TAX INFORMATION BULLETIN

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Contents

New Legislation

Child Support Amendment Act 1999 3

Binding rulings

New application forms for binding rulings 9

Changes to binding rulings regulations 9

Draft public ruling PU3801: Guarantee fees paid by a New Zealand company to an overseas associated company 10

Public ruling – BR Pub 99/4 Land sales – whether income tax exemptions for farm land apply to non-natural persons 10

Public ruling – BR Pub 99/5 Frequent flyer schemes promoted by credit card companies – fringe benefit tax liability 12

Product ruling – BR Prd 99/5 16

Product ruling – BR Prd 99/6 18

Product ruling – BR Prd 99/7 20

Product ruling – BR Prd 99/8 22

Legal decisions – case notes

GST – whether input credit available on sale and subdivision of land acquired in 1984 26

Deduction in respect of loss set-off – whether interest losses cancelled as a result of liquidation; whether Commissioner able to alter assessment 27

Awards for costs in tax cases 28

Whether objector was resident of NZ for the purposes of taxation of income 29

Standard Practice Statements

Payment of debt by compulsory deductions from bank accounts 30

Questions we've been asked

Tax Administration Act 1994 – specific rates of interest/additional tax for tax in dispute 32

Matters of interest

GST and Bloodstock destined for export 33

Regular features

Due dates reminder 34

Public binding rulings and interpretation statements: your chance to comment before we finalise them 35

This TIB has no appendix

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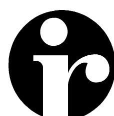

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NEW LEGISLATION

The Child Support Amendment Act 1999 (99/1) was introduced into Parliament on 24 November 1998 as the Child Support Amendment Bill (No 5).

CHILD SUPPORT AMENDMENT ACT 1999

Introduction

The amendments to the Child Support Act 1991 are the result of a recent review of the child support scheme to improve its efficiency. They:

- Allow greater discretion to write off penalties.
- Close the gap between the year in which income is earned and the year of assessment for most liable parents.
- Reduce the opportunities for abuse of the estimations provisions.
- Remove the inequities in the exemption provisions and ensure that the law reflects the original intent of these provisions.
- Allow overseas taxable income to be included in liable parents' child support assessments.
- Introduce a number of other administrative measures that will allow greater flexibility in the administration of the child support scheme.

Background

Inland Revenue administers the child support scheme, set up in 1992. Nearly 700,000 people – including children, custodians and liable parents – are directly affected by the workings of the scheme.[1]

The amendments are intended to improve the overall administrative efficiency of the child support scheme. Most are the result of a recent review of the administration of the scheme. Many of them take up, and in some cases build upon, a number of the recommendations of the Child Support Review 1994 Working Party.

The original proposals relating to the year of assessment, as contained in the bill at introduction, were changed by the Social Services Committee so that the gap between the end of the income year and the beginning of the child support year could be closed completely.

As a result of that, and because of the delayed enactment, several application dates were also changed from those originally proposed in the bill.

The select committee also took the opportunity to include in the bill two minor drafting changes.

Write-off penalties

New sections 135A and 135B

When payments of child support are late, an initial penalty of 10% (or a minimum of $5) of the unpaid amount is imposed, with an additional 2% on the outstanding balance (including penalties) every subsequent month. Inland Revenue has been able to write off these penalties only in very limited circumstances.

Under this system, some new liable parents incurred significant debts before they had an opportunity to establish regular payment arrangements, while others were penalised for a small failure in situations beyond their control.

Key changes

The changes are expected to encourage voluntary compliance with the child support law by giving Inland Revenue greater flexibility to write off penalties, particularly when the liability first arises.

The new section 135A requires that penalties be written off in two situations:

- When liable parents keep to debt repayment arrangements they entered into within three months of when the assessment for their first payment was issued.
- When an initial penalty is greater than the arrears to which it relates and the liable parent has no history of late payments.

[1] "Custodian" may include a person entitled to receive spousal maintenance, "child support" may include spousal maintenance, and "liable parent" may include a person who is required to pay spousal maintenance. Spousal maintenance is a payment between two parties that may be awarded by the courts or arranged by private agreement, for the benefit of the recipient rather than his or her children. A person does not have to have children to receive spousal maintenance, and someone with children may receive both spousal maintenance and child support.

The new section 135B allows Inland Revenue to exercise discretion in considering whether part or all of a penalty should be written off when:

- The liable parent had reasonable cause for the delay in payment, and took corrective action as soon as possible. "Reasonable cause" is defined to mean an event or circumstance that is beyond the control of the liable parent, including a serious illness, accident or disaster, and that caused a reasonable delay in the payment.
- In failing to pay on time, the liable parent had acted in good faith on the advice of an Inland Revenue officer, and that advice proved to be incorrect.
- The delay in payment was due to an honest oversight by a liable parent who has no history of previous late payment and who paid the debt as soon as he or she became aware of the oversight.
- The custodian has taken over responsibility for collecting the child support debt and it would be unfair or unreasonable to enforce collection of the remaining penalty.

The discretionary changes recognise that late payments are not always entirely within the control of a liable parent. If the conditions for write-off are met and the penalty has already been paid, that amount will be refunded. Inland Revenue will publish guidelines to ensure consistent application of the new provisions.

Application date

These amendments apply from 24 July 1999.

Income year of assessment

Sections 2, 29, 30, (new) 38A, 39, 106, 235, 236.

Child support is based on income earned by liable parents two years earlier because that is currently the most recent income information available to Inland Revenue when the assessment is made.

Under the tax simplification initiatives contained in the Taxation (Simplification and Other Remedial Matters) Act 1998, Inland Revenue will receive information on the salary and wages paid to employees from employers each month. This will make it possible to calculate child support assessments on recent income, instead of waiting until after end-of-year tax returns have been filed.

Key changes

The changes are designed to achieve a closer match between the income on which an assessment is based and the current ability of a liable parent to provide financial support.

From 1 April 2001, child support assessments of liable parents who are employees or beneficiaries will be based on their income for the year immediately preceding the child support year.[2] However, child support assessments must be issued in the preceding February to allow liable parents time to exercise their right to object to assessments. As only 10 months of income information will be available in February, the income for those 10 months will be grossed up to provide an annual income amount. There will be no need for an inflation factor to be applied to these incomes, so the existing provision for an inflation factor has been repealed.

The following table compares the existing and new processes.

	Current system	Effective 1 April 2001
Income year on which assessment based	1April 1999 – 31 March 2000	1 April 2000 – 31 March 2001
Income base	Actual income (CY-2)	Partially estimated income (CY-1)
Child support year (Current year)[3]	1 April 2001 – 31 March 2002	1 April 2001 – 31 March 2002
Gap between end of income year and beginning of child support year	12 months	No gap

When the full annual income amounts are known they will be compared against the amounts used in the child support assessments. If the final taxable income amount is at least $500 more or less than the estimated taxable income, Inland Revenue will reassess the liability.

Other liable parents will continue to have their child support assessments based on their income of two years earlier. An inflation factor will be added to their incomes to bring them into line, as closely as possible, with those whose assessments are based on the previous year's income. This inflation factor will be based on the average of headline inflation determined by the Consumer Price Index over the year ending on 31 December before the start of the child support year.

[2] This will affect approximately 75 percent of liable parents.

[3] "Current year" is the year in which child support is assessed and payable; CY-1 is the current year minus one; CY-2 is the current year minus two.

Application date

These amendments will take effect from 1 April 2001.

Estimation of income

Sections 40, 41, 42, 43, 44, (new) 44A, 45, 46, 90, 235, 237, (new) 151A.

The rules on estimating income were designed to recognise that income earned two years earlier is not always a good indicator of current capacity to pay child support. These rules give relief to liable parents whose income has fallen by at least 15 percent from that on which their assessment is based. When this occurs they may ask for a new assessment based on an estimate of their income.

However, the complexity of the procedures created difficulties for liable parents, custodians and the administration of the scheme. Particular problems identified were:

- Some liable parents who estimated their income part way through the year had already paid sufficient to cover their estimated liability for the full year. Despite this, they were still required to pay the minimum amount of $10 per week. This could result in custodians receiving too much child support, which had to be recovered.
- When liable parents chose to estimate their income, a reconciliation based on their income tax returns at the end of the year compared their estimate against their actual income in that year. Even if they revoked the estimation their finalised liability was based on their actual income in that year, which could mean they had to pay more or less than they would have had they not estimated.
- Some liable parents had taken advantage of the estimation provisions by not filing a tax return at the end of the year, which meant that a reconciliation could not be carried out.

The law also allowed for use of money interest to be charged when child support is underpaid, in recognition of the monetary benefit gained by a liable parent through having the use of unpaid child support. Although this was intended to create an incentive to file tax returns, return filing is now partially enforced through the introduction of the late filing fee. The failure of liable parents who have estimated their income to file returns is also addressed through new measures in the amendment Act.

Key changes

When liable parents who have estimated their income do not file end-of-year tax returns to enable an end-of-year reconciliation, Inland Revenue will now be able to issue a reconciliation assessment for the amount that the liable parents would have been required to pay had they not estimated their income. Liable parents will be able to object to this reconciliation by filing a tax return for that income year within 28 days of receiving notification of the assessment. If they do not file a return within this period, the reconciliation stands. They will also be prevented from estimating again until they have filed their outstanding tax return(s). (Application date 24 July 1999)

To ensure that liable parents who estimate their income and do file their income tax returns are not disadvantaged, all liable parents will have their liability capped at the amount they would have had to pay had they not estimated their income. (Application date 1 April 2000)

Example 1

A liable parent is assessed on income of $60,000. She estimates her current year income will be $50,000 and her liability is reassessed. Her actual income for the year is $62,000. Her reconciliation assessment will be based on income of $60,000.

Liable parents who, at the time they estimate, have already paid their liability for the full year based on their estimated income will not have to continue paying the minimum amount of $10 per week. This may lead to some custodians having to go on a social welfare benefit for the rest of the year. If that happens the State will waive its entitlement to retain any child support for that period so that the custodian does not incur a child support debt. (Application date 1 April 2000)

Example 2

A single liable parent pays child support for 3 months based on income of $36,000 a year.

He becomes unemployed and estimates his income for the year at $15,000.

His liability is reduced to the minimum and he has already paid more than that, so is required to pay nothing for the rest of the child support year.

The custodian goes onto a social welfare as a result of losing child support.

When the reconciliation assessment is carried out the custodian may incur a debt for the period she was on the benefit, but the debt can be written off.

When liable parents revoke their estimation, or no longer meet the threshold for estimating income, their child support liability will revert to what would have been payable had they not estimated; they will be required to pay the full amount, and there will be no end of year reconciliation. (Application date 1 April 2000)

Although liable parents are still required to make their election to estimate in writing, they no longer have to do so on an "approved form". However, they will be required to provide documentary evidence to support their estimation. (Application date 24 July 1999)

The provisions for use of money interest have been repealed from the child support year beginning 1 April 1999. However, the change is not retrospective in effect because use of money interest is not applied until after the end of the child support year.

Application dates

Some of the changes can apply immediately, while others must apply from the beginning of the next child support year. The rest are timed to coincide with the changes in the year of assessment, 2001.

Exemptions for long-term prisoners and hospital patients

Sections 73, 74, 75

Some long-term prison inmates and hospital patients are exempted from paying child support in recognition of their limited opportunity to earn income. However, in the past they generally qualified only if they were in prison or hospital for the full child support year; they did not receive it for part years.

The exemption was not available to patients in private hospitals or people in residential care. Nor was it available to patients in public hospitals who were social welfare beneficiaries, even though the combination of the reduced benefit and automatic child support deduction left them with only $17.08 a week from which to meet all their personal needs.

To qualify for the exemption, liable parents had to have no income for the child support year or, if their income was solely from investments, it could not exceed $520 gross. This meant that liable parents could be required to pay a full year's child support even if they were released from hospital or prison in the last few weeks of the child support year and their only income after release was a social welfare benefit.

Key changes

Exemptions from child support liability are now available for the liable parent's full period of imprisonment or hospitalisation if longer than 13 weeks, and he or she meets the income criteria. The income will be calculated on a weekly basis for periods of more than 13 weeks but less than a full child support year.

The exemptions have also been extended to include long-term hospital patients whose sole income is a reduced social welfare benefit and those who are in private hospitals and residential care institutions.

Liable parents who are granted an exemption from child support will no longer need to reapply at the beginning of each new child support year.

Application date

These amendments apply from 24 July 1999.

Notice of assessment

Sections 88,136

Section 88 specified what had to appear in a notice of assessment, even though the content was not always appropriate or necessary. The section also required a notice of assessment to be issued every time a parent's income was reassessed, even if there was no change in the amount payable. This meant liable parents sometimes received notices that contained no new information.

Key changes

The content of notices of assessment can now be varied to suit the particular circumstances to which they relate, and to omit unnecessary or irrelevant information.

Liable parents will continue to receive at least one notice of assessment for each child support year in which they have a liability, but they will receive subsequent notices in that year only if the amount to be paid changes.

A previous oversight has been corrected so that notices of assessment will include the right to apply for an administrative determination when liable parents believe they have grounds for departure from the formula assessment.

Application date

These amendments apply from 24 July 1999.

Refunds

Section 216

The requirement that applications for refunds be in writing delayed those refunds and created unnecessary double handling and paperwork.

A number of credits or overpayments are held on Inland Revenue's child support database.

Key changes

Requests for refunds can now be made verbally or in writing. This is consistent with Inland Revenue's general policy to encourage greater use of the telephone in contacts with the department.

When Inland Revenue is satisfied that the liable parent is not in arrears and has no known future liability, it will be able to refund excess child support without a prior application. If the available final credit is less than $5 and no request for a refund has been received after 12 months from when that credit arose, it will be transferred to the liable parent's tax account.

Application date

The amendment applies from 24 July 1999.

Deductions of child support from wages and salaries

Sections 165,166

Liable parents may have more than one source of income. For example, they may hold down two jobs, or work part-time and receive a social welfare benefit. In the past, even though they may have preferred to have a single deduction for child support, they may have been required to have deductions from more than one source.

The child support law protects liable parents from unreasonable deductions by providing that deductions cannot reduce salary and wages by more than 40 percent. The original legislation required this amount to be calculated on a weekly basis, although administrative practice allowed employers to calculate the maximum deduction according to the pay period under which they operated.

Key changes

Liable parents can now choose to have the whole child support amount taken from only one income source. The maximum deduction from all sources is not to exceed 40 percent of their total after-tax income.

Another amendment allows employers to make child support deductions according to the pay period they operate under, whether fortnightly or monthly, and is a compliance cost saving measure for them. The change makes the legislation consistent with existing practice.

Application date

The amendments apply from 24 July 1999.

"Uplift" of debt and future entitlement

Section 180

When child support and/or spousal maintenance is in arrears, non-beneficiary custodians can take responsibility for collection (uplifting the debt) themselves. Under the previous legislation, however, custodians who withdrew from the scheme had to wait until the final amount of entitlement was in arrears before they could uplift that debt.

The state retains child support received for beneficiary custodians, although they are entitled to receive any spousal maintenance payments. Under the previous legislation, however, they were unable to take over responsibility for collecting spousal maintenance in arrears, a problem that arose because the provisions used the term "financial support", which included "spousal maintenance". The intention of the legislation was to prevent beneficiary custodians from uplifting their child support, which is retained by the state, but the wording had the effect of also preventing the uplift of spousal maintenance.

Key changes

Non-beneficiary custodians who choose to withdraw from the child support scheme but are entitled to a final payment of child support and/or spousal maintenance for the period up to the date they withdraw, can now take responsibility for collection of that final amount themselves. They do not need to wait until it becomes a debt.

Beneficiary custodians who are entitled to spousal maintenance can now take over responsibility for collecting both past debts and future entitlement.

These will be voluntary choices.

Application date

The amendments apply from 24 July 1999.

Custodians' bank accounts

Sections 14, 55, 148

An application for child support must be "properly made". Under the previous legislation this included providing details of the custodian's bank account. These details are not essential to begin processing a child support application, however, particularly when the custodian is a social welfare beneficiary. Delaying the acceptance of an application delayed the start date of entitlement and deprived either non-beneficiary custodians or the state of revenue.

The requirement that a bank account had to be in the custodian's name was intended to ensure that payment went to the sole or principal provider of continuing daily care for the child(ren), but in practice proved to be too inflexible.

Key changes

Processing an application will not be delayed because a custodian has not given Inland Revenue details of his or her bank account. This will eliminate unnecessary delay in the start of child support. However, because it is administratively efficient for payments to be direct credited to a bank account, custodians will still be required to provide account details before any payments can be made.

Custodians who wish to have their child support paid to an account in, say, their child's name, or an account held by a budget advisor, can now choose to do so.

Application date

The amendments apply from 24 July 1999.

Overseas taxable income

New section 39A

Child support is based on past income that is taxable in New Zealand. Under the previous legislation, this meant that liable parents who left New Zealand, and ceased to be resident for income tax purposes, could be assessed under the child support formula for only the minimum amount of $520 a year once their income year did not contain income taxable in New Zealand. As a result, the amount of child support payable often bore no relation to the capacity of the liable parent to contribute to the support of his or her children.

Key changes

Inland Revenue now has the discretion to include income that is taxable outside New Zealand in the child support assessment base when a liable parent is not resident in New Zealand for income tax purposes. (Any overseas income should already be included in the parent's tax return if he or she is resident in New Zealand for income tax purposes.) This will ensure that assessments more accurately reflect that parent's ability to pay child support.

This new provision will be used mainly when a liable parent is resident in a country that has entered into a reciprocal agreement with New Zealand for the collection of child support.

Application date

The amendment applies from 24 July 1999.

Reciprocal agreement with Australia

New 219A of the Child Support Act 1991
Section 2 of the Family Proceedings Act 1980

The amendments are in anticipation of the reciprocal agreement for the collection of child support and spousal maintenance being entered into with Australia. This required a small change to the Child Support Act, although the agreement itself will be given effect in New Zealand by an Order in Council.

Key changes

When the Australian authorities collect child support and remit it to New Zealand, any annual debits arising from exchange fluctuations of up to $20 can be written off.

The Family Proceedings Act 1980 has also been amended so that, once the agreement comes into effect, people residing in New Zealand or Australia will not be able to seek maintenance using the United Nations Convention for the Recovery of Maintenance Abroad. This is to prevent dual liabilities arising.

Application date

The amendment to the Family Proceedings Act 1980 will be given effect by the Order in Council that gives effect to the reciprocal agreement. The small debit write-off provision applies from 24 July 1999.

Remedial amendments

Section 208

The reference to "child support" in section 208(a) has been changed to "financial support" because "financial support" is inclusive of both child support and spousal maintenance. This applies from 24 July 1999.

Section 30

The cross-references to the Income Tax Act 1994 in the definition of "living allowance" in section 30(4) have been changed to reflect changes in the Taxation (Parental Tax Credit) Act 1999. This change will apply from 1 October 1999.

BINDING RULINGS

This section of the TIB contains binding rulings that the Commissioner of Inland Revenue has issued recently.

The Commissioner can issue binding rulings in certain situations. Inland Revenue is bound to follow such a ruling if a taxpayer to whom the ruling applies calculates tax liability based on it.

For full details of how binding rulings work, see our information booklet "Binding Rulings" (IR 115G) or the article on page 1 of TIB Volume Six, No.12 (May 1995) or Volume Seven, No.2 (August 1995). You can order these publications free of charge from any Inland Revenue office.

NEW APPLICATION FORMS FOR BINDING RULINGS

Recent changes to the binding rulings regime, brought about by the enactment of the Taxation (Accrual Rules and Other Remedial Matters) Act 1999 and the gazetting of the Tax Administration (Binding Rulings) Regulations 1999, have necessitated changes to:

- The application for private ruling form - formerly IR113, now IR713
- The application for product ruling form - formerly IR114, now IR714

and brought about the introduction of:

- The application for status ruling form - IR712.

The new forms take into account the fees applicable to binding ruling applications received on and from 26 August 1999, i.e. application fee $310, hourly rate thereafter $155 - both GST inclusive.

Additionally, the forms and their respective information sheets have been combined and condensed, and generally brought up to date.

These forms are available by:

- Phoning the number for "Forms and Brochures" under "Inland Revenue" in the Blue Pages(tm) Government Section of your local telephone directory
- Contacting the Adjudication & Rulings business group - telephone (04) 4747175 or e-mail to: rulings@ird.govt.nz

Please do not use forms IR113 and IR114 after 26 August 1999.

Our booklet "A Guide to Binding Rulings" is being updated, and we will advise the date of its release shortly.

CHANGES TO BINDING RULINGS REGULATIONS

Tax Administration (Binding Rulings) Regulations 1999

The Tax Administration (Binding Rulings) Regulations 1995 have been amended as follows:

- Status rulings are to be specifically included in the regulations to allow Inland Revenue to charge for this type of ruling.
- The hourly fee charged for private, product and status rulings is to be increased from $105 to $155 for applications received after the amended regulations come into force.
- The application fee charged for private, product and status ruling is to be increased from $210 to $310.

A recent legislative review of the binding rulings system identified a number of deficiencies in the system. The resulting changes, some of a policy nature and others of a minor technical nature, were enacted through the Taxation (Accrual Rules and Other Remedial Matters) Act in May 1999. (See TIB Vol 11, No.6)

The amended regulations come into force on 26 August 1999, the 28th day after the date they were published in the Gazette (29 July 1999).

DRAFT PUBLIC RULING PU3801: GUARANTEE FEES PAID BY A NEW ZEALAND COMPANY TO AN OVERSEAS ASSOCIATED COMPANY

In TIB Volume Eleven, No. 6 of July 1999 at page 33, dealing with legislative amendments in the Taxation

(Accrual Rules and Other Remedial Matters) Act 1999, it was noted that section CN4 and associated definitions in section OB1 have been changed to clarify the position on guarantee fees paid to non-residents.

Because of this legislative clarification, the Rulings Unit does not intend to publish its proposed item, "Guarantee fees paid by a New Zealand company to an overseas associated company", whose exposure draft was advertised as being available for public comment in TIB Volume Ten, No. 9 of September 1998.

LAND SALES – WHETHER INCOME TAX EXEMPTIONS FOR FARM LAND APPLY TO NON-NATURAL PERSONS

PUBLIC RULING - BR Pub 99/4

Note (not part of ruling): This ruling is essentially the same as public ruling BR Pub 96/8, published in TIB Volume Seven, No.13, May 1996, but the period of application is from 1 June 1999 to 31 May 2004 and some minor wording and formatting changes have been made. BR Pub 96/8 applied up until 31 May 1999.

This is a public ruling made under section 91D of the Tax Administration Act 1994.

Taxation Laws

All legislative references are to the Income Tax Act 1994 unless otherwise stated.

This Ruling applies in respect of section CD 1(4)(a)(i) and section CD 1(7)(a).

The Arrangement to which this Ruling applies

The Arrangement is the sale or other disposition of land by a non-natural person where the land had been acquired or used for the purposes of a farming or agricultural business carried on by that person and where the sale or disposition would otherwise be subject to section CD 1(2)(e), (f) or (g).

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

- The words "the taxpayer's spouse" in section CD 1(4)(a)(i) and section CD 1(7)(a) do not restrict the meaning of "taxpayer" to natural persons. "Taxpayer" in section CD 1(4)(a)(i) and section CD 1(7)(a) includes non-natural persons such as companies and trusts. Accordingly, the exemptions provided by section CD 1(4)(a)(i) and section CD 1(7)(a) apply to a taxpayer that is a non-natural person if the other requirements of the exemptions are met.

The period for which this Ruling applies

This Ruling will apply for the period 1 June 1999 to 31 May 2004.

This Ruling is signed by me on the 14th day of July 1999.

Martin Smith
General Manager (Adjudication & Rulings)

COMMENTARY ON PUBLIC RULING BR Pub 99/4

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusions reached in public ruling BR Pub 99/4 ("the Ruling").

Background

Amounts derived from certain sales or other dispositions of land that would otherwise be gross income under section CD 1(2), are subject to a number of exemptions.

This Ruling considers whether the exemptions contained in section CD 1(4)(a)(i) and section CD 1(7)(a), that are available in respect of sales of farm or agricultural land in certain circumstances, apply where the taxpayer disposing of the land is not a natural person.

Legislation

Section CD 1(4) states:

Subsection (2)(e) shall not apply to any amount derived from the sale or other disposition of any land in any case where the Commissioner is satisfied that-

(a) The land was acquired by the taxpayer, and used or intended to be used-

(i) By the taxpayer, or by the taxpayer's spouse, or by both of them, primarily and principally for the purposes of a farming or agricultural business carried on by the taxpayer, or the taxpayer's spouse, or both of them; or

....

Section CD 1(7) states:

Subsection (2)(f) and (g) shall not apply to any amount derived from the sale or other disposition of any land in any case where-

(a) That land is a lot resulting from the division into 2 or more lots of a larger area of land which, immediately before that division, was occupied or used by the taxpayer, or by the taxpayer's spouse, or by both of them, primarily and principally for the purposes of a farming or agricultural business carried on by the taxpayer, or the taxpayer's spouse, or both of them;and.

....

Application of the Legislation

The ordinary meaning of the words "by the taxpayer, or by the taxpayer's spouse, or by both of them" in section CD 1(4)(a)(i) and section CD 1(7)(a) does not require the taxpayer to be a natural person. On a literal interpretation, by considering each alternative in section CD 1(4)(a) separately, a non-natural person taxpayer, e.g. a company, could clearly come within the words: "The land was acquired by the *taxpayer*, and used ... by the *taxpayer*... principally for the purposes of a farming or agricultural business carried on by the *taxpayer*".

Alternatively however, it is possible for the reference to the "taxpayer's spouse" to be interpreted as colouring the word "taxpayer" and limiting its meaning to natural persons.

It is the Commissioner's view that the words are to be given their ordinary meaning, and that "taxpayer" as used in the exemptions is not restricted to natural persons. This interpretation is supported by the legislative history of the exemptions. Prior to 1983, the exemptions only referred to "taxpayer", and it was clear that a company or other non-natural persons could come within the exemptions. In 1983, the exemptions were amended to include taxpayers' spouses. The intention at that stage was to extend the exemptions, rather than to narrow them to natural persons.

FREQUENT FLYER SCHEMES PROMOTED BY CREDIT CARD COMPANIES – FRINGE BENEFIT TAX LIABILITY

PUBLIC RULING - BR Pub 99/5

This is a public ruling made under section 91D of the Tax Administration Act 1994.

Taxation Laws

All legislative references are to the Income Tax Act 1994 unless otherwise stated. This Ruling applies in respect of section CI 2(1) and the definition of "arrangement" in section OB 1.

The Arrangement to which this Ruling applies

The Arrangement is the receipt of benefits under a "frequent flyer scheme" (FFS) by an employee through the use of a credit card supplied by an employer to the employee of the employer.

The features of the FFS are:

- The employees of the employer hold corporate credit cards.
- The employees use the credit cards for the purchase of goods and services. Depending on the policy of the employer, the purchases may be in respect of employment related expenditure or private expenditure, or both.
- The goods and services purchased by the employees may include airfares arising from employment related travel.
- The employer is not involved in negotiations or discussions with the credit card company as to the amount or level of benefits under the FFS provided to employees. The employer does no more than give permission or consent for employees to join the scheme.
- The employees of the employer join the credit card company's FFS as individual members.
- As members of the FFS, employees accumulate points in respect of goods and services purchased with their corporate credit cards. The employees can exchange the accumulated points for goods and services, including free or discounted air travel, with the credit card company or any other person nominated by the credit card company.

This Ruling will not apply if the employer is the credit card company providing the benefits under the FFS to its own employees.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

- For the purposes of the FBT rules (as defined in section OZ 1(1)), section CI 2(1) will not apply to the entitlement of benefits received by the employees of the employers under the FFS.

The period for which this Ruling applies

This Ruling will apply for the period from 26 July 1999 until 31 July 2002

This Ruling is signed by me on the 26th of July 1999

Martin Smith
General Manager (Adjudication & Rulings)

COMMENTARY ON PUBLIC RULING BR Pub 99/5

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusions reached in Public Ruling BR Pub 99/5 ("the Ruling").

Background

The subject matter covered in the Ruling was previously dealt with in Public Ruling BR Pub 95/6 (*Tax Information Bulletin* Volume Seven, No. 5, November 1995 at page 7 under the heading *"Tax treatment of credit card companies' frequent flyer schemes"*). Some formatting changes have been made, and the commentary to the Ruling has been modified to provide further clarification.

The Ruling sets out the tax treatment of frequent flyer schemes promoted by credit card companies. This Ruling will not apply where the employer is the credit card company providing the benefits under the FFS to its own employees.

A policy statement dealing with the tax treatment of FFS promoted by airline companies appeared in *Tax Information Bulletin* Volume Five, No. 6, November 1993 at page 2.

Legislation

Section CI 1 states:

In the FBT rules, "fringe benefit", in relation to an employee and to any quarter or (where fringe benefit tax is payable on an income year basis under section ND 4) income year, means any benefit that consists of -

...

(h) Any benefit of any other kind whatever, received or enjoyed by the employee in the quarter or (where fringe benefit tax is payable on an income year basis under section ND 4) income year, -

being, as the case may be, private use or enjoyment, availability for private use or enjoyment, ... or a benefit that is used, enjoyed, or received, whether directly or indirectly, in relation to, in the course of, or by virtue of the employment of the employee ... and which is provided or granted by the employer of the employee;...

Section CI 2(1) states:

For the purposes of the FBT rules, where a benefit is provided for or granted to an employee by a person with whom the employer of the employee has entered into an arrangement for that benefit to be so provided or granted, that benefit shall be deemed to be a benefit provided for or granted to the employee by the employer of the employee.

"Arrangement" is defined in section OB 1 to mean, unless the context otherwise requires:

...any contract, agreement, plan, or understanding (whether enforceable or unenforceable), including all steps and transactions by which it is carried into effect:

Application of the Legislation

Liability for FBT

Under section CI 1, an employer is liable to pay FBT on fringe benefits provided or granted to an employee by the employer. This is not an issue in the Ruling, because the employer is not the person providing the benefit to the employee.

However, under section CI 2(1) an employer can be liable for FBT if the employer enters into an arrangement with another person for the provision of fringe benefits to the employer's employees.

Section CI 2(1) is an anti-avoidance provision. For it to have any application there must be **an arrangement** between the employer and the other party (the provider of the benefit), and that arrangement must provide for or grant a benefit to the employee of the employer entering into the arrangement.

Members of a credit card company's FFS

Some credit card companies give all cardholders the opportunity to join their FFS. These schemes allow cardholders to accumulate points on the scheme as they charge goods and services to their credit cards. These goods and services may be employment related or may be private in nature. Subject to certain conditions (which vary from scheme to scheme), the cardholders can transfer the points to a participating airline FFS. The cardholder can then exchange the points for discounted or free travel or goods or services, depending on the terms of the particular airline FFS.

There will be no FBT liability for the entitlements received if an employee is an individual card holder, even though the employee may charge employment related expenditure to the card that is later reimbursed by the employer. In these instances there is no arrangement between the employer and the FFS provider.

Employees holding corporate credit cards

If the employee holds a corporate credit card and is able to charge private as well as employment related expenditure to the card, the question of whether the corporate employer is subject to FBT will depend on whether there is an arrangement between the employer and the credit card company. Where such an arrangement exists, and the arrangement between the provider and the employer is for the granting of benefits to the employee, the employer will be liable to FBT on the value of those benefits received by the employee.

Where the entitlement arises as a result of both employment related and private expenditure, some adjustment will be necessary to eliminate the portion of benefits arising from the private expenditure.

Is there an arrangement?

There have been a substantial number of cases in which the courts have considered the application and meaning of the definition of "arrangement". Briefly, the major cases are:

The High Court of Australia in *Bell v Federal Commissioner of Taxation* 87 CLR 548 considered that an arrangement:

> ...extends beyond contracts and agreements so as to embrace all kinds of concerted action by which persons may arrange their affairs for a particular purpose or so as to produce a particular effect.

The Privy Council in *Newton and others v Commissioner of Taxation of the Commonwealth of Australia* [1958] 2 All ER 759 took a similar line when it concluded that:

> The word arrangement is apt to describe something less than a binding contract or agreement, something in the nature of an understanding between two or more persons - a plan arranged between them which may not be enforceable at law. But it must in this section comprehend, not only the initial plan but also the transactions by which it is carried into effect - all the transactions that is which have the effect of avoiding taxation, be they conveyances, transfers, or anything else.

This passage was quoted and approved by Eichelbaum J in the High Court decision in *Hadlee and Sydney Bridge Nominees Ltd v CIR* (1989) 11 NZTC 6,155. The Court of Appeal subsequently approved this.

The Privy Council considered the meaning of arrangement in the context of the New Zealand Apple and Pear Marketing Act 1971 in *New Zealand Apple and Pear Marketing Board v Apple Fields Ltd* [1991] 1 NZLR 257. It concluded that:

> Arrangement is a perfectly ordinary English word and in the context of section 27 involves no more than a meeting of minds between two or more persons, not amounting to a formal contract, but leading to an agreed course of action.

The English Court of Appeal in *Re British Basic Slag Ltd's Agreements* [1963] 2 All ER 807 considered the ordinary meaning of arrangement. It concluded:

> Though it may not be easy to put into words, everybody knows what is meant by an arrangement between two or more parties. If the arrangement is intended to be enforceable by legal proceedings, as in the case where it is made for good consideration it may no doubt be properly described as an agreement. But the statute clearly contemplates that there may be arrangements which are not enforceable by legal proceedings, but which create only moral obligations or obligations binding in honour..... When each of two or more parties intentionally arouses in the others expectation that he will act in a certain way, it seems to me that he incurs at least a moral obligation to do so.
>
> An arrangement is so defined is therefore something whereby the parties to it accept mutual rights and obligations.

In *Trade Practices Commission v Email Ltd* 31 ALR 53, the Court considered whether an arrangement could exist when there was a commitment by one party only. It concluded that it would be rare that an arrangement could exist without reciprocity of commitment from the parties to achieve a commercial objective beneficial to each party.

To summarise, the courts have identified the following characteristics that indicate the existence of an arrangement:

- A meeting of minds on an agreed course of action for a particular purpose (see *New Zealand Apple and Pear Marketing Board v Apple Fields*).
- The parties agree to mutual rights and obligations in respect of the course of action to be undertaken (see *Re British Basic Slag Ltd's Agreements*).
- An arrangement is unlikely to exist when only one party makes a commitment to the proposed course of action (see *Trade Practices Commission v Email Ltd* 31 ALR 53).

The recurring theme in these characteristics is that the parties agree to make a combined effort for a common goal. It is arguable that an agreement for the granting of permission to recruit employees into the FFS, between the credit card company and the employer client, is an arrangement under section OB 1. It is clear that where each party agrees to certain actions there is a "meeting of the minds" (*New Zealand Apple and Pear Marketing Board v Apple Fields*) and this is sufficient for there to be an arrangement.

However, before section CI 2(1) has any application, the "arrangement" between the credit card company and the employer must be "for" the provision of a benefit by the employer to the employee.

Is the arrangement "for" the provision of a benefit to the employee?

The use of the word "for" in section CI 2(1) is the critical feature of this component. It was interpreted in the case of *Patrick Harrison & Co. v AG for Manitoba* [1967] SCR 274 as imposing a purpose test. In this case, the Court held that "for the extraction of minerals" meant "with the object or purpose of extracting minerals".

This component limits the arrangements that will fall within the ambit of section CI 2(1) by linking the arrangement to the purpose of providing a benefit to the employees. Accordingly, for section CI 2(1) to apply in this situation there must be an arrangement between the credit card company and the corporate employer to provide a benefit to the employees.

In this Ruling's Arrangement the corporate employer has not entered into any contract or other understanding with the credit card company so that employees receive entitlements under the FFS.

If the employees obtain a benefit or an advantage from joining the FFS, it is from the contractual agreement between the credit card company and themselves rather than from any arrangement between the company and the corporate employer.

It is concluded that any benefit arising from an individual employee's membership of an FFS is not a "benefit" provided or granted by the employer, nor is it provided by way of an "arrangement" entered into by the employer and the credit card company.

However, if there is any form of arrangement between the credit card company and the corporate employer where the benefits pass to employees as a result of that arrangement, there is clearly a provision of a fringe benefit and, accordingly, section CI 2(1) will apply.

Example 1

An employee works for a company. She obtains a personal credit card and joins its associated FFS. Under that scheme she can accumulate points as goods and services are charged on the credit card. After the employee accumulates 10,000 points, she can transfer those points, at her option, to any one of a number of airlines' FFS affiliated to the credit card company's FFS. Once she accumulates a specified number of points on the airline FFS, she can exchange them for free or discounted travel. In the course of her work she incurs a number of employment related charges on the credit card as well as private expenditure. The employee accumulates points on the credit card FFS for both types of expenditure. She very soon reaches the specified threshold of points, and transfers them to a particular airline FFS, exchanging them for a free trip to Fiji.

The company does not have an FBT liability. The receipt of the entitlement under the credit card company's FFS is because of the contractual arrangement between the credit card company and the employee. No arrangement exists between the employer and the credit card company to provide the employee with entitlements under its FFS. It does not matter that some of the points that give the entitlement result from employment related expenditure.

Example 2

The following year the employee obtains promotion in the company and receives a corporate credit card on which she is specified as the cardholder. The credit card is from a different company to that which issued her personal card. This particular credit card company allows cardholders to participate in its FFS. This scheme also allows an accumulation of points as goods and services are charged on the card and a transfer of points, subject to certain conditions, to a participating airline FFS.

The employer does not have an FBT liability on any entitlement received by the employee under the credit card company's FFS. There is no arrangement between the employer and the credit card company to provide entitlements to the employee under the FFS. The employee receives those entitlements because of her contractual relationship with the credit card company.

NOTE: The draft ruling and commentary issued for consultative purposes late last year (PU0042) contained Example 3 which described a situation where the Commissioner could decide that there was an arrangement between an employer and a credit card company in respect of an FFS. It has been decided to remove this example as it raises issues beyond the scope of the "arrangement" to this Ruling which is to rule that there is no liability for FBT where there is no arrangement between the respective parties.

PRODUCT RULING – BR Prd 99/5

This is a product ruling made under section 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling applies to Marcellin College.

Taxation Law

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

This Ruling applies in respect of section 11(2)(e).

The Arrangement to which this Ruling applies

The Arrangement is the supply of tuition services to a person who is not resident in New Zealand pursuant to a contract which provides for that non-resident person to pay the tuition fees in respect of an international student at Marcellin College ("the College"). Further details of the Arrangement are set out in the paragraphs below.

1. The non-resident recipient, being the person who has contracted to pay the fees, is not in New Zealand at any time during the academic year in which the services are performed.

2. The College is a co-educational Catholic school providing education from forms one to seven.

3. The College provides tuition services to New Zealand students free of charge, but also provides tuition services to foreign students on a fee-paying basis.

4. This Ruling only concerns tuition fees.

Process of enrolment and payment of fees for a new international student

5. The contract for the provision of tuition services to foreign students is between Marcellin College and the parent or parents of the student. An application for tuition services form is completed by the parent. The application form states that it is expected that the student will have a New Zealand guardian and homestay whilst he or she is studying at Marcellin College.

6. Upon acceptance by the College, an offer of tuition services to the overseas parent is then made which sets out the tuition fee and relevant terms of the offer. The offer is subject to acceptance by the parent by a required date. This offer, once accepted, constitutes the contract between the College and the parent.

7. There is also a separate contract for the renewal of tuition services containing its own terms and conditions.

Documentation in respect of application, enrolment and payment for a new international student

8. The following documentation is relevant to this application:
   - Application for tuition services by a foreign parent
   - Offer of tuition services to overseas parents
   - Contract of renewal of tuition services.

9. The explanation of each of these documents is as follows:

Application for tuition services by a foreign parent

10. This form is completed by the parent with the relevant details pertaining to the student's background.

11. This form requires the parent to declare and confirm that:
   - The parent is not (at the date of signing) a resident of New Zealand for the purposes of the New Zealand Goods and Services Tax Act 1985 and agrees to notify the school if (at some time in the future while the contract is in force) the parent does become a resident of New Zealand for the purposes of the New Zealand Goods and Services Tax Act 1985.
   - The parent does not (at the date of signing) intend to be physically present in New Zealand on any day that the student will be benefiting from the supply of tuition services by the College. The parent agrees to notify the College immediately if (at some time in the future while the contract is in force) the parent is physically present in New Zealand on any day that the student will be benefiting from the supply of tuition services by the School.

12. The form also states that it is expected that all students will have a New Zealand guardian and homestay while they are studying in New Zealand.

Offer of tuition services to overseas parents

13. This form, containing full details of both the parent and students names, states that the college has entered into a contract with the named parent for the supply of tuition services, subject to confirmation of acceptance by the parent by a required date.

14. The form is also to be used in conjunction with the application for a visa, and contains details of the course content and duration, together with details of the full annual fees payable. The form also states whether the student has been guaranteed accommodation.

Contract of renewal of tuition services

15. This states that the College agrees to renew the contract for the supply of tuition services with the below-signed parent on the conditions contained therein. The relevant terms are:
    - The contract is between the College and the parent who signs below
    - The contract is for the supply of tuition services to the parent
    - The contract is for the period from/to
    - The College agrees to supply tuition services for and to the parent who signs below in consideration of the payment by the parent of the tuition fees
    - The course of tuition is for one year
    - The parent declares and confirms that, at the date of signing, the parent:
      - is not a resident of New Zealand
      - does not intend to be physically present in New Zealand on any day that the student will be benefiting from the supply of tuition services by the College.

16. In regards to the latter, the parent is required to notify the school if, at any time in the future whilst the contract is in force, either of the above circumstances change.

Assumptions made by the Commissioner

This Ruling is based on the following assumptions:

a) The tuition fees charged in respect of the students are solely in respect of tuition services provided by the College.

b) The non-resident parent, who has contracted with the College, is outside New Zealand at all times during the academic year.

c) The New Zealand guardian of the student is not acting as an agent for the non-resident parent.

How the Taxation Law applies to the Arrangement

Subject in all respects to the assumptions above, the Taxation Law applies to the Arrangement as follows:

- The tuition fee charged in respect of the supply of tuition services is a zero-rated supply for GST purposes in accordance with section 11(2)(e) of the Act where the tuition services are contractually supplied by the College to a parent who is not a "resident", in terms of section 2(1), and who is outside "New Zealand", as defined in section 2(1), at the time the tuition services are performed.

The period for which this Ruling applies

This Ruling will apply for the period from the date this Ruling is signed until 31 March 2002.

This Ruling is signed by me on the 25th day of May 1999.

Martin Smith
General Manager (Adjudication & Rulings)

PRODUCT RULING – BR Prd 99/6

This is a product ruling made under section 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling applies to Massey High School.

Taxation Law

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

This Ruling applies in respect of section 11(2)(e).

The Arrangement to which this Ruling applies

The Arrangement is the supply of tuition services to a person who is not resident in New Zealand pursuant to a contract which provides for that non-resident person to pay the tuition fees in respect of an international student at Massey High School ("the School"). Further details of the Arrangement are set out in the paragraphs below.

1. The non-resident recipient, being the person who has contracted to pay the fees, is not in New Zealand at any time during the academic year in which the services are performed.

2. The School is a co-educational state secondary school providing education from forms one to seven.

3. The School provides tuition services to New Zealand students free of charge. The School also provides tuition services to foreign students on a fee-paying basis. The School arranges homestay accommodation where requested.

4. This Ruling only concerns tuition fees.

Process of enrolment and payment of fees for a new international student

5. The contract for the provision of tuition services to foreign students is between Massey High School and the parent or parents of the student. An application for tuition services form is completed by the parent, to which is attached a contract to be signed by the non-resident parent. This constitutes the legally binding contract between the parties once it has been accepted by the School.

6. Upon acceptance by the School, two letters of acceptance are sent together with a fees invoice which sets out separately all of the fees payable for the year in respect of tuition, uniform and stationery, homestay costs and travel costs separately. A letter setting out the refunds' policy for the School is also enclosed with these forms.

Documentation in respect of application, enrolment and payment for a new international student

7. The following documentation is relevant to this application
   - Massey High School application for tuition
   - Contract
   - Letter of acceptance (1)
   - Letter of acceptance (2)
   - Tax invoice
   - Refunds' policy for international tuition contracts.

Massey High School application for tuition

8. This form collects the personal details of both the student and the parents and asks for the name and contact details of a contact person in an emergency. The form alsorequires the parent to indicate whether the student will require homestayaccommodation in New Zealand.

Contract

9. This form is attached to the application form, and the relevant details are as follows:
   - The contract is for the supply of tuition services
   - The contract is between Massey High School and the parent whose signature appears below
   - The term of the contract is for the school year ending 31 December of the relevant year
   - The contract will become binding on all parties once it has been accepted by the School in writing and the relevant fees have been paid
   - That the parent has read the School refund policy
   - That the parent confirms by signing below that, at the date of signing the contract, he or she is not a resident of New Zealand and will notify any changes to this status

- That the parent confirms that, at the date of signing, he or she does not intend to be physically present in New Zealand on any day that the student will be benefiting from the supply of tuition services and will notify any changes from the original intention.

Letter of acceptance (1)

10. This first letter is in the form of a "to whom it may concern" for the purpose of it being provided in support of the visa application. It confirms that the named student will be accepted at Massey High School for the particular academic year on payment of the fees as stated. It also states the names of the persons with whom accommodation has been arranged.

Letter of acceptance (2)

11. This second letter, also in the form of a "to whom it may concern", confirms that the named student has been accepted by Massey High School in the particular year and that the fees as set out in the letter have been paid. The letter also states that school will commence on 1 February and conclude on 9 December of the particular year.

Tax invoice

12. This form is the School's registered tax invoice, and states the name of the student together with the fees payable and itemised separately as to:
    - The tuition fee
    - Uniform and stationery
    - Homestay placement
    - Airport pick-up.

Refunds' policy for international tuition contracts

13. This latter states that the refunds' policy is based on section 4B(7) of the Education Amendment (No. 4) Act 1991. In particular it states:
    - A refund will only be made in special circumstances which have regard to:
      - The costs incurred by the school
      - The salaries of the teachers and support staff already committed to date of withdrawal
      - The facilities and resources already used to date of withdrawal.

      But in any event no refund after 1 March except in exceptional circumstances.

Assumptions made by the Commissioner

This Ruling is based on the following assumptions:

a) The tuition fees charged in respect of the students are solely in respect of tuition services provided by the School.

b) The non-resident parent, who has contracted with the School, is outside New Zealand at all times during the academic year.

How the Taxation Law applies to the Arrangement

Subject in all respects to the assumptions above, the Taxation Law applies to the Arrangement as follows:

- The tuition fee charged in respect of the supply of tuition services is a zero-rated supply for GST purposes in accordance with section 11(2)(e) of the Act where the tuition services are contractually supplied by the School to a parent who is not a "resident", in terms of section 2(1), and who is outside "New Zealand", as defined in section 2(1), at the time the tuition services are performed.

The period for which this Ruling applies

This Ruling will apply for the period from the date this Ruling is signed until 31 March 2000.

This Ruling is signed by me on the 25th day of May 1999.

Martin Smith
General Manager (Adjudication & Rulings)

PRODUCT RULING – BR Prd 99/7

This is a product ruling made under section 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling applies to Mount Albert Grammar School.

Taxation Law

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

This Ruling applies in respect of section 11(2)(e).

The Arrangement to which this Ruling applies

The Arrangement is the supply of tuition services to a person who is not resident in New Zealand pursuant to a contract which provides for that non-resident person to pay the tuition fees in respect of an international student at Mount Albert Grammar School ("the School"). Further details of the Arrangement are set out in the paragraphs below.

1. The non-resident recipient, being the person who has contracted to pay the fees, is not in New Zealand at any time during the academic year in which the services are performed.
2. The School is a state secondary school for boys which provides tuition services to New Zealand students free of charge, but also provides tuition services and accommodation to foreign students on a fee-paying basis.
3. This Ruling only concerns tuition fees.

Process of enrolment and payment of fees for a new international student

4. The contract for the provision of tuition services for foreign students is between Mount Albert Grammar School and the parent. A new international student may apply for a place in the school at any time. An application for enrolment form is completed and signed by the parent of the student.
5. If the School approves the application, the School will send a letter of offer to the parent together with an "Offer of Tuition Services" form and a "Parent Declaration" form.
6. Fees are required to be paid, and when this has been done a letter of acceptance is sent.

Documentation in respect of application, enrolment and payment for a new international student

7. The following documentation is relevant to this application:
   - Form entitled "Application for School Enrolment"
   - International student guide
   - Form entitled "Offer of Tuition Services" and accompanying letter
   - Fees invoice
   - Parent declaration
   - Letter of acceptance.
8. The explanation of each of these documents is as follows:

Application for School Enrolment

9. This document provides no information on the services offered by the School and merely provides for the supply of information by the parent to the School as follows:
   - Student's name and birth details
   - Parent's name, occupation, and address details.

International student guide

10. This is a general information guide setting out the required steps and processes in applying for enrolment at the School by the student.
11. In particular, the guide states that the parent must nominate an active local guardian who will take full responsibility for the student whilst he is in New Zealand.
12. It also states that it is a requirement that the student has full medical and accident insurance.
13. The guide also states the policy on withdrawals and refunds, being that refunds of tuition fees after 1 March of the year will only be made in exceptional circumstances.

Offer of Tuition Services and accompanying letter

14 The offer constitutes the formal contract between the School and the parent and contains the following information:
   - The contract is for the provision of tuition services
   - The course duration is one year

- A commencement date and completion date
- The annual tuition fee.

15 Accompanying the offer is the fees invoice together with a letter confirming a place at the School for the student and requesting the parent to complete and return the enclosed "Parent Declaration" form by the required date.

Parent declaration form

16. In signing this form, the parent is accepting the offer of tuition services and acknowledging that this forms a contract between himself or herself and the School. By signing, the parent is also declaring and confirming with the School:
    - That at the date of signing the contract he or she is not a resident of New Zealand for GST purposes
    - That he or she does not intend to be physically present in New Zealand on any day that their son will be benefiting from the supply of tuition services by the School.

17. The parent is to notify the School immediately if there is any change at any time in the future whilst the contract is in force in respect of either of the above two statements.

Fees invoice

18. The fees invoice sets out the requisite fees as being the fees for tuition services for all of the year.

Letter of acceptance

19. This letter simply acknowledges acceptance of the student for a place in the School and draws the parent's attention to the "Offer of Tuition Services", "Parent Declaration", and "invoice" forms for details of the acceptance.

Assumptions made by theCommissioner

This Ruling is based on the following assumptions:

a) The tuition fees charged in respect of the students are solely in respect of tuition services provided by the School.

b) The non-resident parent, who has contracted with the School, is outside New Zealand at all times during the academic year .

How the Taxation Law applies to the Arrangement

Subject in all respects to the assumptions above, the Taxation Law applies to the Arrangement as follows:

- The tuition fee charged in respect of the supply of tuition services is a zero-rated supply for GST purposes in accordance with section 11(2)(e) of the Act where the tuition services are contractually supplied by the School to a parent who is not a "resident", in terms of section 2(1), and who is outside "New Zealand", as defined in section 2(1), at the time the tuition services are performed.

The period for which this Ruling applies

This Ruling will apply for the period from the date this Ruling is signed until 31 March 2002.

This Ruling is signed by me on the 25th day of May 1999.

Martin Smith
General Manager (Adjudication & Rulings)

PRODUCT RULING – BR Prd 99/8

This is a product ruling made under section 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling applies to Tower Health Limited ("THL").

Taxation Law

All legislative references are to the Income Tax Act 1994 unless otherwise stated.

This Ruling applies in respect of sections BD 2(1), BD 2(2), CB 5 (1)(h) and CD 5 of the Income Tax Act 1994.

The Arrangement to which this Ruling applies

The Arrangement is the Executive Income Protection Indemnity Value Contract issued by THL which provides the following benefits. Note that National Insurance Life & Health Limited changed its name to Tower Health Limited on 1 April 1999.

Total Temporary Disability Benefit

This benefit provides that if the Insured Person suffers a Total Disability, a monthly benefit will be paid as long as the Insured Person remains Totally Disabled until the end of the maximum benefit period.

Total Disability and Totally Disabled are defined as:

The inability of the Insured Person (other than by death), due to Illness or Accident to perform the duties of his or her normal or usual occupation, business or work from which he or she has derived income. An Insured Person is not Totally Disabled if he or she is engaged in any occupation, business or work for financial reward and not under care of a Medical Practitioner.

The amount paid under this benefit is the lesser of:

- The benefit shown in the Policy Schedule or Endorsement Schedule (adjusted by any Inflation Protection Benefit, as described below) and,
- 80% of the Insured Person's monthly income before Total Disability. This is the Insured Person's average monthly Total Income for the 12-month or 36-month period before Total Disability, whichever is greater.

Less the total of the following:

- The Insured Person's Post-Disability Income for the relevant month, and
- If the Insured Person receives any disability lump sum payments under other insurance policies, an amount equal to 1% per month of those lump sum payments (this applies to the first 5 years of the claim).

Post-Disability Income is defined as:

Income from all sources including but not limited to an amount derived by the Insured Person from his or her personal services or personal exertion, employer paid sick leave, payments under other disability contracts, entitlements under the Accident Rehabilitation and Compensation Insurance Act 1992, benefits under the Social Security Act 1964, and entitlement to undrawn profit. It also includes, any other amount (except a superannuation payment) which in [THL's] opinion is either an ongoing income or entitlement to payment or an amount in the nature of income (such as director's fees or a share of profits in some form) which the Insured Person could reasonably be expected to receive from the same source as he or she derived Total Income before his or her Disability (even though the amount is not received). But Post-Disability Income does not include Unearned Income up to $100,000 per annum or a greater or lesser figure than [THL] decide on, from time to time before a claim is paid (relevant amount). It also does not include Unearned Income in excess of the relevant amount if that income has been offset when this Policy was first underwritten.

Partial Disability Benefit

This benefit provides that a monthly benefit will be paid if the Insured Person is Partially Disabled while the Policy is in force. An Insured Person is deemed to be Partially Disabled if that person:

- Was Totally Disabled for a period of more than 14 days in a row; and
- Then returns to his or her usual work, occupation or business, or any other work, occupation or business, but as a result of the illness or accident which caused the Total Disability returns in a reduced capacity or for fewer hours per week than was worked before the disability; and
- Receives total income of less than 80% of that earned before disability.

The dollar value of the benefit to be paid is calculated as follows:

$((A - B) \div A) \times C = D$

where:

A is the greater of the average monthly total income for the 12-month period or the 36-month period before Total Disability.

B is the monthly Post-Disability Income.

C is the amount calculated under the Total Temporary Disability Benefit without the deductions.

D is the Partial Disability Benefit monthly amount.

Recurrent Disability Benefit

The Recurrent Disability Benefit provides that THL will not require a Wait Period before paying the Insured Person the Total Temporary Disability Benefit under the Policy, if the Insured Person:

- Suffers a disability more than once from the same or directly related illness or accident, and it was less than 6 months since he or she was last disabled from that cause; and
- The Insured Person was being paid a monthly benefit for the disability under this Policy .

Wait Period is defined as:

The period specified in the Policy Schedule or an Endorsement Certificate. The period starts from the day the Insured Person suffers a Total Disability or the date a registered Medical Practitioner approved by [THL] certifies that the Insured Person is Totally Disabled, or the date the Insured Person ceases work whichever is later.

Waiver of Premium Benefit

The Waiver of Premium Benefit provides that during any period the Insured Person is being paid a Total or Partial Disability Monthly Benefit he or she will not be charged any premium.

Hospital Benefit

The Hospital Benefit is paid when the Insured Person suffers a Total Disability and is admitted to Hospital as a result. The amount paid is a daily amount equal to 1/30th of the amount of the monthly maximum benefit shown on the Policy Schedule or latest Endorsement Certificate (adjusted by any Inflation Protection Benefit) for each day the Insured Person is in hospital.

The Hospital Benefit will be paid from and including the fourth night of the Insured Person's stay in hospital until one of the following events occur:

- The day the person leaves the hospital; or
- The end of the Wait Period; or
- The 64th day of the stay in hospital; or
- The day a Serious Care Benefit becomes payable to that person.

Premium No Claim Discount Benefit

The Premium No Claim Discount Benefit provides that if no claim has been paid out under the Policy for three consecutive Policy Years, the Insured Person will receive a 15% discount on future premiums. If the Insured Person makes a claim under the Policy while receiving the discount, it will end on the Policy Anniversary Date immediately following the date that the claim was paid.

Inflation Protection Benefit

The Inflation Protection Benefit provides that on each Policy Anniversary Date the Policy Holder is offered the opportunity to increase the maximum amounts of any indemnity value Benefit and Top Up Benefit shown in the Policy Schedule or the latest Endorsement Certificate, without presenting further evidence to THL about his or her health. The increase will be the annual rate of increase in the Consumer Price Index or 5%, whichever is less.

Claims Indexation Benefit

If a Total Disability Monthly Benefit has been paid out arising from the same or directly related cause for 12 months in a row, the Claims Indexation Benefit provides that the amount paid out will be increased on the next Policy Anniversary Date by the annual rate of increase in the latest Consumer Price Index or 5%, whichever is less.

Total and Permanent Disability Benefit

At the end of the Maximum Benefit Period, the Insured Person will be paid an amount equal to 100 times the amount of the last monthly benefit payment if:

- THL has paid the Insured Person a monthly benefit for the Maximum Benefit Period, and
- the Insured Person is, in the opinion of THL (after consideration of all material evidence), Totally and Permanently Disabled as a result of the illness or accident which gave rise to the payment of the monthly benefit.

The amount payable reduces by 20% for every year that the Insured Person's age exceeds 54 years at the time the Total and Permanent Disability becomes payable.

Premium Payback Benefit

The Premium Payback Benefit will be paid shortly after the Policy Anniversary Date immediately following the Insured Person's 60th birthday or the date that the Policy has been in force for 15 consecutive years, whichever is later. Only one Premium Payback Benefit will be paid under the Policy and it will be calculated according to the formula below.

If the Policy ends after it has been in force for at least 15 consecutive years but before the Policy Anniversary Date following the Insured Person's 60th birthday, THL will pay 50% of the amount calculated according to the formula below.

The Premium Payback Benefit is calculated as follows:

The total dollar value of all premiums paid under the Policy (except any premiums paid after the Policy Anniversary Date following the Insured Person's 60th birthday or the date that this Policy has been in force for 15 consecutive years, whichever is later).

Less the dollar value of each of the following:

- Goods and Services Tax
- All Policy fees
- All premium frequency loading fees
- All Benefits paid any time under the Policy and benefits payable in respect of any claims notified before this benefit is paid.

After the Premium Payback Benefit is paid, if the Maximum Benefit Period of the Policy is when the Insured Person reaches the age of 60, the Policy and all cover will end. If the Maximum Benefit Period is to age 65, the Policy will continue until the Policy Anniversary Date following the Insured Person's 65th birthday, as long as the premiums continue to be paid.

Serious Care Benefit

The Serious Care Benefit provides that an amount equal to 12 times the maximum benefit for Total Disability shown on the Policy Schedule or Endorsement Certificate (adjusted by any Inflation Protection Benefit) will be paid out, if:

- The Insured Person is diagnosed as suffering for the first time in their lifetime, one of the Serious Care Conditions defined in the Policy; and
- The diagnosis is made on the basis of clinical findings and reports acceptable to THL; and
- The Insured Person survives for 30 days following the date of diagnosis; and
- The date of diagnosis is at least 90 days after the Commencement Date and before the date on which cover for this benefits ends.

Top Up Benefit

The Top Up Benefit provides a monthly amount in addition to the Total Disability Monthly Benefit. The amount paid is the lesser of:

- The maximum amount of this benefit, as stated in the Policy Schedule; or
- 20% of the Insured Person's monthly total income before disability; or
- The difference between the Insured Person's monthly total income before disability and the total of Monthly Benefit THL pays.

Non-Smoker Discount Benefit

The Non-Smoker Benefit provides that if the Insured Person has not smoked tobacco in the previous 12 months and is not already receiving a non-smoker premium discount, then the Insured Person may apply for this discount.

Assumptions made by the Commissioner

This Ruling is based on the following assumptions:

- The Indemnity Value Contract is taken out by an individual and provides cover for that individual.

How the Taxation Law applies to the Arrangement

Subject in all respects to the assumptions above, the Taxation Law applies to the Arrangement as follows:

- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Total Temporary Disability Benefit will be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Total Temporary Disability Benefit will be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Partial Disability Benefit will be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Partial Disability Benefit will be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Total Permanent Disability Benefit will be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Total Permanent Disability Benefit will be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Top Up Benefit will be gross income under section CD 5:

- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Top Up Benefit will be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Recurrent Disability Benefit will be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Recurrent Disability Benefit will be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Claims Indexation Benefit will be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Claims Indexation Benefit will be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Hospital Benefit will not be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Hospital Benefit will not be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Serious Care Benefit will not be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Serious Care Benefit will not be an allowable deduction under section BD 2(1):
- Any benefit received by the Insured Person under the Indemnity Value Contract by way of the Premium Payback Benefit will not be gross income under section CD 5:
- The portion of premium paid by the Insured Person under the Indemnity Value Contract for the Premium Payback Benefit will not be an allowable deduction under section BD 2(1):
- The Waiver of Premium, Non-Smoker Discount, Inflation Protection and Premium No Claim Discount Benefits under the Indemnity Value Contract have no tax consequences.

The period or income year for which this Ruling applies

This Ruling will apply for the period from 1 April 1999 to 31 March 2002.

This Ruling is signed by me on the 17th day of June 1999.

John Mora
Assistant General Manager (Adjudication & Rulings)

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.

GST – WHETHER INPUT CREDIT AVAILABLE ON SALE AND SUBDIVISION OF LAND ACQUIRED IN 1984

Case: TRA Number 96/104.
Decision Number 014/99

Decision date: 9 July 1999

Act: Goods and Services Tax Act 1985

Keywords: Taxable activity

Summary

The final issue to be determined in this case was whether an input credit based on the market value of the farmland was available at the commencement of the Objector's taxable activity of subdivision and sale. Judge Barber found in favour of the Commissioner. This case was previously reported as *Case T60* (1998) 18 NZTC 8,449.

Facts

The Objector's jointly purchased a number of properties in 1984 and in 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 acquired in 1987. The Commissioner allowed the credit despite the fact that the land was in the name of both of the Objectors. In 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 threshold for registration.

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

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

Decision

Judge Barber agreed with the Commissioner's arguments in respect of section 21(5) and stated that in respect of goods and services acquired or produced after 1st October 1986, there can be no input tax deduction for the Objectors for the purchase of the farmland acquired in 1984.

His Honour also agreed with the Commissioner that section 21(5) expressly requires that there have been no prior deductions in respect of the goods and services in question and the objectors cannot obtain an input tax deduction (on commencement of their sudivisional activity) for the 1987 purchase.

Judge Barber concluded that the only input credit available for the Objector's related to the 1987 purchase and that the husband had taken this input credit on behalf of the Objectors. He stated that the Objectors were not entitled to a GST input in respect of the farm as at the time they commenced their sudivisional activity .

DEDUCTION IN RESPECT OF LOSS SET-OFF – WHETHER INTEREST LOSSES CANCELLED AS A RESULT OF LIQUIDATION; WHETHER COMMISSIONER ABLE TO ALTER ASSESSMENT

Case: Hot Dip Galvanisers (Christchurch) Ltd & Brian Perry Ltd v CIR

Decision date: 20 July 1999

Act: Income Tax Act 1976

Keywords: Offset of losses

Summary

The Court of Appeal held that the Appellants had not discharged the onus of proof, which rested on them and dismissed the appeal.

Facts

The appellant companies together with one other company, L Ltd, formed a specified group for the purposes of section 191(5) of the Income Tax 1976. The two appellant companies applied interest losses incurred by L Ltd against their profits. L Ltd had been wound up on 2 May 1979 and the receivers, appointed under three debentures, paid $888,824 to the debenture holders in the period from 3 February 1977 to 15 March 1993. The Commissioner subsequently determined that the interest deductions which resulted in the company's losses for the 1981,1982 and 1983 income years had actually been remitted or cancelled. On the basis of this determination, the Commissioner issued an amended assessment for each of the appellants disallowing the deduction in respect of the loss set-off.

The Taxation Review Authority was asked to determine whether the interest taken into account in calculating the losses sustained by L Ltd was cancelled or remitted as a consequence of the liquidation of that company and, if so, whether the Commissioner acted correctly in making the amended assessments of the appellants' liability for income tax for the years in question. The Taxation Review Authority held that the Commissioner had the power pursuant to section 188(4) to alter any assessment to reduce losses previously taken into account in assessing the income of a taxpayer . The debt used in the calculation of losses had to have been remitted or cancelled in whole or in part for section 188(4) to operate.

The Taxation Review Authority found that in the present case the loss company had gone into liquidation and had been struck off the register of companies. In terms of section 188(6)(b), the debt had been deemed to have been cancelled as the loss company had been released from its liability under the debenture by operation of the Companies Act 1955. Furthermore, pursuant to section 188(6)(c) a debt is deemed to have been cancelled to the extent to which it has become irrecoverable or unenforceable by action through the lapse of time.

Judge Barber stated that there did not seem to be any dispute between the parties that the payments made by the receivers or liquidators to the debenture holder must be treated as having been applied to capital or loan principal rather than to interest. Accordingly, the Commissioner was correct in disallowing the deduction in respect of the loss set-off. In the High Court Justice Morris concurred with Judge Barber's approach.

Decision

Justice Thomas stated that s191(7B) is a deeming provision which deems s 188(4)(5) and (6) to apply to a company which has obtained a deduction under s 191(5) or (7). It would not make sense, and would have little or no practical application, if the power to "alter any assessment" at "any time" were not to apply to an assessment made in respect of the income-making company relating to a debt to which s 188(4),(5) and (6) applies. The reference to these subsections and s 191(7B) could have no other realistic purpose than to provide the Commissioner with authority to alter the assessment of a company that has obtained a deduction, being the loss made by another company in the specified group, when that loss is remitted or cancelled. Apart from the clear direction in s188(4) the Commissioner may at any time alter any assessment. A construction which required the loss-making company to be assessed first would lead to absurd and unjust results. It would, in effect, provide a tax exemption for any income-making company in a group where the loss-making company was no longer in existence.

The appellants disputed the application of the rule in *Clayton's Case* (1816) 1 Mer 572. They argued that the presumption in *Falk v Haugh* (1935) 53 CLR 163 was applicable to the present case. Justice Thomas considered that it would be impermissible to enter into the question of whether a presumption applied in the present case. There were two reasons for this view. Firstly, pursuant to section 36 of the Inland Revenue Department Act 1974 the objector is

limited to the grounds stated in his or her objection and the burden of proof is on the objector. Secondly, the appeal was an appeal by way of case stated. In the present case it was plain that the case stated by the Authority set out the relevant facts as determined by the TRA and then posed three questions for the opinion of the High Court. The Authority's findings of facts were not put in issue, and the hearing and determination in the High Court could not embrace a rehearing of the facts.

Justice Thomas found that the appellants never disputed that the receiver's payments were to be treated as having been applied to principal rather than interest. His Honour found that in the High Court Justice Morris proceeded on the basis that an appropriation had not been made and that, in those circumstances, the presumption in *Clayton's Case* applied. Justice Morris regarded it as an established fact that neither the receivers nor the debenture holders had made an appropriation of the payments. In proceeding on this basis Justice Morris misconstrued the Authority's judgment and accepted as fact a position, which had never been found or established by the Authority. Justice Thomas found that in actual fact the appellants had not adduced any evidence as to how the receivers or debenture holders dealt with the payments. The receivers' abstracts did not indicate the direction of the payments one way or the other. Accordingly, the circumstances which would permit the application of the presumption had not been established.

AWARDS FOR COSTS IN TAX CASES

Case: National Insurance Company of New Zealand v CIR – 2nd costs hearing

Decision date: 30 July 1999

Facts

The substantive case was reported as *National Insurance Co of NZ Ltd v Commissioner of Inland Revenue* (1997) 18 NZTC 13,489 and on appeal to the Court of Appeal as *Commissioner of Inland Revenue v National Insurance Co of NZ Ltd* (1999) 19 NZTC 13,489. The first hearing on costs is reported as *National Insurance Co of NZ Ltd v Commissioner of Inland Revenue* (No 2) (1998) 18 NZTC 13,761.

In the first costs hearing the taxpayer was awarded $150,000 plus disbursements on the basis that awards for costs in tax cases were much less than in other civil cases.

The issue of costs in tax cases was subsequently heard by the Court of Appeal in *Auckland Gas Co Ltd v Commissioner of Inland Revenue* (1999) 19 NZTC 15,027. The Court essentially said that tax cases are no different to any other civil case, and costs should therefore be determined on the same basis as all other civil cases.

When the substantive issue in this case was heard before the Court of Appeal, the issue of costs to be awarded in the High Court was referred back to the High Court.

Decision

The Court considered the authorities referred by counsel and those relating to costs collected in *McGechan on Procedure* (paras HR46.05 and 46.07 p3-67 - 3-72(a)). In particular the Court gave further consideration to:

- the length of the hearing;
- the number of issues raised and contested by the parties (including the factual and legal complexities involved;
- the amount at stake and the importance of the issues to the parties;
- the extended period for which costs in tax cases are now to be regarded as payable with the new costs regime;
- the relative success of each party;
- the rough-and-ready rule of thumb that at least as much time and effort has to be put into the preparation as the hearing itself;

  the comments of the Court of Appeal on GST.

Having regard to all these factors the Court ordered the Commissioner to pay the sum of $700,000 plus disbursements.

WHETHER OBJECTOR WAS RESIDENT OF NZ FOR THE PURPOSES OF TAXATION OF INCOME

Case: TRA Number 98/40. Decision Number 016/99

Decision date: 27 July 1999

Act: Income Tax Act 1976

Keywords: Whether Objector was resident of NZ, Double Tax Relief Order

Facts

The Objector is a successful businessman who had devoted his time to business almost to the exclusion of his family. The Objector and his wife separated and he moved to Singapore and did not anticipate returning to New Zealand.

The Objector took up the lease of an apartment in Singapore, opened bank accounts, was granted permanent residency, obtained a Singapore Inland Revenue number and started his own business.

In 1995 the Objector returned to New Zealand and reconciled with his wife and family.

The Commissioner contended that the objector was a resident of both New Zealand and Singapore for the purposes of taxation of his income. The Objector contended that from 1991 to 1993 inclusive that he did not have a permanent place of abode in New Zealand.

Decision

Judge Willy found for the objector on the facts of the case. His Honour listed a number of factors that were relevant in showing that the Objector did not intend to return to New Zealand.

Judge Willy held that for the period between 1990 and 1994 the Objector had abandoned his residence in New Zealand and was wholly resident in Singapore and that the reason the Objector kept assets in New Zealand was so he could provide for his family and as an asset base to finance his Singapore business.

Thus the frequent visits of the Objector to New Zealand did not detract from his assertion that for 4 years he became wholly resident in Singapore.

Judge Willy then considered sections 294, 241, and 242 of the Income Tax Act 1976 and the Double Taxation Relief (Singapore) Order 1973 (1973/256). On the facts as found by Judge Willy, the Objector was not a New Zealand resident "for the purposes of New Zealand tax" as defined in Article 3 of the order. He was a Singapore resident for the years covered in the case stated. That being so, income earned by the Objector could not, in terms of section 242, be brought to tax in New Zealand. Article 16 of the order did not need to be considered.

STANDARD PRACTICE STATEMENTS

These statements describe how the Commissioner will, in practice, exercise a statutory discretion or deal with practical issues arising out of the administration of the Inland Revenue Acts.

PAYMENT OF DEBT BY COMPULSORY DEDUCTIONS FROM BANK ACCOUNTS

Introduction

This Standard Practice Statement outlines Inland Revenue's practice on the use of Notices to Deduct. This statement covers:

- monitoring of bank accounts
- overdraft facilities
- investments
- joint bank accounts
- interest
- prosecution

This Standard Practice Statement has been updated to include new legislation.

Application date

This Standard Practice Statement replaces Standard Practice Statement RDC 3, published in TIB V ol Ten No.10 (October 1998). This amended Standard Practice Statement applies to all deduction notices issued on or after 1 September 1999.

Legislation

Section 157 of the Tax Administration Act 1994 allows the Commissioner of Inland Revenue to issue a Notice requiring compulsory deductions to be made from amounts that are, or become payable by any person to a defaulting taxpayer . The Notice may require deductions to be made by way of a lump sum or instalments. The Notice may also require that daily interest be deducted, from the date of the written notice, until the amount in default has been deducted.

Other Legislation

The following legislation is similar in content to section 157 of the Tax Administration Act 1994:

- section 43 of the Goods and Ser vices Tax Act 1985
- section 154 of the Child Support Act 1991
- section 46 of the Student Loan Scheme Act 1992
- section 12L of the Gaming Duties Act 1971
- section 46 of the Accident Compensation Act 1982
- section 130 of the Accident Rehabilitation and Compensation Insurance Act 1992
- section 313 of the Accident Insurance Act 1998.

Monitoring of bank accounts

A Notice to Deduct may require deduction from amounts held on the date of the Notice or from amounts deposited after the date of the Notice. However Inland Revenue and the Bankers' Association have agreed that banks will generally not be required to monitor accounts on a daily basis.

If there is an exceptional case where Inland Revenue considers daily monitoring to be necessar y, Inland Revenue will ask the bank to monitor the account for a specific period. Inland Revenue' s requirements will be discussed with the bank at the time. Unless there are exceptional circumstances, the maximum period a bank will be required to monitor an account is ten working days.

Example

The taxpayer has a large debt, which has been outstanding for some time. Inland Revenue is aware that the taxpayer is expecting to receive funds from an overseas source. It is known that payment of the funds, to the bank, will be made in the first week of the month, but the exact day of payment is not known. Inland Revenue will consult with the bank concerned and request that the account be monitored for the first week of that month.

Overdraft facilities

Inland Revenue cannot, by requiring a deduction to be made from a bank account, put a taxpayer into, or further into overdraft.

If Inland Revenue issues a Notice to Deduct for an account which is in credit and the taxpayer attempts to evade it by transferring funds to an account in overdraft, then the Notice will take priority.

Investments

Compulsory deductions may be made from money that is held in a term investment before the date that the investment is due to mature. This may result in a reduced rate of interest on the investment.

Joint bank accounts

General information

Previously the Commissioner issued Notices to Deduct for joint accounts if the signatory was "either or".

In *ANZ Banking Group (New Zealand) Limited v CIR* (1998) 18 NZTC 13,643 the High Court held the Commissioner could not issue a Notice to Deduct to obtain funds from a joint account in respect of the income tax debt owed by one of the joint bank account holders, because there was no authority to do so.

Inland Revenue will not issue Notices to Deduct for joint accounts, in respect of a debt owed by only one of the account holders except where the Commissioner has specific authority (eg for family assistance and child support).

Family assistance debts

When an overpayment for family assistance has occurred the person who received the overpayment (the recipient) and their partner or spouse (if they were the partner or spouse throughout the income year to which the overpayment relates) are jointly and severally liable for the overpayment (section KD 4(4) Income Tax Act 1994). The Commissioner is therefore able to issue a Notice to Deduct for an account in the name of the partner or spouse or for a joint account in the name of the recipient and the partner or spouse.

Child support debts

The Child Support Act 1991 allows the Commissioner to require deductions from money payable to liable parents for a child support debt. Section 155 of the Act extends this to money held in joint accounts in the name of the liable parent and one or more other persons, where the liable parent can draw from that account without the signature of the other person.

Interest

A Notice to Deduct may require deductions to be made to cover daily interest. The interest starts on the date of the Notice to Deduct and ends on the day on which the amount required to be deducted, has been deducted.

Prosecution

If a bank fails to make the required deductions and there was an amount payable, or an amount that became payable, Inland Revenue has the power to prosecute for not complying with the terms of the deduction notice.

This Standard Practice Statement was signed by me on 9th August 1999

Michael Rapson
Manager, Technical Standards

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 inter est 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.

TAX ADMINISTRATION ACT 1994

Specified rates of interest / additional tax for tax in dispute

A tax practitioner has asked for a summary of the specified rates of interest / additional tax on tax in dispute.

The rates that have been set are:

Period	Rate	
8 March 1999 to present	10.59% 3.38%	– taxpayer's paying rate – Commissioner's paying rate
8 November 1998 to 7 March 1999	12.48 % 4.79 %	– taxpayer's paying rate – Commissioner's paying rate
7 July 1998 to 7 November 1998	14.69% 8.26%	– taxpayer's paying rate – Commissioner's paying rate
1 April 1997 to 6 July 1998	13.9% 7.1%	– taxpayer's paying rate – Commissioner's paying rate
1 April 1996 to 31 March 1997	9%	– for both
1 April 1994 to 31 March 1996	7%	– for both
1 April 1992 to 31 March 1994	10%	– for both
1 April 1989 to 31 March 1992	13.5%	– for both
1 April 1985 to 31 March 1989	20%	– for both

Interest and additional tax, for tax in dispute, are calculated on a daily basis. If the tax is in dispute across more than one of the above periods, the interest or additional tax charged or the interest payable will be calculated at the daily rate that applies in each separate period. For example:

The Commissioner is successful in a case where the tax is in dispute from 1 March 1999 to 31 May 1999. The unpaid tax would attract interest at 12.48 % (on a daily basis) for the first 7 days, then 10.59% (on a daily basis) for the other 85 days.

TIB Vol 11, No. 6 (July 1999) contains details of amendments to the r ules on tax in dispute and use of money interest which confirm their application to income years prior to 1997.

MATTERS OF INTEREST

GST AND BLOODSTOCK DESTINED FOR EXPORT

Introduction

This policy statement amends Inland Revenue's previous policy statements on zero-rating of Goods and Services Tax and export of bloodstock contained in Targeted Circular T/C 91/111, TIBs Vol.2 No.7, Vol.3 No.3, Vol.4 No.6. This statement sets out the policy in relation to bloodstock destined for export that will not be exported within 28 days of the time of supply.

Background

Under section 11(1C)(b) of the Goods and Services Tax Act 1985 the Commissioner may extend the period of time that goods sold for export may remain in New Zealand where it is not practicable, due to the nature of the supply, for the goods to be exported within 28 days of the time of supply.

The previous policy statements set out the maximum extension period available for bloodstock exports to Asia as 10 months and to other destinations as 6 months.

Policy

The Commissioner has a discretion to extend the 28-day period before the supply of goods is charged with GST where, due to the nature of the supply, it is not practicable for the supplier to export the goods within 28 days of the time of supply.

Pursuant to this policy statement, the Commissioner may grant an extension of time to a maximum of 12 months from the time of supply. The extension is available for all age bloodstock to all destinations.

There can be no "consumption" for GST purposes of the bloodstock in NZ prior to export. For a definition of "consumption" please see TIB Vol.4 No.6

An application for an extension must be made in writing accompanied by a copy of the contract of supply directed to your local Inland Revenue office.

Bloodstock exported by the supplier

For goods to be zero-rated when supplied the -

- supplier will enter the goods for export, pursuant to the Customs and Excise Act 1996, in the course of, or as a condition of making the supply and will export the goods; or
- goods will be deemed to be entered for export, pursuant to the Customs and Excise Act 1996, and exported by the supplier in the course of, or as a condition of, making the supply.

By contrast, if a horse is sold in New Zealand and exported by the purchaser, it is the purchaser and not the supplier who is the exporter. As a result this supply could not be zero-rated.

Liability where zero-rated bloodstock is on-sold or not exported

If the zero-rated supply of bloodstock for export is on-sold by the purchaser to another party (regardless of whether the other party is in New Zealand or overseas) then the supply could not be zero-rated. The original supplier would be liable for the GST that would have been chargeable if GST had been levied at the applicable rate (currently 12.5%).

Application date of policy

The policy contained in this statement will be effective from the 16th of August 1999.

REGULAR FEATURES

DUE DATES

September 1999

5 Large employers: PAYE deductions and deduction schedules for period ended 31 August 1999 due.

7 Provisional tax and/or Student Loan interim repayments: first 2000 instalment due for taxpayers with May balance dates.

Second 2000 instalment due for taxpayers with January balance dates.

Third 1999 instalment due for taxpayers with September balance dates.

1999 end of year payments due (income tax, Student Loans, ACC premiums) for taxpayers with October balance dates.

1999 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 2000 year.

20 Large employers: PAYE deductions for period ended 15 September 1999 due.

Small employers: P AYE deductions and deduction schedules for period ended 31 August 1999 due.

Gaming machine duty return and payment for month ended 31 August 1999 due.

RWT on interest deducted during August 1999 due for monthly payers.

RWT on dividends deducted during August 1999 due.

Non-resident withholding tax (or approved issuer levy) deducted during August 1999 due.

30 GST return and payment for period ended 31 August 1999 due.

Non-resident Student Loan repayments - second 2000 instalment due.

October 1999

5 Large employers: PAYE deductions and deduction schedules for period ended 30 September 1999 due.

7 Provisional tax and/or Student Loan interim repayments: first 2000 instalment due for taxpayers with June balance dates.

Second 2000 instalment due for taxpayers with February balance dates.

Third 2000 instalment due for taxpayers with October balance dates.

1999 end of year payments due (income tax, Student Loans, ACC premiums) for taxpayers with November balance dates.

1999 income tax returns due to be filed for all non-IR 5 taxpayers with June balance dates.

QCET payment due for companies with November balance dates, if election is to be effective from the 2000 year.

20 Large employers: PAYE deductions for period ended 15 October 1999 due.

Small employers: P AYE deductions and deduction schedules for period ended 30 September 1999 due.

FBT return and payment for quarter ended 30 September 1999 due.

Gaming machine duty return and payment for month ended 30 September 1999 due.

RWT on interest deducted during September 1999 due for monthly payers.

RWT on interest deducted 1 April 1999 to 30 September 1999 due for six-monthly payers.

RWT on dividends deducted during September 1999 due.

Non-resident withholding tax (or approved issuer levy) deducted during September 1999 due.

29 GST return and payment for period ended 30 September 1999 due.

Binding rulings, interpretation statements, standard practice statements: your chance to comment before we finalise them

This page shows the draft public binding rulings, interpretation statements and standard practice statements that we now have available for your r eview. You can get a copy and give us your comments in these 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 other offices.

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

Name ______________________________

Address ______________________________

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√	*Interpretation statements*	*Comment Deadline*
☐	**IS0025** Dairy farming – deductibility of certain expenditure	30 September 1999

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

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

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The Manager (Field Liaison)

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Inland Revenue Department
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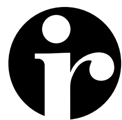

Tax Information Bulletin

Mailing list update form

When you have completed this form please return it to: TIB Mailing List, PO Box 31 581, Lower Hutt

Reason for update
(Please tick)

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- You are already on the TIB mailing list but want to change your name/address required—fill in your details below.
- You don't want to receive the TIB anymore and want your name from the mailing list—attach TIB mailing label or fill in details below.

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