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This TIB has no appendix

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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 *Adjudication & Rulings, a guide to Binding Rulings (IR 715)* or the article on page 1 of *Tax Information Bulletin* Vol 6, No 12 (May 1995) or Vol 7, No 2 (August 1995).

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PRODUCT RULING – BR PRD 03/11

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 has been applied for by Barkworth Olive Groves Pty Limited ("BOGL") – Project No 5.

Taxation Laws

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

This Ruling applies in respect of sections EP 1, BD 2(1)(b)(i), BD 2(2)(e), EG 1, and the section OB 1 definition of "depreciable property".

This Ruling does not consider or rule on the potential application (if any) of sections EF 1 and BG 1, or Determination E 10.

This Ruling considers expense deductibility in relation to section BD 2(1)(b)(i) (incurred by the taxpayer in deriving the taxpayer's gross income). Accordingly it has not been necessary for the purposes of this Ruling to consider or rule on whether investors are carrying on a business for the purposes of the Act.

The Arrangement to which this Ruling applies

The Arrangement is the purchase of a minimum of 250 "E" class shares in BOGL, and the growing of olives on certain land situated in Australia in respect of which the shares provide the right to grow olives, and the appointment of Barkworth Olive Management Limited ("BOML") to manage the growing, processing and marketing of those olives. This Ruling only applies to investors who appoint BOML to manage their Farms.

All amounts quoted in this Ruling are exclusive of Australian GST (if any).

Further details of the Arrangement are set out in the paragraphs below.

1. The Arrangement is governed by the terms of the "Barkworth Olive Groves Project No 5" ("Project No 5") prospectus dated 9 April 2001 ("the prospectus"). Project No 5 is in no way dependent on the Barkworth Group's four existing projects and may be operated independently of the other four. Key aspects of the prospectus are as follows:

   (i) Investors (also referred to as "members" or "Grower") purchase a minimum parcel of 250 "E" class shares of $1 each in a land owning company (BOGL): additional shares may be applied for in parcels of 250.

   (ii) Holders of "E" class shares have the following rights:

   - A member shall have the absolute right to occupy one "Farm" (or section of olive grove) in respect of each 250 "E" Class shareholding held by that member, subject to the payment of all moneys due to BOGL. The Farm shall be an identified area of land as nearly as practicable in area to 0.08 hectares and suitable for the planting of 20 olive trees at spacings of approximately 5 metres by 8 metres. The member's Farm or Farms will be separately identified on a master plan maintained under the supervision of the directors of BOGL.
   - A member shall have an absolute right to process up to 1.5 tonnes of olives per annum in respect of each 250 "E" Class shareholding, subject to the payment of Factory Access Fees. The time allotted for each member's processing

operations will be advised at least two weeks prior to commencement of the harvest period. The member may exchange his or her allotted time with any other member or members with the approval of BOGL: such approval not to be unreasonably withheld. The time allotted per 250 "E" Class shareholding will be as near as practicable to one half-hour and will be with respect to a machine or machines capable of processing in excess of 3 tonnes per hour.

- A member shall have the right to own and operate a business, as defined by the Constitution of BOGL, for the commercial cultivation and harvesting of olives on the member's Farm and the sale of produce therefrom.
- A member shall also have the right to own and operate a business as defined in the Constitution of BOGL, for the commercial processing and marketing of processed olive products which include, but are not necessarily limited to, olive oil and pickled table olives.
- A member shall have the right to use the agricultural infrastructure which includes, but is not necessarily limited to, roads around the property, access to irrigation mains and storage areas. This will be subject to the reasonable regulations imposed by BOGL's directors.
- A member shall have the right to use the processing infrastructure which includes, but is not necessarily limited to, loading and unloading equipment, storage areas, grading and sampling equipment. This will be subject to the reasonable regulations imposed by BOGL's directors.
- A member shall have the right to appoint BOML to manage his or her interests in accordance with the Management Agreement. Alternatively, Growers have the right to manage the business personally or to appoint an employee, contractor, or agent to manage the business on their behalf.
- A member shall have the right to assign, transfer, or otherwise deal with the abovementioned special rights to any person, persons, or corporation with the approval of the directors of BOGL: such approval not to be unreasonably withheld.

(iii) The rights attaching to "E" Class shares expire on 1 July 2021 and, in accordance with the Constitution of BOGL, become ordinary shares. At that time BOGL will assume responsibility for, and the benefits of, the olive trees and from then on the member's benefits will be derived from the member's interest in BOGL by virtue of shares held.

(iv) A member or his or her assignee is obliged to ensure the efficient running of the business. If an employee, contractor, or agent is engaged to fulfil this function, BOGL must be satisfied in regard to the competence of that person or corporation and give its written approval.

Relationship between BOGL and members

(v) The members' interests are separate from the operation of the business of BOGL.

(vi) BOGL will derive income from annual Farm Administration Fees received from members. The year one Administration Fee in respect of the 2001 – 2002 year will be $88 for each parcel of 250 "E" Class shares allotted to the member.

(vii) In year two the Administration Fee will be $75 payable in advance.

(viii) Thereafter, until and including the year 2021, the annual Administration Fee shall be 10% of the gross income generated from the sale of olives attributable to the member's Farm.

(ix) BOGL will also derive income from the payment by the member of Factory Access Fees for each 250 "E" Class shareholding as follows:

- Year 1 – $22
- Year 2 – $225
- Year 3 and thereafter – 15% of the gross income generated from the sale of processed olive products attributable to the member's processing allocation. 90% of all income derived by BOGL for Factory Access Fees will be paid to the Factory Owner and the remaining 10% will be retained by BOGL to cover administration costs. BOGL may also derive income from the commercial use of that residue of BOGL land not being used for olive growing and from any direct interest in olive processing which BOGL may acquire.

2. The members may appoint BOML as the manager of the Farms. The Management Agreement is entered into between BOML and BOGL (as the agent of the members).

3. The Manager's duties until 30 June 2002 (as provided in clause 4.1 of the Management Agreement) are as follows:

   (i) BOML will carry out the duties required to supply olive trees, plant olive trees on the Grower's Farm, bring the trees to an initial harvest, process olives (whether those olives are sourced from the Farm or elsewhere), and market olives and processed olive product. Without limiting the generality of this clause BOML must:

      (a) Supply at least 20 olive trees to the Grower selected from high yield stock in healthy condition.

      (b) Carry out irrigation works to benefit the Grower's Farm.

      (c) Carry out drainage work and work to help prevent soil erosion on the Grower's Farm.

      (d) Prepare the Grower's Farm so that it will be suitable for the planting and growing of at least 20 olive trees.

      (e) Plant the olive trees supplied to the Grower on the Grower's Farm

      (f) Tend the trees and Grower's Farm in a proper and skilful manner

      (g) Comply with BOGL's constitution in so far as it relates to the use of the Farm and Grower's Processing Allocation (except for the payment of Administration Fees and Factory License Fees).

      (h) At BOML's discretion, procure raw olives, olive products or both from sources other than the Farms for processing, marketing and selling.

      (i) Determine the products into which those olives will be processed and the proportions of the various products.

      (j) Carry out the processing of some or all of those olives or olive products attributable to the Grower's Farm following harvest and olives procured from sources other than the Farms (in the Responsible Entity's discretion as it thinks fit and at all times acting in the best interests of the Grower) in a proper and workmanlike manner having regard to proper workplace practices as well as in accordance with acceptable industry practices applicable to processing olives.

      (k) Subject to the Grower's rights under clause 6.3 and 6.4 package, market and sell the olives attributable to the Grower's Farm and the processed olives attributable to the Grower's Processing Allocation using reasonable endeavours to obtain the maximum price available.

      (l) If BOML markets and sells the processed olives attributable to the Grower's Farm and the processed olives attributable to the Grower's Processing Allocation, account to the Grower and if relevant the Custodian for the proceeds of such sale.

      (m) Subject to the Grower's right to carry out its own weeding under clause 6.1, eradicate as far as reasonably possible any pests and competitive weeds which may affect the growth or yield of trees.

      (n) Repair damage to roads, tracks, or fences on the Farms or on neighbouring land resulting from the actions of BOML or its contractors.

      (o) Embark on such operations as may be required to prevent or combat land degradation on the Grower's Farm or land surrounding the Grower's Farm.

      (p) Where the Responsible Entity is not BOML, pay or cause to be paid to BOML the "Barkworth" name license fee paid under clause 7.1.

4. The ongoing duties of the Manager (as provided in clause 4.3 of the Management Agreement) are as follows:

   (i) BOML must continue to maintain the Farm and source, process, and market olives and olive products following the completion of the duties outlined in clause 4.1.

   (ii) BOML's duties must be carried out according to sound agricultural, environmental, and proper workplace practices as well as in accordance with industry practices applicable to growing olive trees and processing and marketing olives or olive products. Without limiting the generality of this clause, BOML must:

      (a) Tend the trees and the Grower's Farm in a proper and skilful manner.

(b) Subject to the Grower's right to carry out its own weeding under clause 6.1, eradicate as far as reasonably possible any pests or competitive weeds which may affect growth or yield of the trees.

(c) Comply with BOGL's constitution in so far as it relates to the use of the Grower's Farm and the Grower's Processing Allocation (except for the payment of Administration Fees and, if applicable, Factory Licence Fees).

(d) Repair damage to roads, tracks, or fences on the Grower's Farm or on neighbouring land resulting from the actions of BOML or its contractors.

(e) Embark on such operations as may be required to prevent or combat land degradation on the Grower's Farm or land surrounding the Grower's Farm.

(f) Subject to the Grower's right to harvest its own trees under clause 6.2, harvest the trees on the Grower's Farm at or around the time estimated by BOML to maximise the produce from all the Farms established at or around the same time as the Grower's Farm.

(g) At the discretion of BOML, procure raw olives or olive products whether from the Farm or from other sources other than the Farms for processing, marketing and sale. Any olives or olive products so acquired will be the property of, and at the risk of, BOML. However, BOML will account for the proceeds as required under clause 4.3(k).

(h) Determine the products into which those olives or olive products will be processed and the proportions of the various products.

(i) During the processing time allowed under the Grower's Processing Allocation, carry out the processing of some or all of the olives attributable to the Grower's Farm following harvest and olives procured from sources other than the Farms, (in BOML's discretion as it thinks fit and at all times acting in the best interests of the Grower), in a proper and workmanlike manner having regard to proper workplace practices as well as in accordance with acceptable industry practices applicable to processing olives.

(j) Subject to the Grower's rights to take and market olives and processed olive products under clauses 6.3 and 6.4, package, market, and sell the olives attributable to the grower's Farm and the processed olives attributable to the Grower's Processing Allocation using reasonable endeavours to obtain the maximum price available.

(k) If BOML markets and sells the olives attributable to the Grower's Farm and the processed olives attributable to the Grower's Processing Allocation under clause 4.3(j), then account to the Grower and if relevant the Custodian for the proceeds of such sale.

(l) If the Responsible Entity is not BOML, then pay or cause to be paid to BOML the "Barkworth" name license paid under clause 7.2.

5. Subject to complying with the conditions set out in clause 6 of the Management Agreement, Growers may elect to:

   (i) Carry out their own maintenance work

   (ii) Have their trees harvested separately

   (iii) Harvest their own trees, and

   (iv) Market their own olives.

6. The Management Agreement (at clause 7.1) makes the following provision for remuneration in the first year:

   (a) **for Growers who subscribe to the Project on or before 31 May 2001:**

   (i) In consideration of BOML carrying out its duties (as set out in clause 4.1 of the Management Agreement), BOML is entitled to be paid:

   - $90 for the supply of 20 olive trees to the Grower (payable on application).
   - $1,025 for irrigation works. Irrigation works consist of the supply and installation (above ground) of trickle tapes and sprinkler heads (together the "irrigation equipment") on the Grower's land (payable on or before 31 May 2001). The irrigation equipment is bought by BOML as agent for the Grower.
   - $2,558 for the performance of management duties under clauses 4.1 (c) - 4.1 (e) "preparation and planting fees" (payable on or before 31 May 2001).

- $2,050 for the performance of the following management duties until 30 June 2002,

  (a) $1,175 for procuring, processing, packaging and marketing olives attributable to the Grower's Farm or sourced externally.

  - $875 for the balance of the management duties listed in clause 4.1.

(ii) BOML is also entitled to be paid $500 for the use of the Barkworth name in carrying on the Grower's business (payable on or before 1 July 2001).

(b) **for Growers who subscribe to the Project after 31 May 2001:**

(iii) In consideration of BOML carrying out its duties (as set out in clause 4.1 of the Management Agreement), BOML is entitled to be paid:

- $90 for the supply of 20 olive trees to the Grower (payable on application).
- $1,025 for irrigation works. Irrigation works consist of the supply and installation (above ground) of trickle tapes and sprinkler heads (together the "irrigation equipment") on the Grower's land (payable on the later of 1 July 2001 or two months after application). The irrigation equipment is bought by BOML as agent for the Grower.
- $4,608 for the performance of management duties from 1 July 2001 until 30 June 2002 (payable on the later of 1 June 2001 or two months after application, being

  (a) $2,558 for the performance of management duties under clauses 4.1 (c) - 4.1 (e) "preparation and planting fees".

  (b) $1,175 for procuring, processing, packaging and marketing olives attributable to the Grower's farm or sourced externally.

  (c) $875 for the balance of the management duties listed in clause 4.1.

(iv) BOML is also entitled to be paid $500 for the use of the Barkworth name in carrying on the Grower's business (payable on the later of 1 July 2001 or two months after application).

(v) In addition to the fees set out in clauses 7.1(a)(i) to 7.1(a)(ii), if BOML procures and markets processed olive products on behalf of the Grower, then BOML is entitled to be paid 85% of the amount by which the gross proceeds from the sale of the processed olive products exceed prospectus projections. From this fee BOML must pay all costs associated with procuring and marketing processed olive products.

7. The Management Agreement (at clause 7.2) makes the following provision for remuneration in the second year:

(i) In consideration of BOML carrying out its duties from 1 July 2002 to 30 June 2003, BOML is entitled to be paid:

- $1,175 for procuring, processing, packaging, and marketing olives attributable to the Grower's farm or sourced externally; and
- $875 for the balance of the duties listed in clause 4.3.
- The Grower must pay these fees, which total $2,050, on or before 1 July 2002.

(ii) BOML is also entitled to be paid $500 in year two for granting the Grower a license to use the "Barkworth" name in carrying on the Grower's business. The fee is payable from the gross income generated from the sale proceeds generated under the Management Agreement. The fee for the license to use the "Barkworth" name is capped at the amount of gross income generated from the sale proceeds generated under the Management Agreement.

(iii) In addition, if BOML procures and markets processed olive products on behalf of the Grower, then BOML is entitled to be paid 85% of the amount by which the gross proceeds from the sale of the processed olive products exceed the prospectus projections. From this fee, BOML must pay all costs associated with procuring and marketing processed olive products.

8. The Management Agreement makes the following provision for remuneration in the third year:

(i) In consideration of BOML carrying out its duties for the third year of the Management Agreement, BOML is entitled to be paid 70% of the gross income generated from the sale of processed olives attributable to the Grower's processing allocation.

(ii) Payment of the above fees includes a fee to use the "Barkworth" name in carrying on the business of the Grower. The amount of that fee is the amount paid under year two increased by the same proportion as the increase in the Consumer Price Index over the one-year period from year two to year three. If there is insufficient income earned from the sale of processed olives to pay this amount, the fee is capped at the income earned.

(iii) In addition, if BOML procures and markets processed olive products on behalf of the Grower, then BOML is entitled to be paid 85% of the gross proceeds from the sale of the processed olive products. From this fee BOML must pay all costs associated with procuring and marketing processed olive products.

9. The Management Agreement makes the following provision for remuneration in the fourth and following years:

(i) In consideration of BOML carrying out its duties under clause 4.3 for the fourth year and all subsequent years, BOML is entitled to be paid fees calculated according to the following table

Year No.	% of Gross Income of Olives	% of Gross Income of Processed Olives
4	90%	70%
5	90%	70%
6	60%	70%
7	50%	70%
8 to 20	40%	70%

(ii) In the above table, "Gross Income of Olives" means the gross income generated from the sale of olives attributable to the Grower's Farm, and "Gross Income of Processed Olives" means the gross income generated from the sale of processed olives attributable to the Grower's Processing Allocation.

(iii) The fees payable are calculated in respect of the olives attributable to the Grower's Farm which are produced during the year corresponding with the percentage of gross income of olives.

(iv) If the Grower has made an election to have his or her trees harvested separately or to harvest the trees themselves such that the gross income of olives is not readily calculable by BOML, the fees payable in consideration of BOML carrying out its management duties under clause 4.3 of the Management Agreement are as per the fees in the following table plus or minus an adjustment.

Year No.	Management Fees $
4	369
5	538
6	565
7	659
8	692
9	850
10	1,042
11	1,094
12	1,149
13	1,206
14	1,266
15	1,330
16	1,396
17	1,466
18	1,539
19	1,616
20	1,697

(v) That adjustment will be that amount actually paid in respect of Farms owned by Growers who have not made the election. The adjustment will be credited or charged to the Grower upon it being calculated by BOML.

(vi) If the Grower has made an election to market his or her own processed olive products, fees payable to BOML for duties carried out under clause 4 of the Management Agreement will be the sum of the percentage of gross income of olives plus additional fees in respect of sourcing, processing, and related activities as set out below subject to adjustment in respect of years 3 to 20.

Year No.	% of Gross Income of Olives	Additional Fees for Sourcing/Procuring
1	-	0
2	-	500
3	-	1,388
4	90%	2,107
5	90%	2,592
6	60%	2,723
7	50%	2,859
8	40%	3,002
9	40%	3,150
10	40%	3,308
11	40%	3,473
12	40%	3,647
13	40%	3,830
14	40%	4,021
15	40%	4,224
16	40%	4,436
17	40%	4,659
18	40%	4,893
19	40%	5,139
20	40%	5,396

10. The projected cashflows for Growers from the operation of a minimum holding of 250 "E" Class shares in BOGL, if BOML is appointed manager, are as follows:

Investing on or before 31 May 2001

Year	Net Project Income
2001	(3,673)
2002	(2,863)
2003	(1,965)
2004	416
2005	632
2006	777
2007	1,099
2008	1,385
2009	1,765
2010	2,008
2011	2,294
2012	2,409
2013	2,530
2014	2,656
2015	2,789
2016	2,929
2017	3,075
2018	3,229
2019	3,391
2020	3,562
2021	3,740

Investing after 31 May 2001

Year	Net Project Income
2001	(90)
2002	(6,446)
2003	(1,965)
2004	416
2005	632
2006	777
2007	1,099
2008	1,385
2009	1,765
2010	2,008
2011	2,294
2012	2,409
2013	2,530
2014	2,656
2015	2,789
2016	2,929
2017	3,075
2018	3,229
2019	3,391
2020	3,562
2021	3,740

11. The Prospectus states that the total net investment (over a period of two years) in respect of each interest for a member electing to have BOML manage the interests, is $9,136 including the 250 x $1 shares in BOGL. After that time it is projected that all costs will be met from revenue the project will generate.

12. Growers will be exposed to the normal risks of any commercial enterprise; some of which will be covered by insurance taken out by BOML.

13. This Ruling does not consider or rule on the taxation implications of financing arrangements (if any) entered into by Growers in order to invest in this Arrangement.

Assumptions made by the Commissioner

This Ruling is made subject to the following assumptions:

i) Growers are liable for any repairs to or enhancement of the irrigation equipment required during the life of the project.

ii) Growers will participate in the project for the full 20 years (until 2021) and have an intention to make a profit from investing in the Arrangement.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

Balance date

a) This Ruling applies only to New Zealand resident taxpayers.

b) The balance date of any Grower for the purposes of Australian income tax, is 30 June.

c) Any foreign source income and foreign expenditure that arises in respect of any Grower's investment in BOGL has been included in the Grower's annual returns of income in Australia.

d) No foreign source income, nor foreign expenditure arising from the investment in BOGL, has been included in the Grower's income tax return for the base year.

e) Any dividends received from BOGL are to be returned when derived and not in accordance with section EP 1.

f) The total net foreign source income (derived from all foreign activities) of the Grower is less than $100,000.

g) The income derived and expenditure incurred by the Grower from the sale of raw olives and processed olive products is not income derived or expenditure incurred under the "accrual rules".

h) The shares in BOGL do not give rise to any "attributed foreign income" as defined in section OB 1.

i) The shares in BOGL do not give rise to "foreign investment fund income" as defined in section CG 16.

j) BOGL is not a "controlled foreign company" as defined in section CG 4.

Factory access fees; procuring, processing and marketing fees; and brand name licensing fees

k) The "year one" factory access fee is payable in respect of the year ending 30 June 2002.

l) The factory access fee; the procuring, processing and marketing fee; and the brand name licensing fee are all set at an arm's length rate.

m) In the year ending 30 June 2002, BOML processed olives on behalf of Growers using a part, or all of, their annual allocation of factory access time for the year ended 30 June 2002.

n) The "year one" procuring, processing and marketing fee is payable in respect of the year ended 30 June 2002.

o) In the year ending 30 June 2002, BOML procured and processed olives on behalf of Growers.

p) The "year one" brand name licensing fee is payable in respect of the year ending 30 June 2002.

q) In the year ending 30 June 2002, Growers used the brand name "Barkworth" for marketing and selling olives and olive products.

Irrigation equipment

r) Growers acquire legal and beneficial ownership of the irrigation equipment by virtue of the $1,025 payment.

s) Growers have not elected to treat the right to use the irrigation equipment as low value property under section EG 16.

t) Growers have not been allowed a deduction in respect of the irrigation equipment under any of sections BD 2(1)(b)(i) and (ii), DJ 6, DJ 11, DL 6, DM 1, DO 3, DO 6, DO 7, DZ 1, DZ 3, EO 5, EZ 5, and EZ 6, or by virtue of an amortisation or other similar deduction allowed under any section of the Act.

u) Growers are not entitled to receive compensation for any decline in the value of the right to use the irrigation equipment.

v) No other taxpayers have been allowed a deduction for the right to use the irrigation equipment.

w) Growers have not elected to treat the property as not depreciable under section EG 16A.

x) Growers have not elected to treat the right to use the irrigation equipment as a financial arrangement under section EH 25.

General

y) The financial projections contained in Prospectus No. 5 demonstrate genuine and commercially achievable rates of return.

z) If BOML contracts with itself, under clause 5.2 of the Management Agreement, then it will do so on an arm's length basis.

How the Taxation Laws apply to the Arrangement

Subject in all respects to any assumption or condition stated above, the Taxation Laws apply to the Arrangement as follows:

- Growers may make an election under section EP 1 to use a foreign tax balance date.
- The cost of acquiring shares in BOGL is a capital expense and not deductible by virtue of section BD 2(2)(e).
- The cost of acquiring olive trees is a capital expense and not deductible by virtue of section BD 2(2)(e).
- The Preparation and Planting Fee is a capital expense and not deductible by virtue of section BD 2(2)(e).
- The annual Farm Administration Fee payable to BOGL is deductible under section BD 2(1)(b)(i).
- The payment of the annual Factory Access Fee is deductible under section BD 2(1)(b)(i).
- The annual Procuring, Processing, Packaging and Marketing Fee is deductible under section BD 2(1)(b)(i).
- The annual Brand Name Fee is deductible under section BD 2(1)(b)(i).
- The irrigation equipment is "depreciable property".
- The $1,025 payment for the irrigation equipment is depreciable under section EG 1.
- Section DB 1 does not preclude Growers who are not registered or liable to be registered for Australian GST from claiming a deduction in New Zealand for the GST inclusive amount.

The period or income year for which this Ruling applies

This Ruling will apply for the period 1 July 2001 until 30 June 2004.

This Ruling is signed by me on the 18th day of June 2003.

Martin Smith
General Manager (Adjudication & Rulings)

NEW LEGISLATION

SCREEN PRODUCTION INDUSTRY – WITHHOLDING PAYMENTS

From 8 September 2003 payments to independent contractors engaged in the film production industry will be subject to a withholding payment tax deduction of 20 cents in the dollar.

The new withholding tax rate applies to payments relating to television, video, or film productions or presentations and includes work commonly involved in the on-set and off-set pre-production, production and post-production processes. The rate will not apply to salary and wages paid within the industry, which continue to be subject to PAYE in the normal way.

A new class of withholding payment overrides all other classes of withholding tax that might apply to workers within the screen production industry, including free-lance journalists and writers.

The new rate of 20 cents in the dollar is consistent with withholding tax rates applying to payments to resident and non-resident entertainers. Having only one rate of withholding tax applying to all independent contractor payments will simplify tax practices for the screen production industry.

The change was approved by Order in Council on 4 August 2003.

Income Tax (Withholding Payments) Amendment Regulations 2003/Number186

LEGISLATION AND DETERMINATIONS

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

DETERMINATION: AMOUNT OF A SPECIFIED WITHHOLDING PAYMENT (BEING PER DIEM ALLOWANCES PAID IN THE SCREEN PRODUCTION INDUSTRY) THAT SHALL BE REGARDED AS EXPENDITURE INCURRED IN PRODUCTION OF PAYMENT

Introduction

This Determination sets out the amount regarded as expenditure incurred in the production of specified withholding payments when those payments are per diem (per day) allowances paid to resident and non-resident contractors and resident and non-resident entertainers working in the Screen Production Industry in New Zealand.

Section NC 2 of the Income Tax Act 1994 requires anyone who makes a source deduction payment to deduct tax when making it.

Under section OB 2 (1) of the Income Tax Act 1994 a withholding payment is included in the definition of "source deduction payments". Consequently, any person who makes a withholding payment must deduct tax from it at the time it is made, unless an exemption applies.

The Screen Production Industry pays per diem allowances to resident and non-resident contractors and resident and non-resident entertainers working on screen productions when they are working away from their town of normal residence. These allowances are to cover the costs of breakfast, lunch and dinner as well as other minor incidental expenses incurred by a contractor or entertainer while working in the Screen Production Industry in New Zealand.

Money paid to resident and non-resident contractors and resident and non-resident entertainers working in the Screen Production Industry in New Zealand, comes within the definition of "withholding payment" in the Income Tax (Withholding Payments) Regulations 1979, so section NC 2 applies.

Therefore per diem allowances come within the definition of "withholding payment" in the Income Tax (Withholding Payments) Regulations 1979 and the Regulations require withholding tax to be deducted from such payments.

Regulation 7 of the Income Tax (Withholding Payments) Regulations 1979 allows the Commissioner to determine an amount or proportion of any specified withholding payment that is considered to be expenditure incurred in the production of that payment. If the Commissioner has made such a determination, the person paying the specified withholding payment is only required to deduct tax from the amount of the withholding payment that exceeds this threshold.

Application

This Determination applies to payments of per diem allowances made to resident and non-resident contractors and resident and non-resident entertainers in the Screen Production Industry. It applies:

- to per diem allowances paid on or after 1 September 2003,
- where the contractor or entertainer is working away from their town of normal residence,
- except where any resident or non-resident contractor, or any resident or non-resident entertainer is also provided with the goods and services for which the allowance is paid by the payer or another party acting on the payer's behalf,
- unless a specific Regulation 7 determination has been issued by the Commissioner in relation to the per diem allowances in question, and
- until the Commissioner varies or revokes this determination.

Interpretation

In this Determination, unless the context otherwise requires, expressions have the same meaning as in the Income Tax (Withholding Payments) Regulations 1979 and sections NC 2 and OB 2(1) of the Income Tax Act 1994.

Determination

Where any resident or non-resident contractor, or resident or non-resident entertainer receives a per diem allowance in relation to services provided to a screen production and that allowance is a withholding payment, the sum of $60 per day shall be regarded as expenditure incurred in the production of the withholding payment. If the allowance is less than $60 per day, the total amount of the allowance shall be regarded as expenditure incurred in the production of the withholding payment.

However, to the extent that the resident or non-resident contractor, or resident or non-resident entertainer is also provided with the goods and services for which the allowance is paid, either by the payer or another party acting on the payer's behalf, then the amount that will be exempted by operation of this Determination from the application of the Income Tax (Withholding Payments) Regulations 1979 shall be reduced on a pro rata basis.

This Determination is made by me, acting under delegated authority from the Commissioner of Inland Revenue under section 7 of the Tax Administration Act 1994.

This Determination is signed on the 8th day of August 2003.

David Kelly
Manager
Resources Sector
Corporates

Examples

1. Contractor/entertainer receives a per diem allowance of $60 while required to work away from their town of normal residence. The cost of the goods and services for which the allowance is paid are incurred by the recipient. The payer does not have to deduct withholding tax because the total payment does not exceed $60 per day.

2. Contractor/entertainer receives a per diem allowance of $60. The contractor is working in their town of normal residence. As the contractor is working in their town of normal residence the determination does not apply. The payer has to deduct withholding tax from the per diem allowance of $60.

3. Contractor/entertainer receives a per diem allowance of $60. Contractor/entertainer is also provided with all meals while working, either on the set, or at some other location. The recipient has not incurred the expense so the determination doesn't apply. The payer has to deduct withholding tax from the per diem allowance of $60.

4. The payer provides goods and services to the value of $15 per day to the contractor/entertainer. Therefore the maximum amount that can be paid as a per diem to the contractor/entertainer without withholding tax being deducted, is $45 per day.

5. Contractor/entertainer receives a per diem allowance of $75. The cost of the goods and services for which the allowance is paid are incurred by the recipient. The payer has to deduct withholding tax from $15 of each daily payment as the payment exceeds the $60 threshold on a daily basis.

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.

FINANCIAL SERVICES EXEMPTION FOR CLUB MEMBERSHIP

Case: Gulf Harbour Development Ltd v CIR

Decision date: 27 June 2003

Act: Goods and Services Tax Act 1985

Keywords: exempt supply, financial services, equity security, composite supply, multiple supplies

Summary

The supply of membership shares in a golf and country club was held to be an exempt supply for GST purposes because it was the supply of an equity security.

Facts

Gulf Harbour Development Ltd ("GHD Ltd") is the representative member of a group of companies which includes Gulf Harbour Holdings Limited, Gulf Harbour Country Club Holdings Limited ("Holdings") and Gulf Harbour Country Club Limited ("Country Club Ltd").

In March 1996, Country Club Ltd sold membership shares to Holdings in consideration for Holdings agreeing to pay all of the costs associated with the development of a golf and country club (Gulf Harbour Country Club: "the Club"). The shareholding in Country Club Ltd comprises fully paid up $1 ordinary shares and fully paid redeemable preference shares ("RPS's"). It is the RPS's that are the membership shares in issue.

Holdings issued a prospectus for the sale to the public of the membership shares in Country Club Ltd. Each membership share is issued for a fixed term of just over 75 years, all memberships expire on 31 March 2073. On that date, each membership share will be redeemed for $1 and all rights attaching to each share will cease.

There are three types of membership shares (individual, restricted and corporate) with obligations and restrictions attaching to each type. All holders of membership shares are required to pay annual subscriptions; and have no entitlement to participate in dividends or distributions of any type (except on liquidation), or to vote or attend any company meetings (except where members' interests are directly affected), or to participate in the company's management and operations (except as described in the prospectus in relation to the establishment and operation of the Club Committee).

The Club board may impose a penalty, fine or suspend rights to use the Club facilities or any other rights attaching to the relevant membership share if holders fail to comply with the obligations and restrictions of that membership share. The Club board may also cause Country Club Ltd to forfeit a holder's membership shares in the case of insolvency, criminal conviction, ceasing to be of good character or failing to comply with the obligations or restrictions of the membership share or with the Club rules.

GST Treatment

Country Club Ltd did not charge GST in respect of the sale of membership shares to Holdings, and Holdings did not receive an input tax credit in respect of that sale.

Holdings did not charge GST on the sale of the membership share to the public because Holdings believed that the on-sale of the membership shares was an exempt supply for GST purposes.

The Commissioner contended that the supply was a composite supply of club membership. Alternatively, the Commissioner contended if the supply was not a composite supply, then there were multiple supplies consisting of an equity share (exempt supply) and a club membership (taxable supply).

GHD Ltd contended there was a single supply of the membership shares and the consideration paid was for shares and not the membership rights.

The issue was whether the supply of membership shares in a golf and country club were an exempt supply for GST purposes, by reason of being the supply of financial services in the form of either equity securities or participatory securities.

Decision

Baragwanath J found the supply of membership shares was the supply of an equity security, and therefore exempt for GST purposes. Because His Honour found this was an equity security, it was not necessary for him to consider the arguments pertaining to participatory securities.

His Honour identified some of the features of membership (at paragraphs 5, 11-21 and 45), but stated:

> …there was no evidence to support the supply of more than the shares; the right to membership passed not as a discrete element but as an incident of share ownership.
>
> At paragraph 4, pg 3

Baragwanath J considered the rights attached to each share and passing to the purchaser include membership of the Club:

> The transfer of the member share carries with it the entire bundle of rights which include entitlement to use the Club facilities including the golf course. That bundle of rights may be described as entailing membership of the Club. But such membership rights inhere in the personal property comprised in the share which is "a share in the capital of a body corporate". That is Parliament's definition of what falls within the exemption. There is no occasion to look beyond it.
>
> At paragraph 79, page 32

His Honour found that, in terms of the definition of equity security, holders of membership shares became entitled to an interest in or right to share in the capital of the body corporate.

Baragwanath J posited the issue in several forms, including:

> A lay response to [the] enquiry what was being supplied might be, as the Commissioner submits, that it was membership of the Club provided through the vehicle of a share transfer. A lawyer's response might be, as the plaintiff argues, that it was a chose in action in the form of a share that carries with it a bundle of legal rights which include the right to access to Club facilities. Each is correct in fact. The issue is which is correct in law.
>
> At paragraph 33, page 15

His Honour stated, in distinguishing *Court Barton Property plc v Customs & Excise Commissioners* (1985) VATTR 148:

> To characterise the present class of transaction as the supply of country club facilities rather than as a share sale would infringe the most fundamental principle—of a company's distinct entity—of the corporate law which Parliamentary counsel, by their reference to the shares exception, have been at pains to adopt.
>
> At paragraph 62, pp 25-26

His Honour traversed the English authorities before him, and also made comment on the substance and reality test, affirming that in New Zealand, the test as to the true nature of a transaction is to be ascertained by considering the legal arrangements actually entered into and carried out.

The Commissioner has filed an appeal of the decision in the Court of Appeal.

TAX AVOIDANCE GST ACT

Case: TRA 019/2003

Decision date: 18 July 2003

Act: GST Act 1985

Keywords: Section 76 Tax avoidance arrangement,

Summary

This case arose because a property /housing developer attempted to take advantage of GST timing differences between the invoice and payments basis which would enable the disputant to claim input tax credits without having to return the output tax credits for some 20 years. The effect of this arrangement was to use public money to fund the development of $80 million worth of property. This case provides precedent for section 76 of the GST Act.

Facts

On 5 November 1998, the Disputant entered into conditional agreements with 114 companies (the A Group of companies) by which it would purchase from each a section of land in a subdivision in which the vendor had contractual rights as a conditional purchaser from the developer, W Developments Limited.

Each agreement provided for a purchase price of $70,000, with a deposit of ten dollars to be held by the vendor's solicitor as stakeholder, with no other money due until settlement.

On 21 May 1999, the A Group of companies entered into agreements to sell all 114 sections to the taxpayer. The total value of these transactions exceeded $80,000,000.

All agreements had deferred settlement dates, which in general ranged between 10 and 20 years after each agreement was entered into.

Each agreement provided for a deposit of $30,000, payable by an initial deposit of ten dollars on execution of the agreement with the balance of $29,990 payable on the later of 20 August 1999 or such other date agreed by the parties. The disputant has paid the initial $10 deposit on each transaction, but nothing more.

Each agreement used the standard form. The form provides that deposits are held by the recipient as stakeholder until the agreement becomes unconditional. This clause was deleted from all agreements.

Each agreement provided for the relevant A Group company to construct a house to an agreed plan and specification prior to settlement. The agreed purchase price for each contract reflected the improved value of each section, and the projected market value at settlement.

The disputant registered for GST on an invoice basis, and the A Group of companies were registered on a cash basis. This meant an input tax deduction could be claimed by the disputant immediately, but the A Group of companies would not be required to account for GST on each transaction until settlement funds were received.

In the GST period ended 31 May 1999, the disputant claimed the input tax credits on the purchase of 13 properties. Three of these were existing houses, and the others were Dominion Road properties. The value of supply of each property for GST purposes was the market value of the property at the time the agreement was entered into.

This method of valuing the supply was based on the agreements for sale and purchase being credit contracts, in terms of a binding private ruling issued by the Commissioner on 15 June 1999. The ruling was to the effect that each agreement for sale and purchase was a credit contract, and thus pursuant to section 10(5) of the GST Act, the value of the supply was the "cash price" as that term is defined in the Credit Contracts Act 1981.

In the GST period ended 31 July 1999, the disputant claimed input tax credits on the purchase of 104 properties. Unlike the method used in the period ended 31 May 1999, which followed the private binding ruling, the supplies were valued according to the purchase price specified in each agreement for sale and purchase. This method meant the total input credit claimed was nearly $9,000,000 instead of just over $3,000,000.

Extracts from the judgment

4. Summary of Evidence

The judgment goes through the evidence presented in significant detail at paragraphs 23-100.

The TRA accepted that the disputant was part of a scheme conceived that would enable the disputant being registered on the invoice basis to obtain substantial refunds of GST consequent on the purchase of the 114 properties. Further, the sale and purchase agreements were structured so that the vendor (the A Group of companies) would not be required to give possession for up to 20 years in the future. In the meantime, the vendors contracted with building companies to develop dwellings on the land.

The price of the property which the disputant agreed to pay on settlement included an agreed sum for the value of all the improvements adjusted upwards to accommodate expected increases in the price of such properties. The GST refund claimed is based on this adjusted figure for the land and buildings payable to the disputant in the GST periods in which the tax invoices are issued.

The 114 vendors being registered on a payments basis are not required to pay output tax until they receive payment for the properties from the disputant. This would not occur until the agreed settlement date in each case.

This allows the disputant the timing advantage of the use of the GST input refunds to pay the deposits on each agreement to the relevant company in the A Group. The A Group then have the funds to complete the purchase of the sections from W Developments Ltd, and along with mortgage finance embark on the building of the houses to fulfil the contracts with the disputant.

The TRA further comments that without the lengthy period of mismatch between the GST input refund and any output liability, the scheme is incapable of execution, essentially amounting to the use of public revenues for periods of up to 20 years.

5 Credit Contract

The TRA held that there is no element of loan in this case and that the agreements were not credit contracts for the purposes of either the Credit Contracts Act or the GST Act.

6 Section 25(4) GST Act

The TRA covers this at paragraphs 120-141 of the judgment. Inland Revenue considers the result is correct on the cancellation issue. The TRA held:

> "GST is a tax on supplies of goods and services embodied in specific transactions. In this case 114 agreements for sale and purchase of land. Where the agreements are between registered persons, as here, section 25(4) provides that if the contract the subject of the input claim is cancelled, then the purchaser must refund to the Commissioner any input refund paid to the extent that the amount of the refund exceeds the amount of the output tax payable on the transaction. Hence there is no output tax payable at the time of supply, and therefore the full amount of the input which would have been payable to the purchaser had the contracts not been cancelled must be repaid to the Commissioner or foregone by the purchaser if the refund has not actually been made. See TRA decision 003/2003 judgment 26 February 2003".
>
> "In coming to this view I do not overlook the fact that the disputant paid a $10 deposit in respect of each contract. That is not a supply for the purposes of the GST Act. The contracts are not divisible into equitable and legal estates. The "supply" is for all the rights in the plot land contracted for. Once it is clear that the vendor cannot perform its bargain to convey those rights, then section 25(4) supervenes to in effect cancel out any GST refund entitlement of the purchaser. **See TRA decision 005/2003 judgment 12 March 2003**".

At paragraphs 135 – 139, the TRA discusses the relevance of section 25.

> "This argument overlooks section 25. It applies not only to contracts which have been cancelled but to those where *"The nature of that supply of goods and services has been fundamentally varied or altered."*
>
> Clearly that is the case here. The nature of the supply to the disputant has been altered by the fact that to make it good the vendor must seek to repurchase all of the 114 contracts, because it is all of them which are the subject of the two GST returns.
>
> That of itself is a *"fundamental alteration"*. Equally, if the vendor is successful in repurchasing only some of the properties, then the disputant will not be entitled to claim the GST input refunds it has. It will require amended returns (if that is possible) and they will be assessed according to their own merits depending upon the precise terms of any renegotiated contracts for supply. The amended s.76 will then no doubt become relevant".

7 Section 76

This case applies section 76. The TRA begins by summarising the circumstances in which the arrangement arose. The TRA accepts that:

- The arrangements were carefully designed to take advantage of the mismatch between registration on an invoice and payments basis;
- The centrality to the scheme of the need for the disputant to secure GST refunds on purchases of $80 million of land where a small company with no assets or income would seek such no doubt experienced advice, or that some other entity which hoped to profit from the scheme would do so on its behalf;
- The fundamental objective of the scheme was to extract $80 million from the CIR in the form of GST on the purcahse of the 114 properties.

Application of section 76

The TRA succinctly finds there is an "arrangement" and that it is "between persons" (paragraphs 160-170).

The judgment goes into more detail on the intent to defeat the intent and application of the Act. It attempts to distinguish income tax avoidance and GST avoidance on the basis that with regard to income tax, the taxpayer is always endeavouring to establish that the transaction should not be brought to tax, and the CIR that it should. Where there is a GST avoidance arrangement, the taxpayer is trying to escape paying output tax while being granted the input credit.

The TRA recognises that (paragraphs 190-192) "the Courts have held that the intent of the Act in relation to outputs and inputs is expressed in unequivocal terms. There is no matching symmetry between payment of output tax and deduction of input tax. Each occurs at the time and in the GST period allowed for by the Act, and at no other time.

This series of transactions has been structured in such a way so as to ensure that the relevant provisions of section 20 apply. There is a liability on the vendor to pay output tax and there is an entitlement on the part of the purchaser to claim an input tax refund. The problem for the revenue base is that it will be many years before the liability to pay the output tax crystalises and in the meantime the disputant being one of the parties to the overall "plans" will have the use of the inputs and in that way make the whole series of arrangements financially possible.

This however in my view is an irrelevant consideration. What the disputant taxpayer does with money it receives by way of an input deduction is entirely a matter for it".

Subjective

Significantly, the TRA finds that it is the intentions of the parties at the time the arrangement is entered into which is crucial and that is a **"wholly subjective matter".**

In deciding what were the subjective intentions of the parties to the transaction it will be necessary to look at all relevant circumstances. Each case will turn on its own facts, but conventionally one would enquire into:

(a) The relationships of the parties. Are they strictly at arms length, or is there a degree of premeditated collusion in the design of the arrangement?

(b) The significance to the transaction of the GST consequences under consideration.

(c) Whether the arrangement is explicable in ordinary commercial terms if the contested GST component is abstracted.

(d) In what way the arrangement defeats the particular intent and application of the GST Act which is relevant to the facts.

(e) The identity, relevant experience and financial probity of the parties as that touches on their ability to perform their side of the bargain without the benefit of the contested GST component.

Viewed in this way the impugned transactions fail on every count. Thus:

(a) The relationships between Mr A and the original proprietor of the disputant company were more social than commercial. The company which she formed was to be no more than a conduit for obtaining the GST input refunds.

(b) The arrangement was entirely dependent on obtaining the GST inputs. The disputant had no ability to pay for any of the land purchased from its own resources. Similarly with the input refunds the A Group of companies had no ability to finance the purchase of the sections which they onsold to the disputant.

(c) If one removes the input refund from the equation the arrangements are wholly inexplicable in commercial terms. They could not and did not come to fruition.

(d) This arrangement defeats the intention of the Act to tax transactions at the time they are entered into by exploiting the mismatches which the Courts have found to exist between payment based and invoice based taxpayers. That served to prevent the application of the Act by denying on the one hand the Crown the revenue which the Act was designed to exact, and on the other, requiring the Crown to disgorge public monies for private use.

(e) The disputant's original proprietor had no relevant business experience, and no resources remotely capable of meeting the financial obligations undertaken. It is inconceivable that any lending institution would have funded the disputant's purchase of $80,000,000 worth of property given the identity, business experience and financial standing of the original proprietor of the disputant company, and the assets of that entity.

REGULAR FEATURES

DUE DATES REMINDER

September 2003

5 **Employer deductions and employer monthly schedule**

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345)* or *(IR 346)* form and payment due
- *Employer monthly schedule (IR 348)* due

22 **Employer deductions**

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345)* or *(IR 346)* form and payment due

Employer deductions and employer monthly schedule

Small employers (less than $100,000 PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345)* or *(IR 346)* form and payment due
- *Employer monthly schedule (IR 348)* due

30 **GST return and payment due**

October 2003

6 **Employer deductions and employer monthly schedule**

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345)* or *(IR 346)* form and payment due
- *Employer monthly schedule (IR 348)* due

20 **Employer deductions**

Large employers ($100,000 or more PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345)* or *(IR 346)* form and payment due

Employer deductions and employer monthly schedule

Small employers (less than $100,000 PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345)* or *(IR 346)* form and payment due
- *Employer monthly schedule (IR 348)* due

FBT return and payment due

31 **GST return and payment due**

These dates are taken from Inland Revenue's Smart business tax due date calendar 2002 - 2003

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