tax

### Introduction

The Farm and Fishing Vessel Ownership Savings Schemes (Closure) Act 1998 allows farm and fishing vessel ownership savings accounts to be closed without payment of withdrawal tax.

### Background

Section KG 1 of the Income Tax Act 1994 allows a tax rebate of 45 cents in the dollar for deposits (within certain limits) to farm and fishing vessel ownership accounts. Withdrawals from the two schemes that did not satisfy the criteria of the schemes were subject to withdrawal tax (Subpart IZ of the Income Tax Act refers).

### Key features

The amendments provide that certain withdrawals which do not satisfy the criteria can be made without payment of withdrawal tax if accounts are closed.

Accounts continuing to exist as at 30 June 2001 will be closed automatically, with deposits being refunded and no withdrawal tax being charged.

From 30 June 1998 savers who have not deposited funds since 14 May 1998 will be able to close their accounts without attracting withdrawal tax.

If deposits are made after 30 June 1998, normal rules will continue to apply, except that the account will be closed on 30 June 2001. All deposits will be refunded on that date, no withdrawal tax will be payable.

Transitional rules apply to deposits made after 14 May 1988 but before 30 June 1998. If accounts are closed before 30 June 2001, withdrawal tax will be charged on the withdrawal of deposits made between 14 May 1998 and 30 June 1998 only.

### Application date

The amendments apply from the date the Act received the Royal assent (22 May 1998).

## 1998 deemed rate of return announced for foreign investment fund regime

The deemed rate of return used for the foreign investment fund regime has been set at 11.01% for the 1997-1998 income year. The rate will apply to all types of investments, including interests in superannuation schemes and life insurance policies.

The FIF regime taxes the income earned by foreign entities on behalf of New Zealand residents, when the Controlled Foreign Company rules do not apply.

The deemed rate of return method is one of four methods for calculating FIF income or loss. The rate for future income years will continue to be set annually.

# Electricity revenue and data logging terminals

## Draft general depreciation determination

We have been advised that there is no suitable general depreciation rate for Electricity Revenue and Data Logging Terminals. The terminals are installed in businesses and homes, and record the amount of electricity used and the times of usage. These details are stored by the meter and downloaded, via modem, from time to time, to give the electricity provider information that allows customers to be billed and enables the provider to design network capacities and to fix charge out rates for the electricity. Customers are also able to access the information so that they may consider how best to take advantage of off-peak rates etc.

The Commissioner proposes to issue a general depreciation determination which will insert a new asset class

“Electricity Revenue and Data Logging Terminals” into the “Power Generation and Electrical Reticulation Systems” industry category, with a depreciation rate of 22% (D.V.) (15.5% S.L.), based on an estimated useful life of 8 years. The Commissioner accepts that there is a much higher rate of technical obsolescence and a higher turn-over when this type of equipment is leased, so the determination sets a separate rate for leased terminals.

The draft determination is reproduced below. The proposed new depreciation rates are based on the estimated useful lives set out in the determination and a residual value of 13.5%.

### General Depreciation Determination DEP[X]

This determination may be cited as “Determination DEP[x]: Tax Depreciation Rates General Determination Number [x]”.

#### 1. Application

This determination applies to taxpayers who own the asset classes listed below.

This determination applies to “depreciable property” other than “excluded depreciable property” for the 1997/98 and subsequent income years.

#### 2. Determination

Pursuant to section EG 4 of the Income Tax Act 1994 I hereby amend Determination DEP1: Tax Depreciation Rates General Determination Number 1 (as previously amended) by:

- Inserting into the “Power Generation and Electrical Reticulation Systems” industry category the general asset classes, estimated useful lives, and diminishing value and straight-line depreciation rates listed below:

<b>Power Generation and Electrical Reticulation Systems</b>	<b>Estimated useful life (years)</b>	<b>DV banded dep'n rate (%)</b>	<b>SL equivalent banded dep'n rate (%)</b>
Electricity Revenue and Data Logging Terminals	8	22	15.5
Electricity Revenue and Data Logging Terminals (when leased)	4	40	30

#### 3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax Act 1994.

If you wish to make a submission on the proposed changes, please write to:

Assistant General Manager (Adjudication & Rulings)  
 Adjudication & Rulings  
 National Office  
 Inland Revenue Department  
 P O Box 2198  
 WELLINGTON

We need to receive your submission by 31 August 1998 if we are to take it into account in finalising the determination.

# Bird netting

## Draft general depreciation determination

We have been advised that there is currently no suitable general depreciation rate for bird netting, used by winegrowers to protect ripening grapes from birds. The netting is removed when the grapes are picked. It is subject to tearing from snagging on the vine as it is put up or taken in, and also deteriorates in sunlight. At the end of each season, netting is patched and repaired before being stored out of the sunlight until the next season's use.

The Commissioner proposes to issue a general depreciation determination which will insert a new asset class "Bird netting" into the "Brewing, Winemaking and Distilleries" industry category, with a depreciation rate of 33% D.V. (24% S.L.), based on an estimated useful life of 5 years.

This determination would be distinguished from the "Questions We've Been Asked" item published in Tax Information Bulletin Volume Seven, No.6 (December 1995) at page 21. That item advised taxpayers to treat bird netting as an expense, because the netting in question was expected to last for only one season. Taxpayers who use that type of bird netting should continue to treat the expenditure as an expense item.

The draft determination is reproduced below. The proposed new depreciation rates are based on the estimated useful life set out in the determination and a residual value of 13.5%.

### General Depreciation Determination DEP[X]

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

#### 1. Application

This determination applies to taxpayers who own the asset classes listed below.

This determination applies to "depreciable property" other than "excluded depreciable property" for the 1997/98 and subsequent income years.

#### 2. Determination

Pursuant to section EG 4 of the Income Tax Act 1994 I hereby amend Determination DEP1: Tax Depreciation Rates General Determination Number 1 (as previously amended) by:

- Inserting into the "Brewing, Winemaking and Distilleries" industry category the general asset class, estimated useful life, and diminishing value and straight-line depreciation rates listed below:

Brewing, Winemaking and Distilleries	Estimated useful life (years)	DV banded dep'n rate (%)	SL equivalent banded dep'n rate (%)
Bird netting	5	33	24

#### 3. Interpretation

In this determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax Act 1994.

If you wish to make a submission on the proposed changes, please write to:

Assistant General Manager (Adjudication & Rulings)  
Adjudication & Rulings  
National Office  
Inland Revenue Department  
P O Box 2198  
WELLINGTON

We need to receive your submission by 31 August 1998 if we are to take it into account in finalising the determination.

## Interpretation statements

This section of the TIB contains interpretation statements issued by the Commissioner of Inland Revenue. These statements set out the Commissioner's view on how the law applies to a particular set of circumstances when it is either not possible or not appropriate to issue a binding public ruling.

In most cases Inland Revenue will assess taxpayers in line with the following interpretation statements. However, our statutory duty is to make correct assessments, so we may not necessarily assess taxpayers on the basis of earlier advice if at the time of the assessment we consider that the earlier advice is not consistent with the law.

## Available subscribed capital – consequences of deemed reregistration

### Introduction

Under the Income Tax Act 1994, the concept of “available subscribed capital” (ASC) is important in determining whether a distribution by a company to its shareholders is a dividend or a return of capital. The definition of available subscribed capital in section OB 1 is concerned with calculating the amount of available subscribed capital referable to a particular class of share at a point in time. Essentially, it reflects the amounts paid to the company on the issue of shares, less amounts paid out on the repurchase of shares when those amounts are not dividends.

Under the Companies Reregistration Act 1993, any company registered under the Companies Act 1955 is deemed reregistered under the Companies Act 1993 as from the close of 30 June 1997 (or some Court-approved extended time). One effect of reregistration is that the previous memorandum and articles of the company cease to have effect, and the company is then governed by the provisions in the Companies Act 1993.

Under section 28 of the Companies Act 1993, companies without a constitution have rights, powers, duties and obligations as set out in that Act. Further, section 36 sets out shareholder rights and powers for such companies, and in particular provides that a share in a company confers on the holder: the right to vote, dividends, and an equal share in the distribution of surplus company assets. If a company has more than one share class, those share classes merge into the ordinary share class.

We have been asked what effect, if any, the merging of share classes, pursuant to a deemed reregistration under the Companies Reregistration Act 1993, has on ASC.

### Legislation

Available subscribed capital is defined in section OB 1 of the Income Tax Act 1994. The relevant parts of the definition are:

Available subscribed capital, ..., means the amount calculated in accordance with the following formula in respect of all shares of the same class (referred to in this definition as the “specified class”) as the share:

$a + b - c$

where -

a is -

- (i) In the case of any company which existed before 1 July 1994, the transitional capital amount; and
- (ii) In any other case, nil; and

b is the aggregate amount of consideration received by the company on or after 1 July 1994 and before the relevant time in respect of the issue of all shares in the company of the specified class, including as consideration -

...

c is the aggregate of amounts distributed -

- (i) Upon the acquisition, redemption, or other cancellation by the company of shares in the company of the specified class; and
- (ii) On or after 1 July 1994 and before the relevant time; and

...

This definition looks at relevant amounts attributable to shares of the same class (referred to as the “specified class”). The formula calculates the total amount the company received on the issue of a particular class of share, less the total amounts distributed by the company following any acquisition, cancellation, or redemption of the shares.

Generally, shares remain in their specified class and the calculation of ASC is relatively straightforward. But if shares move from a class to become members of another class (“altered shares”) as a result of deemed reregistration, the ASC calculation becomes a little more complex.

### Effect of alteration

With an alteration of shareholder rights, a number of issues emerge:

- Does an alteration have the effect of cancelling shares?
- To what class do the altered shares belong?
- On what basis is ASC calculated for altered shares?
- On rectification of altered shares, what is the value of consideration received?



## No share cancellation

An alteration of shareholder rights is not a cancellation and reissue of shares. The shareholder still owns the original shares, but certain entitlements attaching to the shares are varied in some way.

## The appropriate class

For ASC purposes, a specified class is a reference to “shares of the same class” as defined in section OB 1. This definition generally classifies shares on the basis of any 2 (or more) shares having similar attributes. For example, shares of the same class have identical rights as to voting, decision making, and distribution entitlements. The effect of deemed reregistration is that **all** shares become, at the time of deemed reregistration, members of the ordinary share class.

## ASC following deemed reregistration

The ASC definition looks at the balance of the consideration received for all shares in the specified class at the time of calculation, less relevant distributions. For shares originally issued in the specified class, paragraph (b) credits amounts received on issue and paragraph (c) debits amounts distributed.

The definition is concerned with all shares in the specified class at the relevant time – being the time when ASC is calculated. The altered shares simply become members of the new specified class at the time of alteration, and the ASC amount of the altered shares is included in the calculation of ASC of the new specified class.

For “altered” shares, a focus on amounts credited and debited **at issue** is not appropriate because ASC is calculated in terms of the “new” specified class. Accordingly, the altered share component of the ASC of the ordinary share class should reflect **the ASC balance as at the time of alteration**. This approach avoids the ASC of the altered shares being trapped in its original specified class.

The ASC of the altered shares is the balance of the consideration received for all shares in the altered shares class, less relevant distributions. This calculation is made as at the time of the alteration, being the close of 30 June 1997 or such later day if a Court has granted an extended time to reregister.

## Rectification of shareholder rights

If a company decides to alter the rights attaching to a share class, the possibility of varying the relative interests of shareholders arises because of the potential dilution of shareholder rights. The Companies Act 1993 minimises the potential impact of this by ensuring that the company does not take any action that affects the rights attached to shares, unless the action has been approved by a special resolution.

With deemed reregistration, the shareholders do not have the option to decide on the variation of their rights. The rights are altered by statute. For ASC purposes the merging of different specified classes, due to deemed reregistration, may dilute the rights and subscribed capital originally received for shares in the original share class and in the altered classes. If the company takes no action to “rectify” the effect of the alteration of shareholder rights (such as creating a new class of share), the amount of ASC for the specified class will include the ASC amounts for the altered shares as at the time of deemed reregistration.

However, if a company proposes to rectify the effect of the variation, the question arises as to the value of the consideration received for the shares.

- Is it the original issue price?
- Is it calculated on the ASC value per share as at the time of deemed reregistration?
- Is it found by dividing the ASC for the specified class by the number of shares in the class immediately prior to rectification?

In the Commissioner’s view, when enacting the definition of ASC Parliament did not expressly turn its mind to the potential effect of deemed reregistration. However, it is clear that the definition of ASC is concerned with calculating the balance of consideration received less distributions of shares in a share class. Like deemed reregistration, a rectification is not an issue of shares. Accordingly, the relevant consideration should be calculated as at the time the altered shares join the new specified class, i.e. immediately prior to the rectification.

On this basis, it is appropriate that, if a company alters the shareholder rights to rectify the effect of deemed reregistration, it is the proportionate amount of ASC, calculated by dividing the ASC for the specified class by the number of shares in the class immediately prior to rectification, that becomes the ASC of the rectified class.

## Reissue of shares

The result outlined above may be contrasted with one where, instead of a reclassification, the shares of the other class (e.g. preference shares) are redeemed by conversion into ordinary shares. Whereas a reclassification is an **alteration** of the rights attaching to **existing** shares, a conversion involves the issue of new shares. For ASC purposes, the consideration received for the ordinary shares is not based on the price of preference shares at the time of issue, but it is the market value at the point of conversion. This reflects the reality that the conversion triggers a tax event in the form of a cancellation and new issue, while a reclassification, of itself, does not.

*continued on page 10*

from page 9

## Examples

The following examples illustrate the operation of this approach.

---

### Example 1: pre-deemed reregistration

This example illustrates the calculation of ASC as at 29 June 1997 (prior to deemed reregistration).

A company is formed on 1 August 1994, and issues 10,000 ordinary shares at \$1 per share. It issues a further 5,000 ordinary shares at \$1 per share on 1 December 1994; at the same time issuing 4,000 preference shares at \$1.50. A further issue of 3,000 preference shares (at \$1.50 per share) is made on 1 March 1996.

The company decides to cancel some ordinary shares and redeem some preference shares. On 1 December 1996, 4,000 ordinary shares are cancelled at \$1.50 per share. On the same day, the company redeems 2,000 preference shares at \$2.00 per share.

#### Calculation of ASC

##### Ordinary share class

ASC is defined as:  $a + b - c$

$a = \text{nil}$

$b = \text{all consideration received in respect of the issue of ordinary shares, i.e. } \$10,000 + \$5,000 = \$15,000$

$c = \text{the aggregate amount distributed upon the cancellation by the company of shares in the company of the specified class} = \$6,000 \text{ (4,000 at } \$1.50 \text{ per share)}$

ASC for ordinary share class is \$9,000  
 (\$15,000 - \$6,000).

##### Preference share class

$a = \text{nil}$

$b = \$10,500 \text{ (7,000 shares at } \$1.50 \text{ per share)}$

$c = \$4,000 \text{ (2,000 shares at } \$2.00 \text{ per share)}$

ASC for preference share class is \$6,500.

---

### Example 2: post-deemed reregistration

This example illustrates the ASC calculation following deemed reregistration.

This example uses the same facts as Example 1, except that the ASC is measured as at 1 July 1997.

#### Calculation of ASC

Due to deemed reregistration, there are no longer any shares in the preference share class and therefore no ASC to calculate for that class.

##### Ordinary share class

Prior to the alteration of rights, the ASC in the ordinary class was \$9,000 and in the preference share class, \$6,500 (see Example 1).

The effect of the alteration of rights is that the preference shares become ordinary shares. The "altered" preference shares (and the ASC amount) simply join the ordinary share class. The ASC amount is \$15,500. This amount includes the amount of ASC for the ordinary shares as calculated in Example 1 (\$9,000) and the ASC balance of the preference shares when they became ordinary shares as calculated in Example 1 (\$6,500).

---

### Example 3: rectification

In this example the company wishes to re-establish the preference share class, and to this end, on 10 July 1997 it alters the rights of 3,000 ordinary shares.

#### Calculation of ASC

##### Preference share class

When shares join another class, the relevant ASC goes with them. In this example 3,000 ordinary shares become preference shares and the ASC for these shares must be calculated as at the time of reclassification. This figure is found by calculating the value of the ASC per ordinary share, multiplied by the number of shares reclassified.

ASC for the ordinary shares (at the time of reclassification) = \$15,500 (see Example 2).

Number of ordinary shares on issue = 16,000 (see Example 1).

ASC per ordinary share =  $(\$15,500 / 16,000) = \$0.96875$ .

Accordingly the value of the ASC for the 3,000 preference shares is \$2,906.

##### Ordinary share class

The ASC for the ordinary share class following reclassification can be found by calculating the ASC for the class (prior to reclassification), less the ASC for the preference shares (\$2,906).

Prior to reclassification, the consideration received in respect of the issue of the ordinary shares is  $[10,000 \times \$1] + [5,000 \times \$1] + [\text{ASC for the "altered" preference shares} = (\$6,500)] = \$21,500$ .

$b = \$21,500$

$c = \text{the aggregate amount distributed upon the cancellation by the company of shares in the company of the specified class} = \$6,000 \text{ (4,000 at } \$1.50 \text{ per share)}$ .

ASC for the ordinary share class is \$15,500  
 (\$21,500 - \$6,000)

After reclassification, 3,000 ordinary shares become preference shares and item 'b' becomes  
 $\$21,500 - \$2,906 = \$18,594$ .

Item 'c' = \$6,000

ASC for the ordinary share class is \$12,594  
 (\$18,594 - \$6,000).

---

## Interpretation guidelines

The items in this section of the TIB discuss the Commissioner's approach to the interpretation of a general area of law.

Interpretation guidelines are intended to clarify general points of interpretation that are causing, or may cause, difficulty for practitioners, taxpayers, and Inland Revenue. An interpretation guideline is Inland Revenue's opinion as to the better view of the law. That view is developed from an appreciation and assessment of the law on a particular topic, as gathered from leading cases.

## Computer software – payment to non-resident for use Notice of withdrawal of PIB 168 article

The Commissioner gives notice of the withdrawal of the present policy on the income tax treatment of payments made for the use of computer software set out in Public Information Bulletin 168 (January 1988).

The Commissioner is reviewing the income tax treatment of computer software transactions with non-residents and, in the interim, pending the conclusion of the review, believes it appropriate to withdraw the item. The practical effect of this notice is that all published

policy is withdrawn dealing with the income tax implications of computer software transactions with non-residents. Accordingly, pending the completion of the review and publication of a new statement, taxpayers requiring IRD guidance on this matter should contact their local IRD Office or seek a formal binding ruling on the particular transaction from the Rulings Unit in Wellington.

This withdrawal takes effect from the date of publication of this Taxation Information Bulletin.

## Questions we've been asked

This section of the TIB 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.

## Child support - shared custody

### Section 35, Child Support Act 1991 – Position where liable parent shares custody of child

A liable parent has written to the Commissioner concerned about the amount of child support that she must pay. She has three children who regularly stay with her, during which time she is responsible for their care. She has asked if her child support liability may be reduced, taking into account the times she has custody of the children.

Under section 35, an adjustment may be made to the calculation of child support liability under a formula assessment when there is shared custody. The calculation applies when all the following conditions are met:

- A parent has one or more qualifying children.
- The parent shares the ongoing daily care of one or more of those children substantially equally with another person.

- The parent is liable to pay child support to the other person under a formula assessment.

Under section 13(1), when another person has care of a child for at least 40 percent of the nights of the child support year in question, that other person is considered to share the ongoing daily care of a child substantially equally with the principal care provider. As such, he or she is also considered to be a custodial parent for the time the child is in his or her care and may apply for child support on that basis.

Under section 13(2), a person may be considered to share the ongoing daily care of a child substantially equally with the principal care provider, even if they do not care for the child for the minimum 40 percent of the nights. In these cases there must be other special features of the way in which the sharing of care of the child is

*continued on page 12*

from page 11

managed to amount to that care being regarded as substantially equal with the principal provider of care.

In calculating the formula assessed child support liability when there is shared care, the amount is the greater of:

- \$520; or
- An amount calculated in accordance with the following formula:

$$(A - B) \times C$$

In this formula:

- A is the liable parent's child support income for the child support year.
- B is the amount of the living allowance to which the liable parent is entitled for the child support year.
- C is the child support percentage for the liable parent.

In determining the child support percentage (C) in the case of shared custody, every child who is part of the shared custody arrangement as described above, is to be calculated as 0.5 children. In effect, the child support percentage under the formula assessment calculation in such cases is as follows:

No of children	Child support percentage
0.5	12%
1	18%
1.5	21%
2	24%
2.5	25.5%
3	27%
3.5	28.5%
4 or more	30%

A liable parent who is also considered to be a custodial parent in terms of shared custody as previously discussed, may be able to make a child support application for the time the child is in his or her care. Furthermore, that liable parent is also entitled to have that child included in his or her living allowance (B). These options may be discussed further with the local Inland Revenue Child Support office.

If both parents have applied for child support, and neither receives a benefit, the liabilities are automatically offset against each other so that the parent with the higher assessment will pay only the difference between that assessment and that of the other parent.

---

**Example**

George and Mabel have each applied for child support for their child Fred who is cared for substantially equally by each of them. Neither is a beneficiary. George's assessment is for \$6,000 a year (\$500 per month) and Mabel's is for \$4,800 per year (\$400 per month). The result of offsetting will be that George will have a liability of \$1,200 pa (\$100 per month). Mabel will have nothing to pay.

---

Generally, all of the above changes will take effect after Inland Revenue Child Support has been notified, in accordance with the Child Support Act.

The liable parent who originally asked this question had the children for more than 40% of the nights in the child support year, so her child support formula assessment was altered to reflect this. Inland Revenue also advised her that based on her circumstances, she was able to apply for child support for the time the children were in her care.

---

## Legal decisions - case notes

This section of the TIB 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'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.

## Trust taking over former Government activities – whether limited to “financial transaction” for GST purposes Chatham Islands Enterprise Trust v CIR

**Decision date:** 26 June 1998

**Act:** Goods and Services Tax Act 1985

**Keywords:** *Taxable activity, supply, grant, Crown*

### Summary

Justice Heron held that the Trust should pay GST on a sum of money paid by the Government.

### Facts

The Chatham Islands Enterprise Trust came into existence after continuing concern stretching over a number of decades about the responsibility and financial liability for essential services required by Chatham Islands residents. The concept of a local authority trading enterprise (LATE) was contemplated as taking over all of the commercial activities previously undertaken by central or local government on the Chathams.

At the heart of the plan was the injection of a capital sum which would ensure the infrastructure was retained and that the commercial operations could be developed from that point forward. It was agreed that \$8 million would be paid by the Government in two instalments together with the transfer of the assets previously owned by central government.

### Decision

The High Court held that to treat this transaction, in which two payments of \$4 million were made, as a financial transaction would be quite unreal. The Government wanted to step out of a difficult position which required supervision, expenditure and ultimate responsibility and accountability. Into its shoes stepped the Trust, which took over a multitude of responsibilities and obligations and undertook to co-ordinate and effect a replacement structure, quite different from the arrangement which preceded it. To suggest that it was confined to an injection of money only is unrealistic. Hence the payment was made for an implementation of a programme with many pieces and parts, with a variety of services, some financial but not predominately so.

As to Counsel's respective argument involving section 5(6D) it follows, given that the Court took the view that the trust was conducting a taxable activity, that the Commissioner must succeed under section 5(6D)(a). It held that there was a payment to a Trust not being a public authority in respect of that taxable activity and the subsection therefore applies. In consideration of (b) it was held that the overall purpose of the monies was for the benefit and on behalf of other persons in the form of the trading companies. The words should have their ordinary everyday meaning and plainly the payment served two purposes.

The further requirement that such activities be carried on continuously or regularly is met by the multitude of tasks to be performed and sustained by the Trust in return for the monetary consideration.

---

## Business transferred from harbour board to port company – deductions disallowed

### Auckland Harbour Board v CIR

---

**Decision date:** 30 June 1998

**Act:** Income Tax Act 1976

**Keywords:** *Legal fees, depreciation on disposal, establishment costs*

#### Summary

Justice Potter found for the Commissioner with regards to all of the six separate issues involved in this case.

#### Facts

Auckland Harbour Board (“AHB”) operated as a statutory corporation for over 100 years. It operated the Auckland Port and associated harbour services.

The port trading operations of AHB were sold to Ports of Auckland Limited (“POAL”) under the Port Companies Act 1988. AHB was abolished in 1989 when all of the shares in POAL, assets, liabilities and statutory functions were transferred to the Auckland Regional Council.

The Commissioner disallowed deductions for depreciation of assets, transfer of government and local body stock, legal fees, funding an establishment unit and included the proceeds of a land sale in AHB’s assessable income.

The six issues of the case are:

1. Legal fees: this was assessed as capital, being associated with the purchase of a tug boat.
2. Establishment costs: these were assessed as capital costs.
3. Kauri Point: this was a valuation issue.
4. Base price adjustment: this was assessed under section 64J with the application of the accrual rules.
5. Ordinary depreciation – opening book value: the objector should have claimed in the first year for purposes of calculating open written down tax book value of assets.
6. Loss on disposal: the Commissioner held that this was not due to fair wear and tear or obsolescence or uselessness. Sufficient information and explanations were not given.

#### Decision

Justice Potter found for the Commissioner in all of the issues. With regards to issue 6 her Honour found that the Commissioner could not use the so-called “Pickering” formula to calculate fair wear and tear depreciation under section 108 of the Income Tax Act 1976.

---

## Farm land subdivided and sold – whether GST taxable activity

### TRA 96/104, Decision 16/98

---

**Decision date:** 25 June 1998

**Act:** Goods and Services Tax Act 1985

**Keywords:** *Taxable activity*

#### Summary

The principles established in *Newman* and *Wakelin* can be applied in this case. Barber J also found that this case follows a similar pattern to *Case T40*.

#### Facts

The Objectors jointly purchased a number of properties between 1984 and 1987, which together made up a farm. The husband was registered for GST and farmed the property with sheep and cattle. He did not pay any rental on the farm.

In 1991, the husband claimed an input tax credit on the purchase of the farmland purchased in 1987. Inland Revenue allowed the credit despite the fact the land was in the name of both Objectors. The same year, the husband and wife began charging the husband rent for the use of the farm. They did not register for GST because the rental was under the registration threshold.

The farming operation was not a success and the Objectors decided to subdivide the property into 6 lots and sell them. All lots were sold by December 1994.

The Objectors registered for GST on 1 June 1994, having purchased another farm property. The sale of 2 lots were accounted for in the December 1994 return. The other 4 lots were sold in the GST periods ending 31 October 1993, 30 April 1994 and 30 June 1994.

#### Decision

Barber J found on the facts, the Objectors were continuously engaged in the activity of land subdivision from August 1992 to December 1994. The same essential steps of subdivision as established in the *Newman* and *Wakelin* cases occurred here. His Honour held that the subdivision and its work was extensive and of a continuing nature, therefore amounting to a taxable activity.

With regard to the input tax credit, the husband had taken an input tax credit in 1991 when the farmland asset was introduced into the partnership business, and the Objectors could not be entitled to a further input credit on that same asset.

---

## Employee status of company directors

### Roma Properties Limited v CIR

---

**Decision date:** 6 July 1998

**Act:** Income Tax Act 1976

**Keywords:** *Fringe benefit tax*

#### Summary

The Taxation Review Authority allowed the objection and the High Court disallowed it. The Taxpayer appealed to the Court of Appeal, where judgment was given in the Commissioner's favour.

#### Facts

The company sold off land and advanced the proceeds as loans to its Directors, just before FBT was put into

place. The company loans to the Directors were recorded in their current accounts. The shareholders and directors changed their status in the company and became managers of the newly-configured company. They continued to have the same duties as before.

#### Decision

Justice Richardson held that the resolutions to pay directors' fees should be taken at face value. The fees would then be subject to source deduction payments and therefore the directors were employees to whom FBT would apply.

---

## Shares issued as part of purchase – whether payment made

### TRA 91/134, Decision 17/98

---

**Decision date:** 8 July 1998

**Act:** Goods and Services Tax Act 1985

**Keyword:** *Shares issued, purchase price paid*

#### Summary

Barber J found that the Objectors should account for GST on the share component of the sale price as with the rest of the sale price.

#### Facts

The Objectors sold a partly completed commercial property. The sale and purchase agreement provided for the purchase price to be paid by deposit and subsequent monetary instalments except for a residual balance. The purchaser company was to pay the residual balance by issuing 400,000 \$1 shares in the purchaser company.

The agreement provided that the purchaser would issue the shares to the Objector on the basis that the Objectors

would enter into a "put" contract with the proprietor of the purchaser, that they would not sell the shares for under \$2 before 1 September 1988. After 1 September the Objectors could retain their shares and exercise their option to require the proprietor to purchase them at \$2 per share.

On 2 September 1988 the Objectors exercised the option but never received payment due to the proprietor going bankrupt.

#### Decision

Barber J accepted that the Objectors did not actually recover the residual amount of \$800,000 in cash but that this was due to a failure to on-sell the shares by which the Objector had been paid \$800,000 as part of the purchase price. His Honour found that the issue of the shares after the signing of the agreement constituted an absolute discharge of the purchaser's obligation for the payment of \$800,000 under the sale and purchase agreement.

---

---

## Due dates reminder

---

### August 1998

- 5 Large employers: PAYE deductions and deduction schedules for period ended 31 July 1998 due.
- 7 Provisional tax and/or Student Loan interim repayments: first 1999 instalment due for taxpayers with April balance dates.  
Second 1999 instalment due for taxpayers with December balance dates.  
Third 1998 instalment due for taxpayers with August balance dates.  
1998 income tax returns due to be filed for all non-IR 5 taxpayers with April balance dates.
- 20 Large employers: PAYE deductions and deduction schedules for period ended 15 August 1998 due.  
Small employers: PAYE deductions and deduction schedules for period ended 31 July 1998 due.  
Gaming machine duty return and payment for month ended 31 July 1998 due.  
RWT on interest deducted during July 1998 due for monthly payers.  
RWT on dividends deducted during July 1998 due.  
Non-resident withholding tax (or approved issuer levy) deducted during July 1998 due.
- 31 GST return and payment for period ended 31 July 1998 due.

### September 1998

- 5 Large employers: PAYE deductions and deduction schedules for period ended 31 August 1998 due.  
*(We will accept payments received or posted on Monday 7 September as in time for Saturday 5 September.)*

- 7 Provisional tax and/or Student Loan interim repayments: first 1999 instalment due for taxpayers with May balance dates.  
Second 1999 instalment due for taxpayers with January balance dates.  
Third 1998 instalment due for taxpayers with September balance dates.  
1998 end of year payments due (income tax, Student Loans, ACC premiums) for taxpayers with October balance dates.  
1998 income tax returns due to be filed for all non-IR 5 taxpayers with May balance dates.  
QCET payment due for companies with October balance dates, if election is to be effective from the 1999 year.
- 20 Large employers: PAYE deductions and deduction schedules for period ended 15 September 1998 due.  
Small employers: PAYE deductions and deduction schedules for period ended 31 August 1998 due.  
Gaming machine duty return and payment for month ended 31 August 1998 due.  
RWT on interest deducted during August 1998 due for monthly payers.  
RWT on dividends deducted during August 1998 due.  
Non-resident withholding tax (or approved issuer levy) deducted during August 1998 due.  
*(We will accept payments received or posted on Monday 21 September as in time for Sunday 20 September.)*
- 30 GST return and payment for period ended 31 August 1998 due.  
Non-resident Student Loan repayments - second 1999 instalment due.



## Public binding rulings and interpretation statements: your chance to comment before we finalise them

This page shows the draft public binding rulings and interpretation statements that we now have available for your review. You can get a copy and give us your comments in three ways:

**By post:** Tick the drafts you want below, fill in your name and address, and return this page to the address below. We'll send you the drafts by return post. Please send any comments *in writing, to the address below*. We don't have facilities to deal with your comments by phone or at our local offices.

**From our main offices:** Pick up a copy from the counter at our office in Takapuna, Manukau, Hamilton, Wellington, Christchurch or Dunedin. You'll need to post your comments back to the address below; we don't have facilities to deal with them by phone or at our local offices.

**On the Internet:** Visit our website at <http://www.ird.govt.nz/rulings/> Under the "Adjudication & Rulings" heading, click on "Draft Rulings", then under the "Consultation Process" heading, click on the drafts that interest you. You can return your comments via the Internet.

Name \_\_\_\_\_  
 Address \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_

✓ **Public Binding Rulings**

**Comment Deadline**

**2915:** Easements – deductibility of the costs of preparation, stamping, and registration

31 August 1998

✓ **Interpretation statements**

**Comment Deadline**

**3817:** "Owned" and "acquired" – their meaning for depreciation purposes

31 August 1998

*We must receive your comments by the deadline shown if we are to take them into account in the finalised item*



**No envelope needed - simply fold, tape shut, stamp and post.**

Affix  
Stamp  
Here

The Manager (Field Liaison)  
 Adjudication & Rulings  
 National Office  
 Inland Revenue Department  
 P O Box 2198  
 WELLINGTON



