TAX INFORMATION BULLETIN

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CONTENTS

Get your TIB sooner on the internet 2

This month's opportunity for you to comment 3

Binding rulings

Public Ruling – BR PUB 03/05 5

Public Ruling – BR PUB 03/06 11

Product Ruling – BR PRD 03/13 20

New legislation

Tax implications of the Wool Board restructuring – Wool Industry Restructuring Act 2003 28

Fringe benefit tax – Prescribed rate of interest on low-interest, employment-related loans 30

Screen industry – withholding payments 30

Regular features

Due dates reminder 32

Your chance to comment on draft taxation items before they are finalised 34

This TIB has no appendix

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This *Tax Information Bulletin* is also available on the internet in PDF format. Our website is at **www.ird.govt.nz**

It has other Inland Revenue information that you may find useful, including any draft binding rulings and interpretation statements that are available.

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THIS MONTH'S OPPORTUNITY FOR YOU TO COMMENT

Inland Revenue produces a number of statements and rulings aimed at explaining how taxation law affects taxpayers and their agents.

Because we are keen to produce items that accurately and fairly reflect taxation legislation, and are useful in practical situations, your input into the process—as perhaps a "user" of that legislation—is highly valued.

The following draft items are available for review/comment this month, having a deadline of 31 October 2003.

Ref.	Draft type	Description
ED0030	Standard practice statement	Section 17 notices
ED0047	Questions we've been asked	Qualifying trusts – Income tax underpayment

Please see page 34 for details on how to obtain a copy.

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).

You can download these publications free from our website at **www.ird.govt.nz**

ASSOCIATED PERSONS TEST – TIMING IN RELATION TO GROSS INCOME DERIVED FROM THE SALE OR OTHER DISPOSITION OF LAND

PUBLIC RULING – BR PUB 03/05

Note (not part of ruling): This ruling replaces public ruling BR Pub 00/05 which was published in *Tax Information Bulletin* Volume 12, No 7 (July 2000). BR Pub 00/05 applied until 30 June 2003. This ruling is essentially the same as BR Pub 00/05. Its period of application is from 1 July 2003 to 30 June 2008.

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 paragraphs (b), (c), and (d) of section CD 1(2).

The Arrangement to which this Ruling applies

The Arrangement is the sale or other disposition of land by a taxpayer who is associated with another person.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

- For the purposes of determining whether any amount derived from the sale or other disposition of land is included in the gross income of any taxpayer by virtue of paragraphs (b) to (d) of section CD 1(2), the test of whether a taxpayer and another person are associated persons is applied only at the time of the acquisition of the land. The test of association is not applied at the time of the sale or other disposition of the land.

The period for which this Ruling applies

This Ruling will apply for the period from 1 July 2003 to 30 June 2008.

This Ruling is signed by me on the 14th day of August 2003.

Martin Smith
General Manager (Adjudication & Rulings)

COMMENTARY ON PUBLIC RULING BR PUB 03/05

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusion reached in Public Ruling BR Pub 03/05 ("the Ruling").

Background

Paragraphs (b) to (d) of section CD 1(2) include within the gross income of a taxpayer any amounts derived from the sale or other disposition of land if the taxpayer, or any other person associated with the taxpayer, carried on certain businesses at the time the land was acquired.

For the purposes of section CD 1, associated persons or persons associated with each other are defined in section OD 8(4). The Ruling confirms that the test of association under paragraphs (b) to (d) of section CD 1(2) applies at the time the land is acquired. This question is important in general terms because in many cases a taxpayer may be associated with a person at the time of acquisition of land, but may not be associated with the person at the time of the sale or disposition of the land (and vice versa).

A number of commentators have expressed their view as to the timing of the test of association in section CD 1(2)(b) to (d), but there seems to be uncertainty as to the correct view. This uncertainty stems from the wording and tenses used. The Commissioner's view is, and always has been, that the test of association is applied at the time the land was acquired.

Legislation

Section CD 1(1) states:

Any amount derived from the sale or other disposition of any land, being an amount to which this section applies, is gross income.

Section CD 1(2) sets out the amounts that are included in the gross income of any person under section CD 1(1):

For the purposes of subsection (1), the gross income of any taxpayer includes the following amounts—

…

(b) Any amount derived from the sale or other disposition of any land where the taxpayer, or any other person where the taxpayer and that other person **are associated persons**, carried on, at the time the land was acquired, the business of dealing in land, and—

(i) That land, which was sold or disposed of by the taxpayer, was acquired by that taxpayer for the purpose of that business of dealing in land; or

(ii) That land was sold or disposed of by the taxpayer within 10 years after the date on which it was acquired by the taxpayer:

(c) Any amount derived from the sale or other disposition of any land where the taxpayer, or any other person where the taxpayer and that other person **are associated persons**, carried on, at the time the land was acquired, the business of developing or dividing land into lots, being development or division of the kind (not being work of a minor nature) referred to in paragraph (f), and—

(i) That land, which was sold or disposed of by the taxpayer, was acquired by that taxpayer for the purpose of that business of developing or dividing land into lots; or

(ii) That land was sold or disposed of by the taxpayer within 10 years after the date on which it was acquired by the taxpayer:

(d) Any amount derived from the sale or other disposition of any land, where the taxpayer, or any other person where the taxpayer and that other person **are associated persons,** carried on, at the time the land was acquired, the business of erecting buildings, and the taxpayer or that other person carried out, whether before or after the acquisition of that land by the taxpayer, any improvements, not being improvements of a minor nature, to that land (whether by way of erecting a building or otherwise); and

(i) That land, which was sold or disposed of by the taxpayer, was acquired for the purpose of that business of erecting buildings; or

(ii) That improved land was sold or disposed of by the taxpayer within 10 years after the date on which those improvements were completed.

... [Emphasis added]

Section OD 8(4) defines "associated persons or persons who are associated" for the purposes of section CD 1:

(4) In sections CD 1, FF 6, and GD 9, associated persons or persons associated with each other are—

(a) Any 2 companies where there is a group of persons—

(i) The aggregate of whose voting interests in each company is equal to or exceeds 50%; or

(ii) In any case where a market value circumstance exists in respect of either company, the aggregate of whose market value interests in each company is equal to or exceeds 50%; or

(iii) Who have control of both companies by any other means whatsoever; or

(b) A company and any person (other than a company) where—

(i) The person; or

(ii) Any spouse of the person; or

(iii) Any infant child of the person; or

(iv) Any trustee of a trust under which such person or spouse or infant child has benefited or is eligible to benefit,—

or any 2 or more of them have, when aggregated, a voting interest in the company equal to or exceeding 25% or, in any case where a market value circumstance exists in respect of the company, a market value interest in the company equal to or exceeding 25%; or

(c) Any 2 persons one of whom is the spouse or infant child of the other person, or is a trustee of a trust under which that spouse or infant child has benefited or is eligible to benefit; or

(d) A partnership and any person where that person is a partner in that partnership; or

(e) A partnership and any person, where that person and any partner in that partnership are, in accordance with this subsection, associated persons.

Application of the Legislation

Paragraphs (b), (c), and (d) of section CD 1(2) all use the same phrase to include in a taxpayer's gross income "Any amount derived from the sale or other disposition of any land where the taxpayer, or any other person where the taxpayer and that other person are associated persons, carried on, at the time the land was acquired, the business of …".

The question is raised as to whether the use of the words "are associated persons" means that in order for the provisions to be satisfied the test of association is applied:

- At the time of acquisition of the land by the taxpayer: eg this requires a person who carried on the business of dealing in land at the time the taxpayer acquired the land to have been associated with the taxpayer at the time the land was acquired (but that person would not necessarily be associated with the taxpayer at the time of disposition); or
- At the time of disposition: eg this requires a person who carried on the business of dealing in land at the time the taxpayer acquired the land to be associated with the taxpayer at the time the land was disposed of (but that person would not necessarily have been associated with the taxpayer at the time of acquisition); or
- At the time of acquisition and at the time of sale or other disposal: eg this requires a person who carried on the business of dealing in land at the time the taxpayer acquired the land to have been associated with the taxpayer at the time the land was acquired and also to be associated with the taxpayer at the time the land is disposed of.

Plain words

On an ordinary reading of the words of the legislation, it seems clear that the phrase "at the time the land was acquired" relates to the carrying on of the relevant business, rather than to the timing of the associated persons test.

However, it is not clear as to the point in time that the words "are associated persons" are referring to. The word "are" generally indicates a present tense and, therefore, arguably indicates that the test should be applied at the most recent point in time (ie the time of the disposal of the land). However, another reading of the words indicates that the test should be applied at the time of acquisition.

The meaning of the words without the presence of an associated person is clear:

- An amount will be gross income if:
  - a taxpayer derives that amount from the sale or other disposition of land,
  - the taxpayer was carrying on the relevant business when the land was acquired, and
  - the land was acquired for that business or sold within 10 years of acquisition.

There are three elements to the section. First, an amount must be derived from the sale or disposition of land. Second, the taxpayer must have been carrying on the relevant business at the time the land was acquired. Third, the land must have been acquired for that business or sold within 10 years.

Arguably the second element is the most important. The fact that the taxpayer was carrying on the relevant business at the time the land was acquired is central to the issue of the taxability of any amount derived on the sale of the land. For example, if the taxpayer were not carrying on a business of dealing in land, any amount derived would not be taxable under section CD 1(2)(b). However, if the taxpayer were carrying on such a business, any amount derived would be taxable if the land was either acquired for the business or sold within 10 years.

If the land was acquired for the purpose of a relevant business, it is logical that any amount derived from the sale of the land would be taxable. This is entirely consistent with the fact that any amount derived from a business is gross income under section CD 3. However, where the land was not acquired for the purpose of such a business, any amount derived would still be taxable if the land was sold within 10 years. In this situation, it is simply the fact that the taxpayer carried on the relevant business that leads to the inclusion of the amount derived within gross income. All acquisitions of land by the taxpayer are tainted by the existence of the business, regardless of whether the land is acquired as part of that business.

Now consider the effect of the section where an associated person is involved:

- An amount will be gross income of a taxpayer if:
  - the taxpayer derives that amount from the sale or other disposition of land,
  - an associated person of the taxpayer was carrying on the business of dealing in land when the taxpayer acquired the land, and
  - the land was sold by the taxpayer within 10 years of acquisition.

Again, there are three elements to the section. First, an amount must be derived from the sale or other disposition of the land. Second, an associated person of the taxpayer must have been carrying on the business of dealing in land when the taxpayer acquired the land. Third, the land must have been sold within 10 years of acquisition.

In a situation where an associated person is involved, the central focus of the section is even more clearly the fact that a relevant business, such as dealing in land, must have been carried on at the time the land was acquired. As it is the associated person who was carrying on the required business at the time of acquisition, the taxpayer could not have acquired the land for the purposes of the business. In these circumstances the amount derived will only be taxable if the land is sold within 10 years. It is only the existence of the business at the time of acquisition that allows the section to include the amount derived on sale in the taxpayer's gross income. The taxpayer is effectively tainted by the activities of the associated person at the time the land was acquired.

The section, therefore, is concerned with what was happening at the time the land was acquired – was an associated person of the taxpayer carrying on a business of dealing in land? It would seem that in these circumstances it is logical to argue that the associated person must have been associated with the taxpayer when the land was acquired. To separate the associated persons test from the test of the relevant business is an artificial interpretation of the section. Although the section is including in gross income amounts derived on sale, the focus of the section is on the activities of either the taxpayer or the associated person **at the time the land was acquired**.

The time of sale or other disposition of the land is certainly important in the context of section CD 1. The time of the sale of the land is the time at which the application of the section is triggered. However, once the application of the section is triggered by the sale of the land, the focus of the section is clearly on the activities which took place at an earlier time. The mere fact of the sale of the land is insufficient to include any amount derived from that sale in a taxpayer's gross income. The scheme and purpose of the provisions is not simply to bring to tax amounts derived on the sale of property. There must be some other relevant purpose or intention, some other relevant action on the part of the taxpayer or associated person, or some link with business activities, before any amount will be included in gross income.

However, as it is not completely clear on the plain reading of the words that the test is applied at acquisition, relevant case law should be considered.

The question as to the relevant time for testing association does not appear to have been directly considered by any New Zealand court. However, there is implicit support in some TRA cases for the view that the test of association is applied at the time the land was acquired.

For example, in *Case H92* (1986) 8 NZTC 630, the TRA considered whether the objectors were assessable on the profit made on the sale of land, A, under any of sections 65(2)(a) and 67(4)(a), (b) and (e) of the Income Tax Act 1976. On concluding that the objectors were not dealers in land at the time the land was acquired, the issue was then whether an associated company, P, was dealing in land when the relevant land was purchased by the taxpayer. The TRA found that the company's activities did not constitute the business of dealing in land at the time of purchase. Although the TRA did not specifically consider the time at which the parties needed to be associated, the judgment appeared to assume that this was at the time of acquisition. Bathgate DJ said (at page 642):

> The thrust of cross-examination of the objectors concerning P was to show that it was involved in erecting buildings **when A was purchased** by the objectors. **At that time** P and the objectors were associated persons for the purposes of section 67(4)(b) and (c). [Emphasis added]

Case T25 (1997) 18 NZTC 8,160 concerned whether a taxpayer was assessable on the proceeds of the sale of a commercial property. The question to be answered by the TRA was whether, on the date of acquisition by the objector of his interest in the commercial property, the objector carried on any business of developing or dividing land into lots or whether on that date any associated person of the objector (ie the CC Partnership or the R Syndicate) carried on such a business.

Although the timing of the test of association is not specifically referred to by Barber DJ, his Honour makes it clear that he considers the time of acquisition to be the appropriate time and he proceeds on that basis. When discussing whether the objector was a developer or subdivider as at the date of acquisition of the property, his Honour stated (at pages 8,174 – 8,175):

> However, as at 17 October 1978 only two relevant projects had been undertaken. One subdivisional project (of residential land) had been completed and the other was a building project so that, at that date, the objector could not be described as carrying on the business of developing or dividing into lots 'any land' and **nor was any associated person of the objector at that time**.
>
> I appreciate that the CC Partnership and the R Syndicate each commenced in 1974 and ended in late 1979; but on the crucial date, 17 October 1978, the nature of their activity did not offend section 67(4)(ba). [Emphasis added]

Barber DJ's statement that the CC Partnership and R Syndicate ended in 1979 impliedly gives strong support for the proposition that the time for the test of association is at acquisition. In this case the property in question was disposed of in 1988. In these circumstances, if the test of association were to be applied at the time of disposal the above comments by Barber DJ would have been irrelevant.

Notwithstanding the above statements, it is clear that the issue of the timing of the test of association was not argued in *Case H92* or *Case T25*. Case law, therefore, provides limited guidance on the interpretation of the words “are associated persons” in the context of land sales.

However, case law does indicate that one should be careful in the interpretation of tenses. The use of a tense may be decisive only if it is clear what the tense used relates to. For example, in *Maradana Mosque Board of Trustees v Mahmud* [1967] 1 AC 13, the Privy Council considered a provision that empowered the Minister to make a certain order if satisfied that a school “is being administered” in contravention of the Act. Counsel for the Minister argued that it was permissible to take account of the past running of the school. The Privy Council held that only the current method of administration at the time of the order could be considered.

By way of contrast, in *Norman v Simpson* [1946] 1 All ER 74 the United Kingdom Court of Appeal needed to interpret the words “have been” and concluded that the expression could be equated to “are” or “is” in the context before the Court. In that case the use of the words “have been” did not limit the Court to considering only the point in the past at which the sub-letting commenced. In relation to section CD 1(2), it can be argued that the use of the word “are” does not necessarily limit the inquiry to the present time and that it could be interpreted as operating in the past tense.

The approach of the courts has been that if the use of a tense is not clear or is ambiguous, other sources such as the statutory context and the scheme and purpose of the legislation will be used as aids in determining the correct interpretation. This approach is also consistent with the Court of Appeal’s approach to statutory interpretation set out in *CIR v Alcan New Zealand Ltd* (1994) 16 NZTC 11,175.

Section GD 9(1)

The associated persons test is used in many provisions of the Revenue Acts. Generally, these provisions are unhelpful for present purposes as it is obvious in most cases that the associated persons test relates to only one point in time. However, section GD 9(1) is relevant here because it is closely related to the provisions currently being considered. Section GD 9(1) deals with the situation where a person transfers land to an associated person some time after acquisition.

Section GD 9(1) is in the nature of an anti-avoidance provision, and applies where land is transferred from a “transferor” to a “transferee” and the transferor and the transferee “are associated persons”. If the transferee later sells or otherwise disposes of the land, any amount derived from the transaction is gross income of the transferee if that amount would have been gross income of the transferor under section CD 1(2).

Section GD 9(1) states:

Where—

(a) Any land has been transferred from any person (the “transferor”) to any person (the “transferee”); and

(b) The transferor and the transferee are associated persons; and

(c) The transferee subsequently sells or otherwise disposes of that land and the consideration from that sale or disposition exceeds the cost of the land to the transferee; and

(d) If, had the transferor not transferred the land to the transferee but instead had sold or otherwise disposed of the land for the consideration referred to in paragraph (c), that consideration would have been gross income of the transferor under section CD 1 –

that consideration shall be deemed to be gross income of the transferee under section CD 1.

Thus, section GD 9(1), like section CD 1(2), also uses the phrase “are associated persons” in a context where its meaning could be ambiguous. The section is concerned with the situation of a property being disposed of at a profit or gain, ie something that happens in the present and triggers the application of the section. However, the section also refers to the earlier transfer from the transferor to the transferee who “are associated persons”.

In section GD 9(1), the words “are associated persons” clearly relate back to the earlier time of the transfer from the transferor to the transferee, rather than the present time of the disposal of the land. The words “are associated persons” are followed by “and the transferee **subsequently** sells or otherwise disposes of that land”. The use of the word “subsequently” denies any connection to the event of disposal to the words “are associated persons”. The section, therefore, is an example of words in a present tense being used to relate to a past event.

Section GD 9(1) clearly supports the conclusion that “are associated persons” does not necessarily mean associated at the most recent point in time, ie the time of disposal, but can be interpreted as “were associated persons”. In the case of section GD 9(1), this means looking back to the time of acquisition by the relevant taxpayer, ie the transferee.

Legislative purpose

The use of the associated persons test in section CD 1(2) is essentially for anti-avoidance reasons and aims to stop the use of associated persons who are not carrying on any relevant business. This was referred to in the Parliamentary Debates in 1973 on the Land and Income Tax (Annual) Bill (which contained the predecessor provisions to section CD 1). Mr Munroe (MP, Invercargill) explained the difficulties in applying the then current law on the taxation of profits relating to land and the need for amendment, and stated (NZPD Vol 386, 1973: 3653):

There is a provision in the [Land and Income Tax] Act which makes dealing in real or personal property for profit or gain assessable for tax. The Inland Revenue Department has had difficulty with this provision because of interpretations of it by the courts. The courts have tended to take the view before they will uphold an assessment, that as there is no capital gains tax in New Zealand there must be a clear pattern of previous dealings, or the circumstances must be such as to leave an inference that a profit motive was present at the time of purchase. In cases where the taxpayers have been land dealers or builders they have been able to avoid assessment of profits on property deals by claiming quite successfully that the property was held as an investment even if the sale was made shortly after acquisition. **In other cases the land dealers or builders have held properties in the names of members of their families or in associate companies for the purpose of avoiding tax on the sale of the properties.** [Emphasis added]

If the intention were to prevent dealers in land using associates (who are not dealers) to acquire the land, one would expect that the relevant association would need to be examined at the time of acquisition. The intention behind the provisions of section CD 1(2) would seem to be to make it more difficult for a person who is carrying on one of the specified businesses to hide behind associated persons. If the test of association applies only at the time of disposal, this would mean that associated person purchasers of land who are “substituted” for land dealers could avoid being taxed where the association was technically terminated immediately before the disposal of the land.

Furthermore, if the association test applies only at the time of disposal, it would apply to persons who happen (by way of “accident” or otherwise) to become associated with, for example, a land dealer just prior to their disposing of property where no taxable purpose or connection previously existed.

In addition, the anti-avoidance policy would tend to suggest that the possible interpretation of applying the association test at both acquisition and disposal is also incorrect. As such an interpretation would also require the test to be applied at disposal, the concerns expressed above would be equally applicable to that interpretation.

Proposed Amendments

The Income Tax Bill 2002 which seeks to rewrite Parts A to E of the Income Tax Act 1994 proposes changes to section CD 1(2). Clauses CB 6 to CB 9 of the Bill expressly state that the test of association applies when the land is acquired or, in the case of builders undertaking improvements, improved, rather than at the time of disposal.

In respect of builders undertaking improvements this represents a change to the current law. Whereas currently the associated persons test is applied at the time of acquisition of the land, under the proposed changes the test will be applied at the time that improvements were begun.

If the Bill is passed in its present form it is currently proposed that these changes will take effect from 1 April 2005.

Conclusion

In paragraphs (b), (c), and (d) of section CD 1(2), on an ordinary reading of the words “are associated persons”, the time at which the test of association must be applied is ambiguous. However, the scheme and purpose of the provisions indicate that the correct interpretation is that the test of association is applied at the time the land is acquired by a taxpayer. The test is not applied at the time of sale or other disposition of the land, nor must it be applied at both the time of acquisition and at the time of sale or other disposition.

"COST PRICE OF THE MOTOR VEHICLE" - MEANING OF THE TERM FOR FRINGE BENEFIT TAX (FBT) PURPOSES

PUBLIC RULING – BR PUB 03/06

Note (not part of ruling): This ruling replaces public ruling BR Pub 00/10 which was published in *Tax Information Bulletin* Vol 12, No 10 (October 2000). BR Pub 00/10 applied until 31 October 2003. This ruling is essentially the same as BR Pub 00/10. Its period of application is from 1 November 2003 to 31 October 2008.

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

Taxation Law

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

This Ruling applies in respect of section CI 3(1) and Schedule 2 of the Income Tax Act 1994 (and the meaning of "cost price" for the purposes of determining the value of the benefit to the employee).

The Arrangement to which this Ruling applies

The Arrangement is the provision of a motor vehicle by an employer, who owns the motor vehicle, to an employee for the private use and enjoyment of the vehicle by the employee.

How the Taxation Law applies to the Arrangement

The Taxation Law applies to the Arrangement as follows:

The "cost price of the motor vehicle" for the purpose of the calculation of fringe benefit tax under section CI 3(1) and Schedule 2 will be determined as follows:

- The "cost price of the motor vehicle" will include:
  - the purchase price of the vehicle (inclusive of goods and services tax (GST)).
  - the cost of initial registration and licence plate fees (inclusive of GST).
  - the cost of accessories, components, and equipment (other than "business accessories") fitted to the vehicle at the time of purchase or at any time thereafter (all costs inclusive of GST).
  - the cost of sign writing or painting the vehicle in the employer's colours or style (all charges GST-inclusive).
  - the cost (if any) of transporting the motor vehicle to the place where the motor vehicle is to be first used (all charges GST-inclusive).
- The "cost price of the motor vehicle" will not include:
  - the cost of annual vehicle re-licensing fees.
  - the cost of "business accessories", fitted to the motor vehicle at the time of purchase or at any time thereafter.
  - the cost of financing the purchase of the vehicle.

For the purposes of this Ruling:

- The term "business accessories" means accessories, components, and equipment fitted to the vehicle, required for and relating solely to the business operations to which the vehicle is used, and that are in themselves "depreciable property" for the purposes of the Act. Where powered, they will usually require the vehicle's power source to operate them, eg a two-way radio, roof-mounted flashing warning lights, electronic testing/monitoring equipment, etc.
- The term "fitted to the vehicle" means permanently affixed to the vehicle. Permanency would not be negated if the accessory were removed from the vehicle on a temporary basis, for repair or maintenance, or on the removal of the accessory at the time of sale or disposal of the vehicle or the accessory itself.

The period or income year for which this Ruling applies

This Ruling will apply from 1 November 2003 to 31 October 2008.

This Ruling is signed by me on the 4th day of September 2003.

Martin Smith
General Manager (Adjudication & Rulings)

COMMENTARY ON PUBLIC RULING BR PUB 03/06

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusion reached in public ruling BR Pub 03/06 ("the Ruling").

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

Background

If an employee has the private use or enjoyment, or the availability for private use or enjoyment, of a motor vehicle that is owned by the employer of the employee, the employer must pay FBT on the value of the benefit. The benefit is calculated by reference to the cost price of the vehicle to the employer, not the value of the benefit to the employee. If an employer purchases a motor vehicle to be used by, or to be made available for use by, an employee, a number of costs are incurred in addition to the purchase price of the vehicle for the vehicle to be in a state where it can be used by the employee. Some of the additional costs include:

- On-road costs. Under section 5 of the Transport (Vehicle and Driver Registration and Licensing) Act 1986, no motor vehicle can be driven on the road unless:
  - the motor vehicle is registered; and
  - the registration plates and a current license issued for the vehicle are affixed and displayed on the vehicle; and
  - the full amount of the accident compensation levy has been paid.
- The cost of transporting the vehicle to the initial place where it is to be used.
- The cost of fitted accessories, components, or equipment required for and relating solely to the business operations for which the vehicle is used.
- The cost of accessories, components, and equipment, such as towbars, roof racks, and stereos, fitted to the car at the time of purchase or at some later time.

This Ruling identifies the costs that form part of the "cost price of the motor vehicle" for the purposes of calculating FBT.

The Commissioner considers the cost of motor vehicles includes accessories that are permanently affixed to the vehicle. Everything that is permanently affixed to the vehicle, including accessories such as CD players, towbars, and radiotelephone sets, is part of the cost to the employer of making the vehicle available to the employee. Accessories not so permanently affixed are not part of the cost price of the vehicle in the first place and their FBT (or other income tax) status is to be determined separately. However, the Commissioner considers that certain accessories, permanently fitted to the vehicle and relating solely to the business operations for which the vehicle is used, should not be treated as part of the cost of the vehicle for FBT purposes. For example, a radiotelephone set fitted to the vehicle and only able to be used for business purposes would be excluded from the vehicle's cost price because it is a "business accessory". On the other hand, a mobile phone is an example of an item considered not to be part of the cost price of the vehicle because it does not meet the test of being permanently affixed to the vehicle.

Legislation

Section CI 3(1) provides a formula for calculating the value of the fringe benefit that consists of the private use and enjoyment, or the availability for the private use and enjoyment, of a vehicle. This formula is:

$\frac{y \times z}{90}$ when the benefit is subject to FBT on a quarterly basis; and

$\frac{y \times z}{365}$ when the benefit is subject to FBT on an income year basis.

In these formulae, if the benefit is subject to FBT, (z) is the amount calculated in accordance with Schedule 2.

Schedule 2 states:

PART A – MOTOR VEHICLES

Subject to clause 3, in relation to any quarter or (where fringe benefit tax is payable in respect of the vehicle on an income year basis under section ND 14) to any income year, and to any motor vehicle that in the quarter or income year is provided by any person for the private use or enjoyment of an employee or is available for such private use or enjoyment, the value of the benefit that would be able to be enjoyed by the employee, if the employee had unlimited private use or enjoyment or availability for private use or enjoyment of the motor vehicle in that quarter or income year, shall be, -

(a) Where the motor vehicle is owned (whether in the person's own right or jointly with any other person) by that person, 6% or (where fringe benefit tax is payable in respect of the vehicle on an income year basis under section ND 14) 24% of **the cost price of the motor vehicle to that person** or, as the case may be, those persons: (Emphasis added)

(b) Where the motor vehicle is leased or rented by that person from any other person (that person and that other person being associated persons) under a lease or rental agreement that commenced -

(i) …

(ii) On or after 23 September 1985, 6% or (where fringe benefit tax is payable in respect of the vehicle on an income year basis under section ND 14) 24% **of the**

> **cost price of the motor vehicle** to the person who is the owner of the motor vehicle at the time the benefit is provided to the employee: (Emphasis added)

The definition of "Adjusted tax value" in section OB 1 states:

(a) Means, in relation to any depreciable property of a taxpayer and any particular time (and subject to section EG 11, in the case of property in a pool, and to section EG 19(10)(a), in the case of software to which that section applies), the amount calculated in accordance with the following formula:

bv (base value) – ad (aggregate deductions)

where –

bv (base value) is –

(i) Except where paragraph (ii) or paragraph (iii) or paragraph (iv) of this item applies, the **cost of the property** to the taxpayer (excluding any expenditure of the taxpayer allowed as a deduction under any provision of this Act or the Income Tax Act 1976 other than s sections EG 1 to EG 15 and section EG 18 of this Act or sections 108 to 108N and section 113A of the Income Tax Act 1976): (Emphasis added)

Application of the Legislation

The determinative factor in the calculation of FBT on motor vehicles is the "cost price of the motor vehicle to that person" (the employer) as contained in Schedule 2. The calculation of fringe benefit tax on the provision of a motor vehicle to an employee is based on the vehicle's cost price, and **not** its value to the employee. This was the "test" adopted by Parliament and confirmed in *C of IR v Atlas Copco (NZ) Ltd* (1990) 12 NZTC 7,327. At pages 7,334 and 7,335 Sinclair J said:

> The Tenth Schedule to the Income Tax Act clearly states that the value of the benefit is an amount equal to "6% of the cost price of the motor vehicle *to that person*", where "that person" is the person providing the benefit. In other words, the schedule expressly states that the value of the benefit is to be calculated by reference to the cost price to the employer. There is no justification in the legislation for defining the term by reference to the *value* of the benefit to the *employee* rather than the cost of the benefit to the *employer*. There is no room for an employee notion to be introduced when construing the Schedule.

The above comment is consistent with the intent of Parliament that the cost price of motor vehicles for FBT purposes should equal the cost to the employee, had the employee purchased the vehicle rather than having the vehicle provided by the employer. In introducing the Tax Reform Bill 1990, on the 19 December 1990, the then Minister of Revenue (Hon. Wyatt Creech) said that the amendment to the FBT rules was to ensure that the value of the motor vehicle for FBT purposes included GST. He said that this was to ensure that the FBT "cost price" would equate with the cost that the employee would have had to pay had the employee purchased the vehicle.

Meaning of "cost price"

"Cost price" is not defined in the Act for the purposes of the FBT rules. It is, therefore, not clear whether it is limited to the purchase price of the vehicle, as some suggest, or whether it includes costs incidental to the purchase, such as on-road costs and the costs of transporting the vehicle to the place where it will be used.

The words "cost" and "cost price" are used extensively throughout the Act. Section OB 1 defines these words for a very limited number of sections where the words are used. Examples include:

- For the purposes of Part EE (the trading stock rules) "cost" is defined as:

  > In Part EE, for trading stock other than an excepted financial arrangement, means costs incurred in the ordinary course of business to bring trading **stock to its present location and condition** including purchase costs and costs of production calculated under sections EE 5 to EE 7. (Emphasis added)

- "Cost price" in relation to "specified leases" means:

  > …the amount of expenditure of a capital nature incurred by the lessor in acquiring **and installing** that lease asset… (Emphasis added)

The significance of these two definitions (even though they have limited application in the Act) is that they both include a reference to costs ("bringing to its present location" and "installing") that are more than simply the *purchase price* of the item in question. In the definition of "cost" (for the purposes of the trading stock rules), it could be argued that getting the stock "*to its present location*" is synonymous with "*installing*" as used in the definition of "cost price". "Install" is defined in the *Concise Oxford Dictionary* as "*place (heating or lighting etc.) in position for use*". While the two definitions relate to the two different sides of the revenue/capital distinction, they both relate to the assets used in a business.

This leads to the view that there may be very little difference (if any) between the terms "cost" and "cost price" as used throughout the Act. This view is supported by the comments of Fullagar J in *Australian Jam Co. Pty Ltd v FCT* (1953) 10 ATD 220. This case concerned the valuation of trading stock. At 570 the Judge said:

> The words 'cost price' in the section [relating to the valuation of trading stock] are perhaps not literally appropriate to goods manufactured, as distinct from goods purchased, by the taxpayer, but I feel no difficulty in reading them as meaning simply 'cost'.

This implies that "price" adds nothing to the meaning of "cost". "Cost price" is simply "cost". In commenting on the above citation in an item entitled "Some Aspects of Valuation of Trading Stock for Income Tax Purposes" in the *NZ Universities Law Review*, Vol. 1 (September 1964), ILM Richardson (now Sir Ivor) said:

If "price" adds anything to "cost" it is only in emphasis, in stressing that what is involved is the actual expenditure of money by the taxpayer with relation to the trading stock.

In *Phillip Morris Ltd v. F.C. of T.* 79 ATC 4,352, the Supreme Court of Victoria had to decide what constituted "cost price" for the valuation of cigarettes (trading stock) on hand at the end of an income year under section 31(1) of the Income Tax Act Assessment Act 1936. The Court determined that in respect of manufactured goods:

…the words "cost price" in that subsection [section 31(1)] should be understood as meaning "cost".

Both the above cases (*Australian Jam* and *Phillip Morris)* considered section 31(1) of the [Australian] Income Tax Assessment Act, which gives taxpayers an option of valuing trading stock at its "cost price". The wording of the section is very similar to the former New Zealand equivalent - section EE 1(3) prior to amendments that applied from the 1998-99 income year - that is, the same "cost price" option applied to New Zealand taxpayers. It follows that in considering the use of the words "cost price" in New Zealand, the courts would arguably adopt the same position as the Australian courts in the above decisions. Where the words are used in other parts of the Act (including Schedule 2), and there is no specific definition, it is considered that "cost price" should be given a similar interpretation. This means that "cost price" as used in Schedule 2 for FBT purposes also means "cost".

In discussing trading stock, some authorities take the view that "cost price" relates to things purchased, while "cost" relates to things manufactured. For example, in *Phillip Morris* Jenkinson J said:

The statutory conception of "cost price" or, **in the case of manufacturer's stock, "cost"** is merely a value at a particular time… (Emphasis added)

In *Australian Jam*, Fullagar J said:

The words 'cost price' in the section [relating to the valuation of trading stock] are **perhaps not literally appropriate to goods manufactured, as distinct from goods purchased**, by the taxpayer, but I feel no difficulty in reading them as meaning simply 'cost'. (Emphasis added).

In *TRA Case S12* (1995) 17 NZTC 7,102, Barber DJ considered what is meant by "its cost price" in relation to the valuation of foals born to broodmares owned by a horse breeder. He determined that the foal's cost price should include the write-down (depreciation) of the broodmare. At 7,107 he said:

...the Legislature has provided that the breeder or farmer must take progeny into account at "its cost price". Those words do not seem to me to be a particularly happy choice because **"cost price" is normally that which a merchant buys something** (refer Sixth Edition of the *Concise Oxford Dictionary*). The cost is the price to be paid for a thing and the price is the money or other consideration for which a thing is bought or sold. The taxpayer has not purchased the foal but has had the foal created through the mare after servicing from the stallion. However, in their context, the words "its cost price" must be given a sensible interpretation. In the *Shorter Oxford English Dictionary* (3rd Edition) a meaning for "cost" is "That which must be given in order to acquire, produce or effect something". (Emphasis added)

In these cases the courts make a distinction between "cost" and "cost price". "Cost" relating to manufactured goods (the cost of manufacture) and "cost price" relating to goods purchased (the cost of purchase). However, under both the Australian and the former New Zealand trading stock valuation rules there is only one option for valuing trading stock at cost and that is its "cost price". In terms of the legislation, therefore, both manufacturers of trading stock and purchasers of trading stock are required to value their goods under its "cost price". So, in the trading stock context at least, "cost price" includes both the terms "cost" and "cost price".

Trading stock context

As mentioned above, the trading stock rules changed with effect from the 1998-99 income year. The current definition of "cost" applying to the valuation of trading stock requires the "cost" to include, "*any costs incurred in the ordinary course of business to bring the trading stock to its present location and condition including purchase costs and costs of production calculated under sections EE 5 to EE 7*". The effect is that now trading stock must be valued by the taxpayer using generally accepted accounting principals (section EE 5(1)). Effectively, section EE 5(2) says that the trading stock must comply with Financial Reporting Standard No.4 (FRS 4) 1994 (Accounting for Inventories).

In FRS 4, the value of inventories (trading stock) is to include:

4.6 "Cost of inventories" is the total of:

(a) **cost of purchase** (as defined in paragraph 4.10 below);

(b) costs of conversions (as defined in paragraph 4.13 below); and

(c) other **costs incurred in bringing the inventories to their present location and condition**.

4.10 "Cost of purchase" includes:

(a) import duties and other purchase taxes (**other than those subsequently recoverable**);

(b) **Transport and handling costs**

(c) …

(Emphasis added)

As this standard applied from 1994 (replacing the previous standard -SSAP 4), presumably FRS 4 could have been used as a guide by taxpayers in valuing trading stock under the former valuation option, "cost price". That the Commissioner accepted similar calculations to FRS 4 is illustrated by the contents of an item on the valuation of trading stock published in *Public Information Bulletin* No 82 (December 1974). This item

set out the three options available to taxpayers, being cost price, market selling value, or replacement price. It then went on to define "cost" - (note: not "cost price"). In respect of purchases of finished goods the item said:

Here the cost should include **freight inwards**, customs duty, insurance, and sales tax in addition to the actual purchase price of the goods. (Emphasis added)

In the context of their use in relation to trading stock, the words "cost" and "cost price" are interchangeable.

Depreciation context

The only provisions that deal with valuation of capital assets in the Act are the depreciation rules set out in Subpart EG.

Generally, business assets are "depreciable property" as defined in section OB1, being property that "*might reasonably be expected …to decline in value …while used or available for use …in carrying on a business for the purposes of deriving gross income*". This is provided that the assets are not trading stock, land, financial arrangements, or intangible property. Motor vehicles are "depreciable property" and will qualify for depreciation deductions under Part EG.

Under section EG 2(1)(a) depreciation is calculated:

- where the diminishing value method is being used, on the "adjusted tax value" of the property.
- where the straight-line method is being used, on the "cost of the property" to the taxpayer.

"Cost" is not defined in the Act for the purposes of section EG 2. "Adjusted tax value" is defined in section OB 1. The main component of this definition is the "base value" of the property. "Base value" in the majority of cases, especially in respect of property acquired after the beginning of the 1993-94 income year, will be its "cost".

As stated above, as far as trading stock is concerned there appears to be no difference between the use of the words "cost" and "cost price". The words are interchangeable. If the same applies in respect of the word "cost" used in subpart EG, it could mean that "cost" and "cost price" are interchangeable elsewhere in the Act, eg in Schedule 2, in determining the "cost price" of a motor vehicle for FBT purposes.

The definition of "cost price", as it applies to Schedule 2, was discussed in *C of IR v Atlas Copco (NZ) Ltd*. This case considered whether the "cost price" in respect of motor vehicles was the GST inclusive or exclusive cost. While it was not necessary for the Court to formulate an exhaustive meaning of "cost price", Sinclair J concluded that the words "cost" and "price" are susceptible to a wide variety of meanings. At page 7,332 Sinclair J referred to expert accounting evidence on the meaning of "cost" and stated:

This accords with the expert evidence given by two accountants, Mr John Hagen and Professor David Emanuel. Professor Emanuel cited a number of definitions of "cost" from leading textbooks on accounting:

"(a) 'Costs represent the financial sacrifices which are involved in acquiring or producing assets.' Ma, Matthews and Macmullan, The Accounting Framework (2nd ed, 1987) at p 43.

(b) 'Accountants have placed a great deal of emphasis upon the principle of objective evidence, and nowhere is it more apparent than in accounting for the acquisition of plant and equipment. Cost is used as the valuation method in this instance because it is more easily identified than any other valuation and because it is said to be the sacrifice given up now to accomplish future objectives.' McCullers and Schroeder, Accounting Theory: Text and Readings (1978) at p 233.

(c) 'We define cost here as the sum of the quantitative representations of the sacrifices necessarily incurred **to bring the fixed asset to its place and state of use**.' Most, Accounting Theory (1977) at p 235. (Emphasis added)

(d) 'Cost is thus the economic sacrifice expressed in monetary terms required to obtain a specific asset or group of assets.' Hendriksen, Accounting Theory (3rd ed, 1977) at p 270.

(e) 'Cost is an economic sacrifice, an outflow of wealth, by giving up asset value or incurring liability value.' Staubus, Activity Costing for Decisions (1988) at p 192."

Professor Emanuel then summarised the position by saying that:

"Cost is the economic sacrifice associated **with getting the purchased item to its current location and condition."** (Emphasis added)

It is interesting to note that here the accountants used the term "cost" rather than "cost price" – the term (as used in Schedule 2) that the Court was considering. This is consistent with the earlier analysis that the words are interchangeable.

In *Atlas Copco* the Commissioner objected to the evidence of the accountants. At page 7,333 the Court said:

Counsel for the Commissioner objected to the evidence of the two accountants on the basis that the interpretation of "cost price" is a question of law for the Court, and to rely upon the interpretation of accountants would infringe the "ultimate issue" rule. Moreover, counsel felt that the accountants had mistakenly placed economic substance over legal form in analysing the nature of the payment paid by the purchaser.

It is true that defining "cost price" is a question of statutory interpretation and, as such, must be resolved by the Court. **Where the meaning of words in a statutory context is unclear or ambiguous, however, the Court may derive some assistance from common business parlance and practice**, as well as international standards. Moreover, as I have already discussed, the approach of the accountants accords with both the economic substance and the legal form of the transaction: the GST component of the purchase price which may be recovered by a registered purchaser cannot be considered part of the effective "cost price". (Emphasis added)

Here the Court accepts that where uncertainty in the legislation exists, common business practice can be taken into account in defining terms or words. As sufficient doubt surrounds the use of the words in question, accounting or business usage may be of assistance.

Generally, the accounting treatment is that the initial cost of a fixed asset includes the costs of putting it into the working condition necessary for its intended use, installation costs, and freight etc (see for instance, FRS 4, 4.6(c), and the expert evidence given in *Atlas Copco* (cited above)).

This further strengthens the proposition that no fundamental difference exists between "cost" and "cost price" as used in the Act.

Conclusion

On the above analysis it is concluded that "cost" and "cost price" as used in the Act are interchangeable. The calculations of both terms, using accepted accounting principles, include costs in addition to what can be termed the "purchase price". This means that for the purposes of the phrase "cost price of the motor vehicle" in the FBT rules, the "cost price" of a motor vehicle will be more than just its purchase price.

What is the "cost price" of a motor vehicle for FBT purposes?

When a new motor vehicle is purchased, a number of Government charges have to be paid before the purchaser can use the vehicle on the road. The purchaser may also have accessories fitted to the vehicle at the time of purchase or at a later date. Some of these accessories may be of a non-business nature, such as a towbar, CD player, CNG/LPG conversion, air conditioning, alloy wheels, etc. Generally, unless they are part of a special deal, these accessories will be additional costs to the purchaser. In some instances the purchaser may have a business accessory, eg a radio-telephone, fitted to the vehicle at the time of purchase or at a later date.

The question to be considered is whether all or any of (the cost of) these items forms part of the "cost price" of the vehicle.

Government charges

Fees payable at the time of purchase of a new car so that it can be driven on the road include:

- Once only payments: registration fee, number plate fee.
- Annual (recurring) fees: annual relicensing fee, ACC levy, label fee.

It is arguable that without payment of the initial registration and plate fees (as distinct from the recurring annual re-licensing fees) by the employer the vehicle cannot be used immediately. The employer has to pay these costs before the vehicle can be "put on the road" or in a position to be used. This suggests that they are properly to be treated as part of the "cost price" of the car.

Support for the view that "cost" includes such items as getting the vehicle "on the road" so that it can be used, is found in the High Court of Australia case of *BP Refinery (Kwinana) Ltd v FCT* (1960) 8 AITR 113. At page 117, Kitto J in considering the issue of what was included in the term "cost", said.

> … in my opinion, the word "cost" in section 56 (1)(b) bears the meaning which it has in the business life of the community. It seems to me impossible to suppose that the depreciation provisions of the Act are intended to apply only to those simple cases in which the ascertainment of cost is a purely arithmetical process. I interpret it as embracing the whole sum which, according to accepted accountancy practice as applied to the circumstances of the case, ought to be considered as having been laid out by the taxpayer in order to acquire the subject-matter as plant, **that is to say installed and ready for use** as plant for the purpose of producing assessable income. (Emphasis added)

Therefore, the cost of the vehicle must include expenditure making it "ready for use" by the taxpayer. Without payment of the registration and plate fees the vehicle is not ready for the purpose intended.

Whether the costs of the initial registration fee and the plate fee form part of the cost of the vehicle is not entirely clear. The Commissioner considers the better view of the law, and the likely intent of Parliament, is that such expenses form part of the cost price of the vehicle, particularly given that they are one-off costs that fall into the "once and for all payments" category (see *BP Australia Ltd v FCT*/1965/3 All ER 209) and hence are capital in nature. These fees are intended to make the vehicle able to be used.

The remaining fees are annual charges and normal accounting practice would treat them as revenue expenditure, even if they were incurred upon purchase of the vehicle.

In summary, the better view is that registration and plate fees are "once and for all" payments, are of a capital nature, make the vehicle able to be used, and are part of the "cost price" of the vehicle. Annual charges (licensing, ACC levy, etc.) are revenue expenditure and not part of the "cost price".

Business accessories

Generally, accessories permanently fitted to the motor vehicle are properly to be included as part of the vehicle's cost. As discussed earlier, accessories, such as stereos, towbars, roofracks, etc., fitted to a vehicle will form part of its cost price. However, some components or equipment fitted to vehicles may be of a purely business nature. The issue arises as to whether such components or equipment should also be included in the "cost price of the vehicle" for FBT purposes.

There is no legislative direction on this issue. This may indicate that all accessories, components, or equipment attached to the vehicle form part of its "cost price". It is arguable, however, that business accessories, components, and equipment fitted to the vehicle should not be treated as forming part of the cost price, where they are required and relate solely to the special business operations for which the vehicle is used, and are in themselves depreciable property for the purposes of the Act, eg a two-way radio telephone in a salesperson's vehicle. Such components or equipment are fitted to the vehicle to facilitate the business use of the vehicle, and may be considered as separate business assets located in the vehicle.

Another factor (relevant to this last-mentioned aspect) possibly pointing to the components or equipment as not being part of the cost price, is to consider the nature of the assets and how they are treated by businesses for accounting purposes. For example, it is most likely that components such as two-way radios are accounted for and depreciated separately. The radios can be removed from vehicles, or moved from one vehicle to another, and it seems logical that they be treated as separate assets for depreciation purposes. Note: motor vehicles and radiotelephone equipment are listed separately in Depreciation Determination DEP 1. Two-way radios have their own depreciation rate because they are regarded as assets in their own right and not accessories (to a motor vehicle). They form part of a larger asset, for example, the entire radio telephone network, consisting of radios in vehicles and the central control unit in the employer's premises. In such circumstances, even though they are a form of accessory or addition to the motor vehicle, they are an asset in their own right and therefore require a separate asset classification. Usually, radio networks are purchased as a package consisting of a number radios (for each vehicle) plus the central control station. To treat the network as part of the cost price of each car would require an apportionment of the overall expense, including installation costs to each vehicle. The Commissioner does not consider this to be a sensible approach.

The same could be said of accessories such as roof-mounted flashing lights, and electronic monitoring equipment. If these types of assets are added because they are required for and relate solely to the business operations for which the vehicle is used, they will be treated similarly to the two-way radio system.

Therefore, where business components, such as two-way radios, roof-mounted flashing lights, electronic testing or monitoring equipment, etc, are fitted to the vehicle and are paid for by the employer, they do not form part of the "cost price" for FBT purposes. As mentioned earlier, such accessories are business assets of the employer, coming within the definition of "depreciable property" for the purposes of the Act.

As previously discussed under the heading "Application of the Legislation", it was the clear intent of Parliament that the "cost price" for FBT purposes should equal the cost to the employee had the employee purchased the vehicle rather than having it provided by the employer. It follows that if the employee had to pay for the vehicle, the cost to the employee must also include accessories fitted to the vehicle as already discussed. Exceptions are the cost of separately depreciable components or equipment fitted to the vehicle solely to meet the special needs of any business operations for which the vehicle is used.

Therefore, the Commissioner considers that business components fitted to the vehicle, which are required for and relate solely to the business operations for which the vehicle is used, and are in themselves depreciable property, should be excluded from the "cost price" of motor vehicles for FBT purposes. This covers assets requiring the vehicle's power source in order to operate: they are not part of the cost price of the car itself.

There may be isolated instances, where the type of business asset mentioned above will unavoidably be used for non-business purposes. The Commissioner considers that any extraordinary and unenvisaged use of the accessory for non-business use over the life of the asset will not in itself negate the purpose of fitting the accessory to be "solely for business purposes" in this context.

Cost of non-business accessories

Commonly, when a vehicle is purchased the owner asks for certain "extras" or accessories (other than business accessories) to be fitted to the vehicle. If these accessories are not "optioned" (and included in the purchase price), the dealer will charge for their cost and fitting to the vehicle. Such accessories can include:

- stereos, towbars, sunroof, roofrack, CNG/LPG conversions, alloy wheels, air-conditioning, electric windows and locking systems, higher specification tyres, etc.

Where the vendor charges for any of these accessories, the question arises as to whether they should be added to the "cost price" of the vehicle for FBT purposes. The same issue arises if the accessories are acquired from another person or supplier, or acquired at a later date.

Such accessories are of a capital nature and should be added to the vehicle purchase price to arrive at its "cost price". They are part of the vehicle as a whole and are not generally removed at the time the vehicle is sold or otherwise disposed of. They are either singularly or collectively a "once and for all" payment(s), culminating in the "cost price" of the vehicle that is provided to the employee by the employer for the employee's "private use and enjoyment".

Under this interpretation, the cost price may vary from period to period, depending on when accessories are added (or in the unlikely or rarer event of an accessory being removed).

Therefore, in summary, accessories fitted to a vehicle form part of its "cost price" for FBT purposes (as contemplated in Schedule 2), irrespective of the time they are purchased and fitted to the vehicle.

Cost of sign writing or painting the vehicle in the employer's colours or design

It is the Commissioner's view that costs associated with sign writing and painting the motor vehicle in the employer's colours, logo, or design are part of the "cost price" of the vehicle for FBT purposes. It was concluded earlier that "cost price" for the purposes of Schedule 2 means something more than the "purchase price" of the motor vehicle. While the cost of sign writing or painting may not add to the value of the motor vehicle, that is not the test. As discussed earlier, the test is the "cost to the employer", not the "value to the employee". Some may argue that the costs associated with sign writing and painting the vehicle are primarily of a business nature and should be excluded from the vehicle's cost price. However, unlike business accessories, the sign writing and painting will generally not be depreciable property and therefore, such costs must be added to the cost of the vehicle. The better view of the law is that the costs are correctly attributable to the vehicle itself and form part of the cost price for FBT purposes.

Transporting or freighting the vehicle to its place of use

In the above discussion on "cost price", it is clear that the courts have accepted that the cost of transporting or freighting goods (whether those goods are trading stock or capital assets of the business) to the place where they are to be used is part of the cost of the goods. As a general rule, the initial cost of fixed assets will include expenditure incurred to put it (the asset) into the working condition necessary for its intended use. And in *Atlas Copco*, "cost is …associated with getting the purchased item to its current location and condition". This would include installation costs and freight.

The cost of transporting a purchased motor vehicle to the place where it can be used by the taxpayer, is clearly part of its "cost price", both for FBT and depreciation purposes. For example, the purchase of vehicles direct from a manufacturer or from another source overseas, where the purchaser pays for the cost of transporting the vehicle to New Zealand. It is the Commissioner's view that these transport costs form part of the "cost price" of the vehicle for FBT purposes.

However, these costs only relate to the initial cost of getting the vehicle to the place it will first be used by the employer, after acquisition. Subsequent transport costs of moving the vehicle within New Zealand (say from one branch of the employer's firm to another) are considered to be part of the normal business operations of the employer and on revenue account.

Cost of repairs and maintenance

Another issue is the costs of repairs and maintenance of the vehicle and/or accessories, and whether they should be added to the cost price.

Generally, repairs and maintenance expenditure on the vehicle or accessories will not increase the vehicle's "cost price" for FBT purposes. However, if work on the car is more than normal repairs and maintenance, such as replacing the existing motor with one of larger capacity, the question arises whether that alteration will increase the cost price of the vehicle for FBT purposes. If the repair or replacement is considered to be of a revenue nature, and deductible for income tax purposes, the cost price of the vehicle will not increase in value for the calculation of FBT. On the other hand, if the repair or replacement is of a capital nature, the cost price for FBT purposes must be increased by the amount of that capitalisation. Each case will need to be considered on the basis of its own facts applying established capital/revenue distinction rules. If the FBT cost price is increased, the recalculation of FBT (on the increased cost price) will apply from the quarter in which that capital expenditure was incurred.

Example 1

Employer A purchases a secondhand motor vehicle as a company car for the use of a salesperson employee. The employee will be travelling long distances, so the employer purchases a CD player and has it fitted to the vehicle. As the employee has the full use of the vehicle for private use and is likely to tow his own trailer from time to time, he asks the employer to purchase and fit a towbar to the vehicle. The employer agrees. The "cost price" of the vehicle for FBT purposes will be the total of the purchase price plus the cost of acquiring and fitting the CD player and the towbar (all costs GST-inclusive).

Example 2

Employer B is looking for a vehicle to replace an existing vehicle written-off by the firm's Wellington-based accountant. The accountant will be entitled to use the vehicle for private purposes when it is not being used for business purposes. While on a trip to Auckland the employer locates a suitable secondhand car, purchases it, and has it transported to Wellington where the accountant will use it. The "cost price" of the car for FBT purposes will be the purchase price plus the cost of transporting it to Wellington (both costs GST-inclusive).

Example 3

Employer C decides to replace the company's fleet of cars used by its sales representatives, because of the high cost of maintaining the existing fleet. The sales representatives are permitted to use the vehicles for private use when they are not required for business purposes. Through a contact with a motor vehicle dealer, the company decides to purchase 10 secondhand cars direct from Japan. The employer agrees on a purchase price with a Japanese car dealer and arranges for the vehicles to be shipped to New Zealand. The "cost price" of the vehicles for FBT purposes will be the total of:

- the purchase price of the cars, including any costs or commissions paid in Japan or in New Zealand
- the cost of transporting the cars to New Zealand
- GST and any import or inspection levies payable at the time of importation
- the cost of initial registration and licence plate fees, and
- the cost of any accessories fitted to the cars at the time of purchase or any time after purchase, either in Japan or on their arrival in New Zealand.

Example 4

Employer D is a forestry contracting firm, and has recently purchased a four-wheel drive motor car for its forestry foreman. The foreman has the full use and enjoyment of the vehicle for private purposes while not working. As with the employer's other work vehicles, the car is fitted with a radiotelephone used only for communication between the company's headquarters and its own vehicles. As the radiotelephone is fitted solely for business purposes, and may be considered a separately depreciable business asset located in the vehicle, it does not form part of the cost price of the vehicle for FBT purposes.

Example 5

An employee of Employer E is a travelling salesman. When the employer purchased a new vehicle for the employee's use, a mobile phone kit (mobile phone and car kit) was installed in the car at the employer's expense. The cost of the mobile phone will be excluded from the cost price of the motor vehicle because it is not "permanently affixed to the vehicle". Whether use of the mobile phone gives rise to a fringe benefit in its own right must be decided on the facts.

Comments on technical submissions received

Many comments received in the course of producing this item suggested that the cost of fitted accessories should not be subject to FBT, as they have no inherent benefit for employees. As noted earlier in the ruling commentary, this argument ignores the fact that the statutory test, in the context of motor vehicles, is not the value of the benefit to the employee, but the cost price of the vehicle to the employer.

It is considered that the Commissioner's approach in excluding any such fittings and accessories on the basis of being business assets is arguably a favourable interpretation of the legislation to taxpayers, particularly when compared to the wording in the Australian legislation where such a test has been specifically legislated.

PRODUCT RULING – BR PRD 03/13

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 PMP Distribution Limited ("PMP").

Taxation Laws

All legislative references are to the Income Tax Act 1994 ("the ITA") unless otherwise stated.

This Ruling applies in respect of sections BD 2(2)(c), DE 1, NC 13 and KC 2; the definitions of "extra emolument", "income from employment", "salary or wages", "specified office holder" and "withholding payment" in section OB 1; the definition of "source deduction payment" in section OB 2(1); the definition of "PAYE rules" in section OZ 1(1); regulation 4(1) and clause 5(d) of Part A of the Schedule to the Income Tax (Withholding Payments) Regulations 1979 ("the Regulations"); and section 6(3)(b) of the Goods and Services Tax Act 1985 ("the GST Act").

The Arrangement to which this Ruling applies

The Arrangement is the engagement of persons ("the deliverers") by PMP pursuant to a standard form contract, for the delivery of newspapers, leaflets, brochures, catalogues, advertising material, samples and other such items to households and other premises throughout New Zealand. Further details of the Arrangement are set out in the paragraphs below.

1 PMP carries on the business of distributing newspapers, leaflets, brochures, catalogues, advertising material, samples and other such items to households and other premises throughout New Zealand.

2 PMP engages the deliverers pursuant to a standard form contract which includes a Deliverers' Handbook, the conditions contained in which are required to be agreed to by the deliverers when entering into a contract ("the Contract"), to deliver particular items within a specified period, to each house, flat or other premises located within a designated area, by placing one of each item in each letter box (or other specified location). The deliverers are paid specified rates per item delivered (varying depending on the weight of the item). The Contract is affixed to this Ruling as Appendix I.

Condition stipulated by the Commissioner

This Ruling is made subject to the following condition:

a) The relationship between PMP and the deliverers is, and during the period of this Ruling will continue to be, entirely in accordance with the Contract affixed to this Ruling as Appendix I, and there are no other collateral contracts, agreements, terms or conditions, written or otherwise, relating to the engagement of the deliverers.

How the Taxation Laws apply to the Arrangement

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

- For the purposes of the PAYE rules, any payment made to a deliverer by PMP pursuant to the Contract will not be "salary or wages", an "extra emolument" or a payment made to a "specified office holder" in respect of the activities of a specified office, within the meaning of those terms as defined in section OB 1. To the extent that any such payment is also not a "withholding payment", it will therefore not be a "source deduction payment" as defined in section OB 2(1), for the purposes of the PAYE rules.
- For the purposes of sections BD 2(2)(c) and DE 1, any payment made to a deliverer by PMP pursuant to the Contract will not be "income from employment" as that term is defined in section OB 1.
- For the purposes of the PAYE rules, any payment made to a deliverer by PMP pursuant to the Contract will not be a "withholding payment" as defined in section OB 1, to the extent that such payment relates to the delivery of any item the carriage of which does not require PMP to be registered as a postal operator under the Postal Services Act 1998.
- For the purposes of the PAYE rules, any payment made to a deliverer by PMP pursuant to the Contract (other than a payment made to a company), will fall within the class of payment specified in clause 5(d) of Part A of the schedule to the Regulations and be declared to be a "withholding payment" by regulation 4(1) of the Regulations and thus a "withholding payment" as defined in section OB 1, to the extent that such payment relates to the delivery of any item the carriage of which requires PMP to be registered as a postal operator under the Postal Services Act 1998.
- In accordance with section NC 13, and in relation to payments made pursuant to the Contract to deliverers entitled to the child rebate provided for by section KC 2, the amount of any tax deductions

required to be made will be reduced to $0 if the deliverer's total weekly earnings do not exceed $20, or their annual earnings are not expected to exceed $1,040, and reduced by $3 per week if the deliverer's total weekly earnings exceed $20, and their total earnings for the income year are expected to exceed $1,040.

- For the purposes of the GST Act, the provision of services by any deliverer to PMP under the Contract will not be excluded from the definition of "taxable activity" in section 6 of that Act by section 6(3)(b) of that Act.

The period or income year for which this Ruling applies

This Ruling will apply for the period 2 July 2003 to 2 July 2006.

This Ruling is signed by me on the 2nd day of July 2003.

Martin Smith
General Manager (Adjudication & Rulings)

APPENDIX I

PMP DISTRIBUTION

THE DELIVERERS' HANDBOOK & CONTRACT

Welcome to PMP Distribution. You are now a member of a nationwide team delivering free newsletters, circulars, addressed mail, samples etc., to over 1,000,000 suburban letterboxes. Our policy is to have the best distribution service in the country and pay the highest possible rates to our contractors. Our clients depend on you to deliver their material carefully and reliably

This handbook lists the Do's and Dont's when delivering newspapers, circulars etc., as well as being the contract by which you are engaged.

WELCOME TO OUR TEAM – GOOD LUCK

REMEMBER – If in doubt call your Supervisor

DO's

1 DELIVER to every letterbox at every house or flat in the area given to you. Read the map or street list given to you carefully. Put the circulars RIGHT INSIDE each letterbox. This stops the circulars getting wet, or being blown away.

2 START AND FINISH as instructed. Your Supervisor will instruct you when your deliveries are to be undertaken and what your regular delivery days are. From time to time you will receive instructions for a special delivery. Failure to deliver your material on the instructed days could cause us to lose a particular client's business and as such will have an affect on all contractors of this company. If you deliberately fail to deliver your material on the instructed day or days, you risk having your contract instantly terminated.

3 ASK you supervisor for more papers when new houses or flats appear in your area. If you run short of circulars or papers you MUST let your Supervisor or the office know about it. From time to time you may be asked to re-count or update the numbers of business, shops, homes or apartments that you deliver to on your delivery run.

4 NOTIFY YOUR SUPERVISOR IN THE EVENT OF ABSENCE:

Should you be absent due to holidays or sickness, or unable to complete delivery, you must notify your supervisor immediately. It is your responsibility to arrange for a reliable replacement and you must notify your Supervisor who this replacement will be, including their address and phone number. Failure to do this is very serious and could mean you will have your contract terminated.

5 CONTACT YOUR SUPERVISOR should you injure yourself while delivering or for any problems you may have about deliveries, ie. Absences or anything else at all that you are not sure about. Your Supervisor is there to help you. Don't just guess – this can take a lot longer to fix up than a quick call to your supervisor. Your Supervisor's name and phone number is on page 5 of this handbook.

6 SHOULD you encounter dogs, or have someone interfere with material after you have delivered, please discuss with your parents and Supervisor.

DON'TS

1. DO NOT use the newspaper tube, or milkbox, unless specifically instructed to do so. Never leave material on top of the letterbox, dropped on the lawn or in a hedge.

2. DO NOT deliver to letterboxes bearing "No Circulars" type signs unless specifically instructed to do so.

DO NOT deliver to letterboxes that are obviously not being cleared.

3. DO NOT fold one circular inside another. Each item must be kept separate. It is all right to pre fold and 'stack' the items on top of each other but NOT inside each other.

4. DO NOT throw away excess circulars. If you are getting too many – there must be a reason – talk to your supervisor. If you run short of circulars call your Supervisor, they normally have spares.

5. DO NOT deliver after dark. Be careful crossing roads. If you have someone annoying you or have any concerns about someone's behaviour during your delivery please discuss it with your parents and Supervisor.

6. DO NOT DUMP PAPERS OR CIRCULARS. If you do, your contract will be instantly terminated and you may be required to pay the cost of cleaning up as well as the cost of the circulars. Your Local Council may also impose a fine for littering for this sort of misbehaviour.

CONDITIONS OF CONTRACT

The parties acknowledge that this agreement is entered into by both parties on the basis that the Deliverer (referred to as either "Deliverer" or "Contractor") is an independent Contractor and that the Deliverer is not an agent or employee of the Company.

COMMENCEMENT DATE

Your commencement date is: ______________________________

and your delivery days are normally: ______________________________

PAYMENT

You will be paid credit. You need to make sure that you detach and fill out the form and give us your correct bank account number and deposit slip with bank numbers on it. You will be paid approximately monthly, and you will receive a remuneration report that explains how your earnings were calculated within a week of the payment being credited to your bank account.

Both parties acknowledge and agree that all payments received by the Deliverer pursuant to this agreement are gross payments, and that the Deliverer is solely responsible for his/her own Accident Compensation levies, Income Tax liabilities and Goods and Services Tax liability or any other income related payments or deductions that may be legislated for from time to time. Where required, the Company will deduct withholding tax from payments made to the Deliverer.

DELIVERY PAYMENT RATES – CIRCULARS

We set delivery rates based on how long we consider that it would take an average person to deliver in your allocated area. We reserve the right to change delivery payment rates from time to time.

RATES PER 100	Item 1	Item 2 and subsequent items
Under 50 grams/item		
51 – 100 grams/item		
Over 100 grams	as advised by supervisor	as advised by supervisor

Rates for other products such as newspapers, addressed mail and samples will be as advised by your supervisor.

REDUCTION

You must be aware that due to the nature of our business, we may cease to distribute any regular publication without notice, and due to the demands of clients and volume of work may need to vary the timing of material you are asked to handle. Where the situation is such that you will not receive any more delivery work from us, you may not receive any notice to this effect although we will try to give you notice

PERFORMANCE OF SERVICES

The Contractor may sub-contract the services, or otherwise engage or obtain assistance from others for the performance of the services but at all times remain personally responsible to PMP Distribution under the terms of the agreement and is the only person to whom PMP Distributions will pay the fee for the service

The Contractor shall if necessary, having regard to the bulk, weight or volume of the items to be delivered, and may at the Contractor's discretion, provide and use (but in all respects at the Contractor's cost, expense and risk) a car, trailer, trolley or other carrying equipment in connection with the delivery of the items.

CONDITIONS OF CONTRACT

The contractor is an independent Contractor and as such is free (in addition to the Contractor's freedom recognised above) to select the Contractor's own means and methods of performing the services and, subject to the delivery window requested by PMP Distribution, the hours during which the Contractor will perform those services. The Contractor in connection with the performance of the services shall indemnify and keep PMP Distribution indemnified against all actions, proceedings, liabilities, claims, damages, costs and expenses arising out of or in any way related to the Contractor's activities hereunder.

TERMINATION

Please give us as much notice as possible if you wish to terminate your contract, although the minimum notice we require is two weeks. If we have to terminate your contract, you will get two weeks notice unless the company believes you are guilty of serious breach of contract, for example 'dumping'. These notice periods may be reduced by mutual agreement.

The Company may at any time terminate this agreement forthwith if in the Companies reasonable opinion there has been a serious breach of this agreement and in particular, but without limitation:

(a) If the Deliverer has been guilty of gross negligence in duties or obligations under this agreement; or

(b) The Deliverer has willfully disregarded any reasonable or lawful instruction of the Company or supervisor given under the terms of this agreement; or

(c) The Deliverer has compromised safety, or breached Company standards, or Company rules such as to expose the Company to any potential liability.

(d) If the Deliverer has been guilty of grave impropriety or misconduct.

CONFIDENTIALITY

In the course of providing services, the Deliverer may receive and handle knowledge and information relating to the Company's business or clients which is considered to be confidential. The Deliverer shall not, either directly or indirectly, use or disclose such information, which has or may be acquired during the term of this contract with the Company, concerning the business affairs, property or customers of the Company.

This clause applies to all information whether or not it is recorded or memorised and includes information which is or may be of use to any competitor of the Company.

This restriction will apply throughout the Deliverer's relationship with the Company and after the termination of the contract without any time limit. However, the restriction will cease to apply to such confidential knowledge or information, which may become publicly known other than by breach of this clause on the part of the Deliverer.

Upon termination of this agreement, or as the Company may direct, the Deliverer shall deliver to the Company all documents, manuals, papers, equipment and property belonging to the Company.

COMPETITIONS

Should any of our deliveries contain competitions, you should note that you and your immediate family might not be permitted to enter.

SUPERVISOR

Your supervisor is ______________________________ of ____________________________________

Phone number ____

Your group leader is ____________________________ Phone number ___________________________

HEALTH AND SAFETY POLICY (DELIVERERS)

PMP Distribution recognises the need for deliverers to carry out their deliveries in a safe manner and therefore we issue the following instructions to help meet this aim.

1. Bundles of material can sometimes be quite heavy so you should be careful lifting them and always bend your knees and then lift as recommended by the ACC.

2. When carrying material please make sure you are comfortable with the weight and not straining yourself. If need be go back home and reload.

3. Wear sensible shoes with non-slip soles so that you will not slip over.

4. Make sure that you are visible at all times especially early morning or at dusk.

5. If dogs are troubling you then you must report specific details to your Area Supervisor.

6. Should you have an accident then you must report it to your Area Supervisor as soon as you can. Your Area Supervisor will fill out an Accident Report.

7. If using a cycle then the following applies:

   (a) Your cycle must meet the Police Safety standards.

   (b) You will need a light to be visible if delivery early morning or dusk.

   (c) Always wear your helmet. It is law that you must do so.

   (d) Cycling on the footpath is permitted whilst delivering but you must use the road when you have finished your run. Please take care to be on the lookout for cars backing out of driveways.

   (e) Make sure that your load is well secured and you are comfortable with the load.

   (f) If the weather is bad then please take care in looking after yourself.

8. Please identify any safety hazards on your run and notify your Supervisor, so you can work together to minimise any risks.

CONTRACT

Please complete this form and IR330 and return it to your Supervisor.
This must be done before we can give you any deliveries or payments.

We need to know your details so that we can pay you and a few other details for our records. You also need to agree to accept the Conditions of Contract and the Do's and Don'ts set out in this Handbook together with any amendments made in the future, before we can contract you.

1. PERSONAL DETAILS

(Surname) ____________________ (First Names) ______________________________

Address: ____

____

Telephone Number: ______________ Date of Birth ____________________

Email address ____

Male ☐ Female ☐ School Student ☐ Tertiary Student ☐ Adult ☐

2. ACC

Please deduct 3.75% of my monthly earnings and pay it to me in
the month the ACC annual account is due to help me manage my cashflow. Yes No

3. ACCOUNT DETAILS

Full Name ____

Name of Bank ________________________ Branch ____________________________

BANK ACCOUNT NUMBER (Not EFT-POS card number)

PLEASE PROVIDE DEPOSIT SLIP
WITH YOUR BANK NUMBER ON IT

Bank Branch Account Number Suffix

Reference:

Please check your account number carefully, if unsure please check with your bank, we want to make sure your pay gets into your account.

4. AGREEMENT TO CONDITIONS OF CONTRACT CONTAINED IN HANDBOOK

I agree to the Conditions of Contract and the Do's and Don'ts set out in the Handbook. I also agree to abide by any policy set by the company during my engagement. I also request that my payments be direct credited to the above account.

Signature: ________________________ Date: ________________________
PMP Distribution (by its duly authorised representative)

Signature: ________________________ Date: ________________________
Contractor (If the Contractor is under 18 years of age the contract must be signed by their parent or guardian)

Signature: ________________________ Date: ________________________
Parent or Guardian (if required)

FOR OFFICE USE ONLY:

Area Supervisor: __________ Area No. ____________________

Type: DIST/SUP/CONT/OFFICE

Start Date: __________ Negative No. __________ Contractor No. ____________

SEE OVER FOR IRD DETAILS

NEW LEGISLATION

TAX IMPLICATIONS OF THE WOOL BOARD RESTRUCTURING – WOOL INDUSTRY RESTRUCTURING ACT 2003

Introduction

The Wool Industry Restructuring Act 2003 ("the Act") provides for the structural reform of the wool industry by dissolving the New Zealand Wool Board ("the Board"), disbursing its assets and liabilities, and resolving a number of transitional and consequential issues. The Act provides for the conversion of the Board, which was a statutory body, into a company incorporated under the Companies Act 1993. This company, named Wool Board Disestablishment Company Ltd, assumes the Board's assets and liabilities and will oversee the disbursement of the Board's net assets to wool-growers as provided for in the restructuring plan. The board converted into a company on 15 September 2003—the restructuring day as notified in *New Zealand Gazette* (11/9/03 Notice:go6006).

The net assets of the Board have been allocated to wool-growers by the issue of exchangeable shares, redeemable shares and ordinary shares in Wool Board Disestablishment Company Ltd, on the basis of sheep numbers. The end result of the allocation, exchange and redemption of these shares is that:

- merino wool-growers have received cash and shares in a company called Merino Grower Investments Ltd and
- non-merino growers have received cash and shares in a company called Wool Equities Ltd. Non-merino growers can use this cash to acquire further shares in Wool Equities Ltd.

The Act contains a number of provisions to address the tax issues associated with the restructuring. These provisions, which are discussed in "Key features", allowed the restructuring to occur without any adverse tax implications. The "Detailed analysis" explains the various steps of the restructuring in relation to the distribution of the assets of the Board to wool-growers and the associated tax implications.

Background

The New Zealand Wool Board was a statutory body established under the Wool Board Act 1997 and was treated as a statutory producer board for tax purposes. Under that Act, the Board's assets ultimately belonged to the wool-growers. The Act also allowed for the imposition of a levy on wool produced in New Zealand.

Wool Equities Ltd was a subsidiary of the Board.

Merino Grower Investments Ltd was a company that was incorporated around 2001, and its shares were held by a discretionary trust (Merino Distribution Trust) on behalf of the merino wool-growers. This company had a loan from the Board.

Key features

The tax-related provisions in the Act are explained below. These provisions ensured that the restructuring occured without any adverse tax implications.

Conversion of the Board

As part of the restructuring, the Board was converted into and continues as a company incorporated under the Companies Act 1993, named Wool Board Disestablishment Company Ltd. Section 11 of the Act provides that this company is the same "person" as the Board and that no new entity is created as a result of the conversion. The conversion, therefore, has not given rise to tax implications, and any tax obligations or liabilities of the Board became those of the company.

Issue of shares to wool-growers

Section 36(1) of the Act provides that the issue by Wool Board Disestablishment Company Ltd as part of the share allocation plan in the restructuring plan of shares to a wool-grower is:

- not a dutiable gift
- not a dividend for income tax purposes, and
- not otherwise gross income of the grower for income tax purposes.

Section 36(5) of the Act ensured that proceeds from the sale, exchange, redemption or other disposition of a share (or other equity or similar instrument) received by a wool-grower as part of the restructuring process are not gross income for income tax purposes. This provision ensured that the exchange, redemption or other disposition of the shares received is not treated as revenue account property that is acquired for the purposes of resale and therefore taxable.

These provisions ensured that no tax implications have arisen as a result of the issue of shares in Wool Board Disestablishment Company Ltd and from the various transactions undertaken as part of the restructuring process in relation to those shares so the merino wool-growers own all the shares in Merino Grower Investments Ltd and the non-merino growers own all the shares in Wool Equities Ltd.

Available subscribed capital

Section 36(3) of the Act provides for Wool Board Disestablishment Company Ltd to have available subscribed capital of $47,720,400. This available subscribed capital has been allocated between the classes of shares issued by Wool Board Disestablishment Company Ltd on the restructuring day and in such proportions as it nominated.

Continuity of shareholding interest and net tax losses

Section 36(2), (4) and (6) of the Act deals with the continuity of shareholding interest in relation to the restructuring process, to ensure that shareholder continuity is not breached as part of that process.

In particular, section 36(2) provides that in relation to the issue of shares by Wool Board Disestablishment Company Ltd to non-merino wool-growers, those growers are treated as having held those shares at all times before the restructuring day. This provision allows the tax losses and imputation credit balances of this company (in substance, the tax losses and imputation credit balances of the Board) to be utilised by Wool Equities Ltd in the future, subject to the continuity rules. As part of the restructuring process, Wool Board Disestablishment Company Ltd became a wholly owned subsidiary of Wool Equities Ltd.

Section 36(4) of the Act deals with the transfer of the shares in Merino Grower Investments Ltd by the Merino Distribution Trust to a person who is a merino wool-grower as a part of the restructuring plan. It provides that merino wool-growers to whom the shares have been transferred are treated as having held the shares at all times before the transfer. The provision ensured that the transfer of shares in Merino Grower Investments Ltd from the trustees to the merino wool-growers did not constitute a breach in shareholder continuity and, as a result, the tax losses and imputation credit balances of Merino Grower Investments Ltd can be carried forwarded subject to the continuity rules.

As part of the restructuring process, the issue of the shares by Wool Board Disestablishment Company Ltd was to two trusts that will deal with the shares in terms of the restructuring plan on behalf of wool-growers. There is a separate trust for merino wool-growers and non-merino wool-growers. Section 36(6) ensures that these trusts nominated to hold shares or rights on behalf of growers are each treated as nominees for income tax purposes.

Without these provisions, the tax losses and imputation credit balances may have been forfeited as part of the restructuring.

Section 37 of the Act provided for the transfer of 7.2 percent (the merino wool-growers' share of the Board) of the tax losses to be carried forward by the Board immediately prior to the restructuring day to Merino Grower Investments Ltd.

Statutory producer board tax rules

Section 62(2) of the Act provides that on restructuring day, the Board ceased to be a statutory producer board for tax purposes. Section 38 of the Act, however, allows Wool Board Disestablishment Company Ltd to be treated as a statutory producer board for tax purposes for the period in which it continues to be responsible for the administration of the wool levy imposed under this Act.

Application date

Sections 11, 36, 37, 38, 39 and 62(2) apply from the day after the date on which the Act received the Royal assent (7 July 2003).

Detailed analysis

This part of the item provides an explanation in broad terms of the various steps of the restructuring plan relating to the distribution of the assets of the Board to the wool-growers and the associated tax implications.

Merino wool-growers

Before the restructuring day, the Board converted its loan to Merino Grower Investments Ltd into mandatory convertible notes and these notes were converted, as part of the restructuring plan, into shares in that company.

On the restructuring day, Wool Board Disestablishment Company Ltd issued exchangeable shares and redeemable shares (both non-voting shares) to merino wool-growers on the basis of sheep numbers. Section 36(1) of the Act ensures that issue of these shares does not constitute a taxable event.

Wool Board Disestablishment Company Ltd redeemed the exchangeable shares by transferring the mandatory convertible notes it held in Merino Grower Investments Ltd to the merino wool-growers. Section 36(5) of the Act ensures that the proceeds of this redemption (the mandatory convertible notes) are not treated as gross income. These mandatory convertible notes converted into shares in Merino Grower Investment Ltd. Section 36(4) of the Act ensures that the change in ownership of Merino Grower Investments Ltd from the Merino Distribution Trust to the merino wool-growers who received those shares did not constitute a breach in the shareholding continuity rules.

Wool Board Disestablishment Company Ltd redeemed the redeemable shares for cash. Wool Board Disestablishment Company Ltd was able to use its available subscribed capital to ensure that the redemption of these shares was not a taxable dividend.

Non-merino wool-growers

On the restructuring day, Wool Board Disestablishment Company Ltd issued exchangeable shares, redeemable shares (both non-voting shares) and ordinary shares (voting shares) to non-merino wool-growers based on sheep numbers. Section 36(1) of the Act ensures that issue of these shares does not constitute a taxable event.

Wool Equities Ltd was granted an option to purchase the ordinary shares in Wool Board Disestablishment Company Ltd when they were issued. Wool Equities Ltd exercised this option, thereby acquiring all the ordinary shares in Wool Board Disestablishment Company Ltd. The effect of this is that Wool Board Disestablishment Company Ltd became a subsidiary of Wool Equities Ltd, thereby allowing both companies to be able to group for tax purposes. Section 36(2) of the Act ensures that the non-merino wool-growers are treated as having held the shares in Wool Board Disestablishment Company Ltd at all times before the restructuring day.

Wool Board Disestablishment Company Ltd redeemed the exchangeable shares for the shares it owns in Wool Equities Ltd. The result is that the non-merino growers own all the shares in Wool Equities Ltd. Section 36(5) of the Act ensures that the proceeds of this redemption (the shares in Wool Equities Ltd) are not treated as gross income.

Wool Board Disestablishment Company Ltd redeemed the redeemable shares for cash. Wool Board Disestablishment Company Ltd was able to use its available subscribed capital to ensure that the redemption of these shares was not a taxable dividend. Non-merino wool-growers can reinvest all or some of the proceeds from this redemption in a further issue of shares by Wool Equities Ltd.

FRINGE BENEFIT TAX – PRESCRIBED RATE OF INTEREST ON LOW-INTEREST, EMPLOYMENT-RELATED LOANS

The prescribed rate of interest used to calculate fringe benefit tax for low-interest employment-related loans has decreased from 7.74% to 7.33% for the quarter beginning 1 July 2003.

The rate is reviewed regularly to ensure it is in line with the Reserve Bank's survey of first mortgage interest rates. It was last changed with effect from the quarter beginning 1 April 2003.

The new rate was approved by Order in Council on 25 August 2003.

Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations (No 2) 2003/214

SCREEN PRODUCTION INDUSTRY – WITHHOLDING PAYMENTS

A correction has been made to the Income Tax (Withholding Payments) Amendment Regulations 2003 to ensure that the withholding tax rate of 20 cents in the dollar applies only to payments to New Zealand resident independent contractors. The rate applying to contract payments to non-resident contractors will remain at 15 cents in the dollar.

The amendment will apply from 8 September 2003, the date from which the original Regulation applies.

The amendment was approved by Order in Council on 1 September 2003.

Income Tax (Withholding Payments) Amendment Regulations (No 2) 2003/Number 215

REGULAR FEATURES

DUE DATES REMINDER

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

November 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

7 Provisional tax instalments due for people and organisations with a March balance date

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

28 GST return and payment due

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

YOUR CHANCE TO COMMENT ON DRAFT TAXATION ITEMS BEFORE THEY ARE FINALISED

This page shows the draft binding rulings, interpretation statements, standard practice statements and other items that we now have available for your review. 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 **www.ird.govt.nz.**
On the homepage, click on "The Rulings Unit welcomes your comment on drafts of public rulings/interpretation statements before they are finalised . . ." Below the heading "Think about the issues", click on the drafts that interest you. You can return your comments by internet.

Name ____________________

Address ____________________

____

	Standard practice statement	*Comment deadline*
☐	Section 17 notices	31 October 2003

	Draft questions we've been asked	*Comment deadline*
☐	Qualifying trusts – Income tax underpayment	31 October 2003

Items are not generally available once the comment deadline has passed

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

Affix
Stamp
Here

The Manager (Field Liaison)
Adjudication & Rulings
National Office
Inland Revenue Department
PO Box 2198
Wellington