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CONTENTS

Get your TIB sooner on the internet 2

Binding rulings

Product ruling – BR Prd 05/05 3

Product ruling – BR Prd 05/06 8

Product ruling – BR Prd 05/07 12

Product ruling – BR Prd 05/08 15

Product ruling – BR Prd 05/09 19

Legislation and determinations

Livestock values – 2006 national standard costs for specified livestock 23

Questions we've been asked

FBT – Value of brokerage provided by sharebrokers to employees 25

The meaning of "benefit" for FBT purposes 26

Records for controlled foreign companies or foreign investment funds to be available in English 28

New legislation

Order in Council: Student loan scheme – repayment and interest write-off thresholds for the 2006-07 tax year 29

Legal decisions – case notes

Reinstatement of cancelled GST registration upheld by Court of Appeal
Lopas and McHerron v The Commissioner of Inland Revenue 30

Strike out of judicial review
Ron West Motors (Otahuhu) Ltd v TRA and The Commissioner of Inland Revenue 31

Taxpayer appeal against capital expenditure decision
Fullers Bay of Islands v The Commissioner of Inland Revenue 32

Regular features

Due dates reminder 34

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BINDING RULINGS

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

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

For full details of how binding rulings work, see our information booklet *Adjudication & Rulings, a guide to binding rulings (IR 715)* or the article on page 1 of *Tax Information Bulletin* Vol 6, No 12 (May 1995) or Vol 7, No 2 (August 1995).

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

PRODUCT RULING – BR PRD 05/05

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 The New Zealand Guardian Trust Company Limited as Trustee of the AMP Superannuation Tracker Fund.

Taxation Laws

All legislative references are to the Income Tax Act 2004 unless otherwise stated.

This Ruling applies in respect of sections BD 4(2), DA 2(1), DB 17, FI 1, FI 2 and the definition of "superannuation fund" in section OB 1.

This Ruling does not consider how (if at all) sections CH 1, DB 40 and ED 1 apply to the Arrangement.

The Arrangement to which this Ruling applies

The Arrangement is the redemption of Units in the AMP Superannuation Tracker Fund ("the Fund") by members who receive securities for their redemption, and those shares are trading stock or revenue account property of that member. Further details of the Arrangement are set out in the paragraphs below:

1. The AMP Superannuation Tracker Fund ("the Fund") is a registered superannuation scheme under the Superannuation Schemes Act 1989. The Fund is not listed on the New Zealand stock market ("NZX").

2. The Fund has been designed to provide members with a simple and cost effective method of investing in a portfolio with a performance broadly representative of the New Zealand share market.

3. The Trustee of the Fund is the New Zealand Guardian Trust Company Limited ("the Trustee") although the Trust Deed contains provisions for the retirement or removal and replacement of the Trustee.

4. The Manager of the Fund is AMP Investment Management (N.Z.) Ltd ("the Manager"). The Manager invests the investors' contributions into the Fund. The Investment Manager/ Promoter of the Fund is AMP Capital Investors (New Zealand) Ltd ("the Investment Manager"). The Investment Manager purchases securities in the Index, described more particularly in paragraphs 6–8 below. Both the Manager and the Investment Manager are owned by AMP Ltd, incorporated in New South Wales.

5. The Fund was established, as a wholesale registered superannuation scheme, principally for the purpose of paying benefits to persons who are trustees of superannuation schemes registered under the Superannuation Schemes Act 1989 and who elect to invest in the Fund.

Investment policy

6. According to the Members' Booklet of the Fund, dated 29 June 2001:

> The objective of the Scheme is to track the Russell/Ord Minnett [JB Were) Tradeable Index (the Tradeable Index) as closely as practical. This will be achieved by holding constituent company securities which, as far as possible, match the composition of the Tradeable Index. ...
>
> The Manager and the Trustee can adopt such other index of securities as they agree from time to time.

7. In accordance with the current Members' Booklet (not being materially different to the draft provided to the Commissioner on 17 January 2005), the Manager and the Trustee have agreed to adopt the NZSX 50 Index ("the Index") administered by New Zealand Exchange Limited. The transition to tracking the Index occurred on 31 January 2005 (refer to paragraph 24(h) below), and the Fund commenced tracking the Index on 1 February 2005. Apart from permitted investments of the cash pool, the Fund will, commencing on 1 February 2005, only invest in the securities that make up the Index and will continue to track the Index as near as practicable irrespective of whether the sale of the shares will give rise to a profit or loss.

8. Despite the Trust Deed providing that the Manager and Trustee can invest in other Indexes, and apart from permitted investments of the cash pool, the Fund will, having made the transition to the Index, only invest in the securities that make up the Index.

9. The Fund is required to buy and sell shares as required to ensure that it continues to correspond as near as practicable to the Index. Such buying and selling will not be motivated by any intention to derive a profit or gain from such sales. In this regard, Clause 5.3.1A of the Trust Deed states:

> The Fund shall seek to track the Index by investing in Constituent Company Securities as near as practically possible to their weightings in the Index and the Trustee's primary investment duty shall be to seek to achieve this purpose. All other investment duties (express or implied) shall be construed subject to this duty. The Fund and the Trustee shall not have an intention to profit from holding, acquiring or selling Constituent Company Securities.

10. The Trustee and the Manager have confirmed that, to the best of their knowledge, the Fund has complied with the previous rulings (BR Prv 05/02, and BR Prd 05/01), relating to the Fund.

Adjustments to the Fund

11. The Fund is rebalanced in the following circumstances:

    (a) The Fund's portfolio is monitored regularly, being daily, to ensure that it is tracking the Index. The reference to "Fund's portfolio" means the Constituent Companies held by the Fund.

    (b) The Manager will rebalance the Fund to the Index following any adjustments to the Index. Such rebalancing will occur as soon as possible but in any case within three business days of a change to the composition of the Index.

Management and operation of the Fund

Borrowing

12. Clause 10.3.2 of the Trust Deed provides that:

> The Trustee may not borrow any money for the purposes of the Plan otherwise than for the purpose of satisfying payment of any Administration Expenses in which case the Trustee may borrow money on terms considered appropriate by the Trustee and may charge any or all of the Plan to secure the repayment of any moneys borrowed.

Hedging

13. This Fund only tracks shares quoted on the NZX and hence the Fund will purchase shares in New Zealand dollars. Accordingly, the Fund will not be exposed to foreign exchange risks. The Fund does not enter into any hedging transactions.

Contributions to the Fund

14. Contributions to the Fund will be by way of parcels of securities or cash. Cash may be accepted in the following circumstances:

    (a) where there is a contemporaneous redemption against which the contribution can be netted off by receiving cash into the Fund and then paying it out on the redemption, or

    (b) to the extent the application cannot be made in securities due to uneven parcel sizes provided the cash pool remains below 0.5% of the total assets of the Fund and, except where the situations listed in paragraph 16 below arise or where the cash is committed to fund an obligation that was known at the time of receipt of the subscription, the cash is converted to Constituent Company Securities as soon as practicably possible.

15. Members wishing to contribute cash may be required to purchase a parcel of securities through a separate arrangement with the Manager, or through other intermediaries (such as brokers and financial advisors).

Cash investments held by the Fund ("cash pool")

16. The proportion of the Fund's assets to be held as the cash pool will not exceed what is strictly necessary in order to fulfil the purposes of the cash pool (as stated in paragraph 17 of this Ruling), and will not in any event exceed 0.5% of the total assets of the Fund, except if:

    (i) the Fund receives a large cash contribution (provided the cash is invested as soon as possible and in any event within three business days), or

    (ii) a member requests a large cash redemption (provided the cash is distributed within three business days of the sale of securities), or

    (iii) the Fund receives a large cash inflow from or in respect of a Constituent Company, such as a distribution due to a pro-rata buy-back or takeover or a change in the Constituent Companies of the Index (provided the cash is invested as soon as possible and in any event within three business days), or

    (iv) the Fund holds cash as a result of disposing of securities in the course of and for the purposes of winding up the Fund.

17. The purpose of the cash pool as set out in Clause 5.2.5 of the Trust Deed is:

> The Trustee may maintain or invest in Cash in any amount representing up to five percent (5%) of the Current Fund Value at any time, PROVIDED THAT the investment in Cash shall only be used to facilitate the easier administration of the Fund and

> to reduce the number of transactions required to be made or to facilitate redemptions from time to time, but may not be used by the Manager or the Trustee to increase the performance of the Fund by maximising the holding of securities considered to be likely to give a high return or minimising the holding of securities considered likely to give a low return.

18. "Cash", as defined in Clause 3 of the Trust Deed includes:

> deposits, or negotiable instruments, in each case having maturities which are not later than the times at which the proceeds of realisation thereof are expected to be required, and on which there is full indefeasible liability of:
>
> (a) a New Zealand registered bank (having the meaning given to that term by the Reserve Bank of New Zealand Act 1989) approved by the Manager for the purpose; or
>
> (b) the New Zealand government.

19. The size and operation of the cash pool will be strictly managed so as to reflect its threefold purpose of:

    (a) allowing funds to accumulate to an appropriate amount for investment, and

    (b) minimising the number of equity security sale and purchase transactions, and

    (c) managing the liquidity of the Fund in respect of meeting its anticipated liabilities and withdrawals.

20. When the cash held by the Investment Manager reaches the minimum investment level, it will be applied to acquire securities to track the Index as soon as possible and in any event within three business days. The Manager has advised that the minimum amount required to enable the purchase of every security in the Index in a marketable and economically sensible sized parcel is approximately $150,000, but may reduce where a lower amount can permit transaction costs to be maintained at the current level (or a level not materially different).

21. It is not envisaged that the amount of cash required to enable the purchase of securities in a marketable and economically sensible sized parcel will change from $150,000 unless there are improvements in share trading systems that make it economic to trade in smaller parcels of shares. This would be beneficial for the Fund as it would be able to invest surplus cash sooner and keep the cash levels in the Fund at a lower level than might otherwise be the case if the Fund is confined to a predetermined minimum parcel size.

22. The Fund does not normally hold cash equivalents. Rather, the cash amounts are normally held in bank deposits and interest is paid on these deposits.

Dividend reinvestment

23. In the event of a dividend reinvestment option being available to the Trustee, the Manager will only accept such an option if it is consistent with tracking the Index. In all other cases, the Manager will decline the option and will always accept the cash dividend that will be immediately allocated to members.

Events that trigger acquisitions or realisations

24. There are certain reasons or events when investments held by the Fund will have to be bought or sold. The Trustee will only dispose of securities (other than cash pool investments):

    (a) If the Fund is voluntarily or involuntarily wound up or if the Trustee is replaced (and this of itself means that there is a technical disposal of securities to the new Trustee and the new Trustee assumes ownership of the same securities held by the previous Trustee immediately before the Trustee is replaced).

    (b) If there is a change in the Index composition and the composition of the Fund no longer tracks the Index or when the Fund is otherwise required to buy and sell securities to maintain tracking.

    (c) When transferring securities to a member if the member redeems Units for securities.

    (d) Where there is no option available to receive dividends in the form of cash, and dividends are received in the form of bonus securities and are converted to cash.

    (e) To satisfy a legal claim against the Fund or Trustee or to meet expenses of the Fund, but only to the extent to which such a claim or expense cannot be met from existing resources.

    (f) If a member or members require cash on redemption of Units and such redemption cannot be met from the cash pool.

    (g) Where securities are purchased in error.

    (h) As a consequence of the Fund ceasing tracking the Russell/JB Were Tradeable Index and commencing tracking the NZSX 50 Index.

Redemption of Units

25. A member is only able to dispose of their Units by redeeming them. A member may redeem Units subject to the conditions in Clause 8 of the Trust Deed. Clause 8 requires redemptions to be for amounts of at least $10,000 or all of a member's Units and no member is to be left with less than $100,000 worth of Units. The redemption can be in the form of cash and/or cash equivalents and/or securities.

26. The Units in the Fund are valued on the basis of the market value of the securities and other assets that the Fund holds.

27. Redemptions are usually made through the transfer of Constituent Company Securities (equal to the value of the Units being redeemed and may also contain a small cash balancing item) but may, in the circumstances described below, be made in cash.

28. In the following circumstances a redemption will be made in cash (where that cash is not committed for other purposes):

    (a) where there is a contemporaneous contribution against which the redemption can be matched, or

    (b) where the cash is sufficient to fund the redemption in full, that redemption will be made from the cash pool, and

    (c) where the cash is not sufficient to fund the redemption in full, the balance of the redemption will be made from securities in the proportions that will ensure that the Fund will continue to match the composition and weighting of the Index as near as practicably possible.

29. Clause 8.3.2 of the Trust Deed provides:

> Every Benefit payable under this clause 8.3 shall be determined by multiplying the Redemption Price calculated on the date of acceptance by the Manager by the number of Units redeemed and become payable to the Member net later than ten (10) Business Days following the date on which the Manager receives the Benefit request or on any later redemption date requested by the Member.

30. Redemption Price is defined in clause 3 of the Trust Deed to mean the "Current Unit Value" less the "Exit Fee".

31. Current Unit Value is defined in clause 3 of the Trust Deed as:

> ... on any date an amount that is arrived at by dividing the Current Fund Value by the number of Units on issue on such date ...

32. The Current Fund Value is defined in clause 3 of the Trust Deed as:

> The amount calculated by adding as at any time when a valuation is required in relation to the Fund:
>
> (a) the total of the market value of all Cash, units in the AMP Investments' Tracker Fund and investments of the Fund determined pursuant to clause 6; and
>
> (b) the income of the Fund due but not yet received; and
>
> (c) any other amounts which, in the opinion of the Manager, should be included for the purposes of making a fair and reasonable determination of the value of the Fund having due regard to duly accepted accounting practice and accounting principles from time to time;
>
> and deducting therefrom such amounts:
>
> (d) as are required to meet liabilities properly attributable to the Fund (actual or contingent and not otherwise allowed for in determining the value of any asset) to the extent that the Manager has decided that provision should be made in the accounts of the Plan;
>
> (e) as represent Administration Expenses payable by the Trustee or the Manager; and
>
> (f) which, in the opinion of the Manager, should be included for the purpose of making a fair and reasonable determination of the current value of the Fund having due regard to generally accepted accounting practice and accounting principles current from time to time.

33. Clause 3 of the Trust Deed provides that Market Value in relation to a Constituent Company Security in the Index means:

> ... its value as in the Index at any relevant time.

34. Exit Fee is defined in clause 3 of the Trust Deed to mean:

> …such sum, if any, as the Manager in its absolute discretion may determine (either generally or in relation to a particular Benefit) to be a fair fee payable in relation to the relevant Benefit to provide for the likely per Unit cost of realising Assets to meet that Benefit, having regard to the Manager's estimate of the aggregate of all costs, charges, expenses, disbursements, commissions, brokerage and other usual fees which would be likely to be incurred in respect of the sale or disposal of Assets on the date of calculation of the Redemption Price of Assets to fund a unit's Redemption Price were sold or disposed of on such date.

Suspension of redemptions

35. Clause 8.5 of the Trust Deed provides that the Manager can suspend redemptions in certain circumstances up to a period not exceeding 20 business days. The Fund will not utilise the power to suspend the redemption of Units except in exceptional circumstances (where and to the extent that it is necessary to do so) being:

    (i) if the Fund is unable to convert sufficient assets into cash, to meet a redemption request, or

    (ii) if the market value of the Units at the time is not a true reflection of the actual value of the Units, due to a suspension in trading of any Constituent Company Securities on any exchange, or

(iii) if, for reasons beyond its control, the Manager is unable to calculate the redemption price.

Any such suspension will be for a maximum period of three business days, unless an exceptional circumstance occurs that is beyond the control of the Trustee and the Manager of the Fund, in which case the suspension shall be only for such period as is strictly necessary for the Fund and/or the Manager to recover from that event.

Utilisation of member expenses for tax purposes

36. The Trust Deed has been amended to allow the Trustee to credit a Member's Account with Units in recognition of any tax deduction that the Plan has received as a result of an election by that member under section DI 3(2) of the Income Tax Act 1994. The Trust Deed was amended, by the Second Deed of Amendment dated 1 February 2002, by inserting Clause 12A. Sub-clause 12A.l, which is relevant for the purposes of the Ruling, provides that:

> Where a Member has made an election under section DI 3(2) of the Income Tax Act 1994 ("section DI 3(2) ") that any expenditure, which is incurred by the superannuation scheme for which the Member is a trustee (or, in respect of a superannuation scheme constituted under an Act of Parliament, the person appointed to administer the superannuation scheme), be treated as if it were expenditure incurred by the Plan and the Plan has received a tax deduction as a result of that election, the Trustee shall credit to the Member Account of the relevant Member such number of Units as the Trustee considers equitable to recognise such tax deduction. For the avoidance of doubt, the number of units to be issued in normal circumstances would be calculated by reference to the amount determined by dividing the amount of any tax benefit which the Manager considers arises from the tax deduction by the Issue Price applying on the Business Day on which the tax benefit is considered by the Manager to arise.

37. The Fund will always issue Units according to the above Clause and there will be no discretion as to whether the Fund will in fact issue Units in accordance with the above Clause.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following Conditions:

a) The Fund is an investment vehicle primarily for investment into by superannuation funds, being superannuation schemes registered under the Superannuation Schemes Act 1989, which are themselves either:

(i) widely-held investment vehicles for direct investment by natural persons, or

(ii) vehicles for investment (directly or indirectly) by other superannuation funds that are widely-held vehicles for direct investment by natural persons.

b) The Fund operates in accordance with its Trust Deed dated 10 February 1999, a Members' Booklet not materially different to the draft provided to the Commissioner on 17 January 2005, the Deed of Arrangements dated 10 February 1999 (as amended on 27 August 2001), the Deed of Amendment dated 30 January 2002, and the Second Deed of Amendment dated 1 February 2002.

c) The Fund is a registered superannuation scheme under the Superannuation Schemes Act 1989.

d) The Fund only tracks the Index.

e) In determining the market value of a security at any time the last sale price for that security, as quoted on the New Zealand stock market at that time, shall be used.

f) The Manager, in determining the Members' entitlement to securities on redemption of Units in the Fund under clause 8.3 of the Trust Deed, shall use the market value of those securities at the valuation time (as defined in the Trust Deed).

g) The amounts derived by the Member from the subsequent sale or disposal of securities received on redeeming Units in the Fund will be assessable income of the Member.

h) Members do not acquire Units in the Fund for the purpose of acquiring securities.

i) Units in the Fund are not tradeable on a secondary market.

j) The trust is established by its Trust Deed mainly for the purpose of paying benefits to superannuation funds.

How the Taxation Laws apply to the Arrangement

Subject in all respects to any assumption or condition stated above, and the qualification in respect of sections CH 1, DB 40 and ED 1 under the heading "Taxation Laws" above, the Taxation Laws apply to the Arrangement as follows:

- Pursuant to sections FI 1 and FI 2, the cost of any securities acquired by a member on redemption of Units in the Fund is the market value of those securities on the date the member acquires the securities.
- Section DA 2(1) does not apply to the cost of any securities acquired by a member on redemption of units.

- The cost of a security acquired by a member on the redemption of Units (being the market value of the security on acquisition) is an allowable deduction under section DB 17. It is deductible in the income year in which the Units are redeemed under section BD 4(2).

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 October 2005 and ending on 30 September 2008.

This Ruling is signed by me on the 2nd day of December 2005.

Howard Davis
Senior Tax Counsel

PRODUCT RULING – BR PRD 05/06

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 The New Zealand Guardian Trust Company Limited as Trustee of the AMP Superannuation World Index Fund.

Taxation Laws

All legislative references are to the Income Tax Act 2004 unless otherwise stated.

This Ruling applies in respect of sections BD 2, BD 4(2), DA 1(1), DA 2(1), DB 17, FI 1, FI 2, HH 3(5) and the definition of "superannuation fund" in section OB 1.

This Ruling does not consider how (if at all) sections CH 1, DB 40 and ED 1 apply to the Arrangement.

The Arrangement to which this Ruling applies

The Arrangement is the redemption of Units in the AMP Superannuation World Index Fund ("the Fund") by members who receive securities for their redemption, and those shares are trading stock or revenue account property of that member. Further details of the Arrangement are set out in the paragraphs below.

1. The Fund is a registered superannuation scheme under the Superannuation Schemes Act 1989.

2. The Fund invests in securities of those companies that are included in the AMP World Index (the "AMP Index" or the "Index"). The AMP Index is a customised version of the Morgan Stanley Capital International World Index (the "MSCI World Index") and tracks those securities in the MSCI World Index which are from "Grey List" countries if the market capitalisation of the country's securities included in the MSCI Index represents at least 1% of the MSCI Index. The Fund has been designed to provide members with a simple and cost efficient method of investing in a portfolio with a performance broadly representative of the world share market.

3. The Trustee of the Fund is the New Zealand Guardian Trust Company Limited ("the Trustee"), although the Trust Deed contains provision for the retirement and replacement of the Trustee.

4. The Manager of the Fund is AMP Investment Management (N.Z.) Limited ("the Manager"), a wholly owned subsidiary of AMP Limited.

5. Clause 5.3.1 A of the Trust Deed provides:

   > The Fund shall seek to track the Index by investing in Constituent Company Securities as near as practicably possible to their weightings in the Index and the Trustee's primary investment duty shall be to seek to achieve this purpose. All other investment duties (express or implied) shall be construed subject to this duty. The Fund and the Trustee shall not have an intention to profit from holding, acquiring or selling Constituent Company Securities.

6. The Trust Deed also ensures that any statutory superannuation schemes (ie any superannuation scheme constituted under an Act of Parliament or government superannuation scheme) can also join the Fund.

7. The Fund is required to buy and sell shares as required to ensure that its portfolio continues to correspond as near as practicably possible to the Index. Such buying and selling will not be motivated by any intention to derive a profit or gain from such sales. The sole purpose of the Fund will be to continue to track the Index as near as practicably possible irrespective of whether the sale of shares will give rise to a profit or loss.

8. The beneficial interest in the Fund is divided into Units. Every Unit confers an equal interest in the Fund, but does not confer any interest in any particular investment of the Fund.

9. The Applicant and the Manager have confirmed that, to the best of their knowledge, the Fund has complied with the previous rulings (BR Prv 04/69 and BR Prd 02/08) relating to the Fund.

The Trust Deed and Members Booklet for the Fund

10. The terms of the Fund are provided in the Trust Deed. There are no clauses in the Trust Deed or

Rules of the Fund or any other documents that operate differently for specific members or groups of members.

Membership

11. The Fund was established as a wholesale registered superannuation scheme in which any other superannuation scheme can invest. The Fund was not established by any particular financial institution as an investment vehicle for that institution.

Date of adjustments

12. The Fund is rebalanced every quarter and other adjustments are made as a result of mergers, takeovers, rights issues and share buy-backs when those events occur.

Mergers, takeovers, share buy-backs and right issues

13. The Index may be adjusted from time to time because of mergers, takeovers, share buy-backs, distributions of capital, cash issues, and substitutions of companies in the Index. With the exception of any situation where shares in a Constituent Company are compulsorily acquired pursuant to any companies legislation, listing rules or takeover code requirements, in the event of a merger or takeover, the Manager will adjust the Fund portfolio at a time as close as practically possible (but in any event within three business days) to the time the Index is adjusted. The Fund will not accept an offer, unless as a consequence of not accepting the offer, the Fund would track the Index less accurately than if it had accepted the offer.

14. In the event of a share buy-back by a Constituent Company of the Index, the Manager will adjust the Fund portfolio at a time as close as practicably possible (but in any event within three business days) to the time the Index is adjusted. This adjustment will not be made through electing to participate in a buy-back scheme of a Constituent Company, except if the Fund is able to accept a buy-back offer at the same time as an Index adjustment for that Constituent Company occurs.

15. In the event of any rights issue by a Constituent Company, the Manager will hold the entitlement if the entitlement is included in the Index. If the entitlement is not included in the Index, but the securities the subject of the entitlement will be immediately included in the Index, the Manager will retain the entitlement and take up the securities. If the Manager does not know whether the securities the subject of the entitlement will be included in the Index, the Manager will sell the entitlement at the earliest possible time and reinvest the proceeds in the Constituent Companies to track the Index.

Events that trigger acquisitions or realisations

16. Initial contributions to the Fund are made through the Manager. The Manager deposits the cash contributions from the members into the Fund. The Manager invests these cash contributions, in return for which the Manager receives Units on behalf of members. The Manager subcontracts the function of converting contributions to parcels of shares in companies included in the Index to Henderson Fund Management plc (“the Investment Manager”), which is based in the United Kingdom. The Investment Manager will purchase securities in the Index according to the pre-determined rules for calculating and maintaining the AMP Index set out in the current private ruling for the Fund (BR 04/69).

17. Under the Trust Deed, the Manager is responsible for further issues of Units in the Fund. The Manager is also responsible for Unit redemptions.

18. Dividends, net of any fees or expenses of the Fund, that accrue to the portfolio of shares held by the Fund will be invested in securities that constitute the Index or held in cash pending the investment of that dividend.

19. There are certain reasons or events when investments held by the Fund will have to be bought or sold. The Fund will only sell or otherwise dispose of securities in the following circumstances:

    - If the Fund is voluntarily or involuntarily wound up, or if the Trustee is replaced (and this of itself means that there is a technical disposal of securities)
    - If there is a change in the AMP Index composition and the composition of the Fund no longer tracks the Index or when the Fund is otherwise required to buy and sell securities to maintain tracking
    - On the redemption of Units in order to pay benefits to members
    - Where proceeds are received by the Fund in the form of securities
    - Where there is no election available and where dividends are received in the form of bonus securities and they are converted to cash
    - Where securities are purchased in error
    - To satisfy a legal claim made against the Fund or the Trustee
    - To meet any expenses of the Fund, which are authorised by clause 10.3.10 or 11.3.2 of the Trust Deed.

20. Clauses 10.3.10 and 11.3.2 provide for the Trustee and Manager to be reimbursed from the Fund for all Administrative Expenses (as defined in the Trust Deed) incurred by them.

Payment of benefits

21. A member is only able to dispose of its Units by requesting the Manager to redeem the Units for the purpose of paying a benefit to that member. A member may redeem Units subject to the conditions in clause 8 of the Trust Deed. Clause 8.3.3 requires redemptions to be for amounts of at least $10,000 or all of a member's Units and no member is to be left with less than $100,000 worth of Units. The Manager may also suspend redemptions in the limited circumstances noted at paragraph 31 below. The redemption can be in the form of cash and/or cash equivalents and/or securities. Even though the Trust Deed gives the Manager a general discretion to redeem by cheque or the transfer of Constituent Company Securities or a combination of them (clause 8.14 of the Trust Deed), redemption in securities will only arise at the request of the member (ie redemption in securities will not arise at the discretion of the Manager/Trustee). In addition, the Manager will not exercise this discretion with a view to increasing the performance of the Fund in any way. Where a member requests a redemption in securities the Manager will only decline a request for redemption in securities due to size constraints (ie the units held by the member is small and as such a parcel of securities cannot be formed).

22. The Units in the Fund are valued on the basis of the market value of the securities and other assets that the Fund holds.

23. Redemptions will be made from the cash pool if sufficient funds are available, otherwise redemptions will be financed from the sale of securities. In addition, following a redemption, the cash pool will not normally be topped up and there is no specified period of time in which the cash pool will be injected with further funds. Accordingly, if there is insufficient cash to pay a redemption if it arises, the redemption will be financed through the sale of securities.

24. Members redeem Units directly with the Fund, with the Manager acting on behalf of the Trustee (ie members do not sell their Units to the Manager who then redeems them with the Fund).

25. Clause 8.3.2 of the Trust Deed provides:

> Every Benefit payable under this clause 8.3 shall be determined by multiplying the Redemption Price calculated on the date of acceptance by the Manager by the number of Units redeemed and become payable to the Member not later than ten (10) Business Days following the date on which the Manager receives the Benefit request or on any later redemption date requested by the Member.

26. Redemption Price is defined in clause 3 of the Trust Deed to mean the "Current Unit Value" less the "Exit Fee".

27. Current Unit Value is defined in clause 3 of the Trust Deed as:

> ... on any date an amount that is arrived at by dividing the Current Fund Value by the number of Units on issue on such date ...

28. The Current Fund Value is defined in clause 3 of the Trust Deed as:

> The amount calculated by adding as at any time when a valuation is required in relation to the Fund:
>
> (a) the total of the market value of all Cash, units in the AMP Investments' World Index Fund and investments of the Fund determined pursuant to clause 6; and
>
> (b) the income of the Fund due but not yet received; and
>
> (c) any other amounts which, in the opinion of the Manager, should be included for the purposes of making a fair and reasonable determination of the value of the Fund having due regard to duly accepted accounting practice and accounting principles from time to time, and deducting therefrom such amounts:
>
> (d) as are required to meet liabilities properly attributable to the Fund (actual or contingent and not otherwise allowed for in determining the value of any asset) to the extent that the Manager has decided that provision should be made in the accounts of the Plan;
>
> (e) as represent Administration Expenses payable by the Trustee or the Manager; and
>
> (f) which, in the opinion of the Manager, should be included for the purpose of making a fair and reasonable determination of the current value of the Fund having due regard to generally accepted accounting practice and accounting principles current from time to time.

29. Clause 3 of the Trust Deed provides that Market Value in relation to the Constituent Companies Securities in the Index means:

> ... the last sale price of that security on its home stock exchange at any relevant time (provided that the last sale price is the same as or higher than the current buy price and lower than the current sell price. In the event that the last sale price is lower than the then current buy price, then the market value is the then current buy price and in the event that the last sale price is higher than the current sell price then the market value is the current sell price).

30. Exit Fee is defined in clause 3 of the Trust Deed to mean:

> …such sum, if any, as the Manager in its absolute discretion may determine (either generally or in relation to a particular Benefit) to be a fair fee payable in relation to the relevant Benefit to provide for the likely per Unit

cost of realising Assets to meet that Benefit, having regard to the Manager's estimate of the aggregate of all costs, charges, expenses, disbursements, commissions, brokerage and other usual fees which would be likely to be incurred in respect of the sale or disposal of Assets on the date of calculation of the Redemption Price if Assets to fund a Unit's Redemption Price were sold or disposed of on such date.

Suspension of payment of benefits

31. Clause 8.5 of the Trust Deed provides that the Manager can suspend redemptions in certain circumstances up to a period not exceeding 20 business days. The Fund will not utilise the power to suspend the redemption of units except in exceptional circumstances (where and to the extent that it is necessary to do so) being:

    (i) if the Fund is unable to convert sufficient assets into cash, to meet a redemption request, or

    (ii) if the market value of the units at the time is not a true reflection of the actual value of the units, due to a suspension in trading of any Constituent Company Securities on any exchange, or

    (iii) if, for reasons beyond its control, the Manager is unable to calculate the redemption price.

    Any such suspension will be for a maximum period of three business days, except if an exceptional circumstance occurs that is beyond the control of the Trustee and the Manager of the Fund, in which case the suspension shall be only for such period as is strictly necessary for the Fund and/or the Manager to recover from that event.

32. The Fund has suspended redemptions on one occasion before. This suspension occurred as a result of the terrorist attacks in New York on 11 September 2001 as none of the underlying securities held by the Fund were being traded.

Ability to decline membership

33. Clause 7.1.5 of the Trust Deed provides that the Manager may accept or decline any application to become a member and shall not be required to give reasons for any such decision.

34. The Manager has never refused an application for membership. However, the Manager may in the future refuse applications for membership. The circumstances where this is likely to arise include:

    - where the applicant is not, or ceases to be, a registered superannuation scheme or statutory superannuation scheme, or
    - where accepting the application could result in the Fund breaching a Condition of the existing private ruling for the Fund (BR Prv 04/69 or any such replacement ruling).

Hedging

35. The Fund will not take any action to hedge or manage foreign exchange risks or exposures that arise from the investments of the Fund being held in non-New Zealand currencies. The Fund does not enter into any hedging transactions.

Borrowing

36. Clause 10.3.2 of the Trust Deed provides that the Trustee may not borrow any money for the purposes of the Fund otherwise than for the purpose of satisfying payment of any Administrative Expenses.

Cash investments held by the Fund

37. Although it is not an objective of the Fund to invest in cash securities, the Fund may hold cash to facilitate the easier administration of the Fund. The Fund will hold cash in the following instances:

    - Following the sale of securities in the course of tracking the Index, pending the reinvestment of that cash
    - Following a contribution to the Fund, pending the investment of that contribution
    - Following the receipt of a cash dividend or a non-cash dividend and its conversion to cash, pending the investment of that dividend
    - Following the sale of securities to meet a request to redeem units in cash
    - To accumulate the minimum amount of cash that will be used to purchase securities in a marketable and economically sensible sized parcel so as to minimise the Fund's transaction costs. The Manager has advised that this amount is presently US$1 million, but may reduce where a lower amount can permit transaction costs to be maintained at the current level (or a level not materially different)
    - Following the disposal of securities in the course of and for the purpose of winding up the Fund.

38. The proportion of the Fund's assets to be held as cash or cash equivalents will not be greater than what strictly arises out of the above described circumstances, and in any event will not exceed 1% of the total assets of the Fund, except if the Fund receives a large cash contribution (provided the cash is invested as soon as possible and in any event within three business days) or a member requests a large cash redemption (provided the cash is distributed within three business days of the sale of securities), or the Fund holds cash in the course of or for the purpose of winding up the Fund.

39. Cash equivalents must have a maturity date of six months or less. Cash equivalents will not include units in any unit trust or group investment fund.

40. It is not envisaged that the amount of cash required to enable the purchase of securities in a marketable and economically sensible sized parcel will change from US$1 million unless there are improvements in share trading systems that make it economic to trade in smaller parcels of shares. This would be beneficial for the Fund as it would be able to invest surplus cash sooner and keep the cash levels in the Fund at a lower level than might otherwise be the case if the Fund is confined to a predetermined minimum parcel size.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

a) The Fund is an investment vehicle primarily for investment into by superannuation funds, being superannuation schemes registered under the Superannuation Schemes Act 1989, which are themselves either:

   (i) widely-held investment vehicles for direct investment by natural persons, or

   (ii) vehicles for investment (directly or indirectly) by other superannuation funds that are widely-held vehicles for direct investment by natural persons.

b) The Fund operates in accordance with its Trust Deed dated 4 December 1998.

c) The Fund is a registered superannuation scheme under the Superannuation Schemes Act 1989.

d) The Fund only tracks the AMP World Index.

e) The market value of a security at any time shall be the value quoted on the relevant Stock Exchange at that time, as determined by the method provided in the definition of market value in Clause 3 of the Trust Deed.

f) The Manager in determining the Members' entitlement to securities on redemption of Units in the Fund under clause 8.3 of the Trust Deed, shall use the market value of those securities at the valuation time (as defined in the Trust Deed).

g) The amounts derived by the Member from the subsequent sale or disposal of securities received on redeeming Units in the Fund will be assessable income of the Member.

h) Members do not acquire Units in the Fund for the purpose of acquiring securities.

i) Units in the Fund are not tradeable on a secondary market.

j) The Fund is established by its Trust Deed mainly for the purpose of paying benefits to superannuation funds.

How the Taxation Laws apply to the Arrangement

Subject in all respects to any assumption or condition stated above, and the qualification in respect of sections CH 1, DB 40 and ED 1 under the heading "Taxation Laws" above, the Taxation Laws apply to the Arrangement as follows:

- Pursuant to section HH 3(5) any amounts (including securities) received by members as a result of redemption of Units in the Fund will not be income of the member.
- Pursuant to sections FI 1 and FI 2, the cost of any securities acquired by a member on redemption of Units in the Fund is the market value of those securities on the date the member acquires the securities.
- Section DA 2(1) does not apply to the cost of any securities acquired by a member on redemption of units.
- The cost of a security acquired by a member on the redemption of Units (being the market value of the security on acquisition) is an allowable deduction under section BD 2, section DA 1(1) and section DB 17. It is deductible in the income year in which the Units are redeemed under section BD 4(2).

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 October 2005 and ending on 30 September 2008.

This Ruling is signed by me on the 2nd day of December 2005.

Howard Davis
Senior Tax Counsel

PRODUCT RULING – BR PRD 05/07

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 SkyCity Consolidated Group – IRD No 63-352-039

Taxation Laws

All legislative references are to the Income Tax Act 2004 unless otherwise stated.

This Ruling applies in respect of:

- Section CD 2;
- Section CD 3(1);
- Section CD 4(1);
- Section CD 5(1).

The Arrangement to which this Ruling applies

The Arrangement is the issue of bonus shares by SkyCity Entertainment Group Ltd ("the Company") and the offer by the Company of an option to redeem the shares where shareholders elect to retain the shares. Further details of the Arrangement are set out in the paragraphs below.

1. The Company, a member of the SkyCity Consolidated Group ("the Group"), is a public company. The Company was incorporated in New Zealand. The Company has in excess of twenty thousand ordinary shareholders, a very small percentage of whom are likely to be taxable at the 39% marginal income tax rate.

2. The Company typically distributes two dividends a year to shareholders—an interim dividend paid in April and a final dividend paid in October. Until April 2005 dividends were paid in cash without a reinvestment option. The Company has previously fully imputed all dividends paid and will continue to do so in the period for which this Ruling applies. At the time the Company pays dividends it has often not had sufficient imputation credits in its imputation credit account to fully impute the dividends. In these circumstances it has paid further income tax sufficient to ensure there is not a debit balance in its imputation credit account at year end and it will continue, if necessary, to pay further income tax during the period for which this Ruling applies so that it will have sufficient imputation credits in its imputation credit account at the end of each imputation year to have fully imputed a cash dividend equal to the amount of the bonus issue which is not redeemed in each and every year during the term of the Arrangement.

3. The Board of the Company has been considering ways to maintain the Company distribution policy without reducing its equity base (i.e. ways to make distributions without negatively impacting cashflow). Maintenance of the equity base is a high priority for the Company at the current time due to recent expansion activity undertaken by the Group, including the acquisition of interests in casinos located in Christchurch and Darwin, Australia, an increase in its shareholding in SkyCity Leisure and Riverside Casino, as well as the development of its Adelaide facilities.

4. On 21 February 2005 the Company announced that it would introduce a new dividend reinvestment plan (DRP) under which shareholders may choose to reinvest all or part of their cash dividends in additional shares in the Company. The DRP was available in respect of the interim dividend for the 2005 financial year paid on 1 April 2005. Additional shares issued under the DRP were issued at their market price but in terms of the Offer Document dated 9 March 2005 the Board may determine that the shares will be issued at a discount. The Company has issued 1,212,484 new shares to shareholders under the DRP in respect of the dividend of $0.12 per share paid on 1 April 2005. These new shares represent 0.289 percent of the ordinary shares in the Company.

5. The Board has been considering an alternative mechanism that would encourage share uptake while still giving those shareholders who require a cashflow a mechanism by which to receive cash. Under the proposed plan bonus shares will be issued to all shareholders. The default option under the plan would be that shareholders retain the shares. It is intended that the Arrangement would continue in effect for an indefinite period in order to build up the shareholder equity base to a satisfactory level.

6. The estimated maximum amount which would be paid by the Company in respect of the redemption of shares under each bonus issue would be 5 percent of the market value of all shares in the Company.

Details of proposed bonus issue

7. The Company will issue a notice to shareholders informing them that they will be issued with bonus shares. The shares will be ordinary shares. The number of shares that a shareholder would receive would be based on:

   (i) the net amount the shareholder would have received if the Company had declared and paid a cash dividend rather than proceeding with the bonus issue; and

   (ii) the weighted average of the Company's share price for the five trading days following the relevant record date, less a discount of not more than 5% (and excluding brokerage fees). The discount will be included in the calculation to encourage share retention.

8. The number of bonus shares to be issued to a shareholder would be calculated in accordance with the following formula:

$$\text{Number of shares} = \frac{S \times A}{P \times D}$$

where:

S is the number of ordinary shares in the Company held by the shareholder before the bonus issue;

A is the amount per share (expressed in cents and fractions of cents (after deduction of any amounts of resident withholding, or other, taxes, if any)) which would have been distributed to the shareholder if the Company had instead made a cash distribution;

P is the weighted average sale price for the Company's shares (expressed in cents and fractions of cents) based on trades of those shares on the NZSX on the five trading days immediately following the relevant record date; and

D is calculated as (1 – Discount) expressed as a decimal.

(A mechanism for "roundings" will also be included in the above calculation.)

9. At the same time shareholders will be notified that the Company will provide an off-market facility available to allow shareholders to make an election to redeem their bonus shares for the equivalent cash value. The option to redeem will be made available at the time of notification of the issue of the bonus shares. The aggregate buyback price for a shareholder's bonus shares would be the number of shares issued to the shareholder multiplied by "(P x D)" in the above calculation.

10. The discount to be applied will depend on the market at the time of the announcement and will consequently be flexible depending on anticipated market reaction. The higher the discount the more likely shareholders will retain the shares. Conversely where the discount is too low there is less incentive to retain the shares. The Directors, in determining the level of discount, have sought to be fair to all shareholders by determining a rate which favours retention but does not appear to harshly penalise shareholders (through dilution) who have primarily invested for the regular cash flow.

11. The approximate timetable for each bonus issue and buy back (based on NZ Companies Act and NZSX Listing Rule requirements) would be as follows:

Day 1

Notice to NZX and ASX of proposed bonus issue (Appendix 7 NZSX Rules and ASX equivalent) including notice of value of bonus shares to be issued (as a $ value per share held).

Day 15 (first Friday at least 10 business days after Day 1)

Record date for Bonus Share entitlement.

Day 22 (5 business days after Day 15)

Determination of strike price for determining number of bonus shares to issue and resulting bonus share ratio.

Day 26 (say 4 days after day 22)

Details of bonus shares to be issued and buyback offer sent to shareholders. Shareholders given 14 days to elect whether to accept buy back offer.

Day 41 (15 days after Shareholders notified)

Date for shareholder acceptances of buy back offer.

Day 43

Issue of Bonus Shares and completion of buyback.

Day 45

Holding statements and payment cheque distributed.

Reasons for the structure of the Arrangement

12. The commercial advantages which the Company seeks to achieve from the Arrangement are as follows:

a) The reduction of the amount of the net cash outflow:

b) The maintenance as much as possible of the Company's equity base in light of the recent and planned business expansions;

c) The maintenance of the Company's policy of making two distributions a year to shareholders;

d) The provision of a mechanism for those shareholders who wish their share of profits to be retained within the Company:

e) The prevention of any negative impact on the Company's share price;

f) Due to the decrease in the dividends paid by the Company, the reduction of the amount of imputation credits used.

g) The provision of a mechanism for those shareholders who wish to receive cash.

13. The Company considers that, as with many New Zealand stock exchange listed companies, its dividend policy and perceptions of its dividend policy has a direct impact on the share price of the Company. The Company has historically maintained a bi-annual high yield dividend policy. As a result investors who require an income stream from their investments may be attracted to invest in the Company. The level of capital growth in the Company, however also may make it attractive to shareholders who are seeking a capital gain. The Company considers that if the redemption option were not available material numbers of shareholders, requiring income from their shares, might seek to exit the stock, thereby having a negative impact on share price. Historically where a Company has reduced its dividend payout ratio this has had a negative impact on the share price.

14. The share issue has been structured to maximise the proportion of shares retained. The Arrangement operates so as to issue shares to all shareholders and give them the option of redeeming within a set period. Shareholders would have two weeks to decide whether to accept the offer to redeem the shares. The Company considers that if shareholders are required to apply for redemption of the shares, the level of share uptake should increase as the default result for shareholders who do not act will be that they retain the shares.

15. The Company also considers that a bonus issue in lieu would be less well received by its shareholders and the investment market in general than the Arrangement. The Company considers, on reasonable grounds, that denying shareholders who do not respond to the notice of a bonus issue within a specified timeframe the opportunity to receive cash is unlikely to be viewed favourably by shareholders.

16. The market reaction to the change in policy is unknown but the Company would anticipate that approximately 40 – 50 percent of the amount of the bonus issue would be retained by shareholders.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

a) The Company will not elect that the bonus issue will be treated as a "taxable bonus issue" (as defined in section OB 1).

b) For the purpose of the Companies Act 1993 and the NZX Listing Rulings the Arrangement is a pro rata bonus issue to all existing shareholders followed by an acquisition by the Company of its own shares.

c) During the period of this Ruling the Company will have sufficient imputation credits in its imputation credit account at the end of each imputation year to have fully imputed a cash dividend equal to the amount of the bonus issue which is not redeemed in each and every year during the term of the Arrangement.

d) The advantages that the Company is seeking to obtain from implementing the Arrangement are as set out in paragraph 12 of this Ruling.

e) The primary reason that the Company has chosen to implement this Arrangement as compared to other similar arrangements, such as its existing DRP, is that it considers, on reasonable grounds, that it will result in materially more shares being retained by shareholders, and thus greater funds retained by the Company, than under alternative available arrangements, and the Company has no advice or information contrary to or inconsistent with this that has not been disclosed to the Rulings Unit. This has the purpose of enabling the Company to retain profits for the expansion of its business and encouraging and maximising the retention of bonus shares while preventing any negative impact on the Company's share price and preventing any negative perceptions by the market of the Company's profit distribution policy.

f) The Company has not taken individual shareholders' tax consequences into account in deciding to implement this Arrangement.

g) The Company has disclosed to the Rulings Unit all advice, analysis or other documentation relating to the purposes and advantages of implementation of this Arrangement.

How the Taxation Laws apply to the Arrangement

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

- The bonus issue is a non-taxable bonus issue (as defined in section OB 1) and does not constitute dividends as defined in sections CD 3(1), CD 4(1) and CD 5(1).

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 5 December 2005 and ending on 31 March 2009.

This Ruling is signed by me on the 5th day of December 2005.

Howard Davis
Senior Tax Counsel

PRODUCT RULING – BR PRD 05/08

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 SkyCity Consolidated Group – IRD No 63-352-039

Taxation Laws

All legislative references are to the Income Tax Act 2004 unless otherwise stated.

This Ruling applies in respect of:

- Section CB 1,

- Section CB 2;
- Section CB 3;
- Section CB 4;
- Section CD 2;
- Section CD 3(1);
- Section CD 4(1);
- Section CD 5(1);
- Section CD 14;
- Section CD 21;
- Section CD 42;
- Section FC 4;
- Section GC 22;
- Section LB 1;
- Section LB 2.

The Arrangement to which this Ruling applies

The Arrangement is the issue of bonus shares by SkyCity Entertainment Group Ltd ("the Company") and the offer by the Company of an option to redeem the shares where shareholders elect to redeem the shares. Further details of the Arrangement are set out in the paragraphs below.

1. The Company, a member of the SkyCity Consolidated Group ("the Group"), is a public company. The Company was incorporated in New Zealand. The Company has in excess of twenty thousand ordinary shareholders, a very small percentage of whom are likely to be taxable at the 39% marginal income tax rate.

2. The Company typically distributes two dividends a year to shareholders—an interim dividend paid in April and a final dividend paid in October. Until April 2005 dividends were paid in cash without a reinvestment option. The Company has previously fully imputed all dividends paid and will continue to do so in the period for which this Ruling applies. At the time the Company pays dividends it has often not had sufficient imputation credits in its imputation credit account to fully impute the dividends. In these circumstances it has paid further income tax sufficient to ensure there is not a debit balance in its imputation credit account at year end and it will continue, if necessary, to pay further income tax during the period for which this Ruling applies so that it will have sufficient imputation credits in its imputation credit account at the end of each imputation year to have fully imputed a cash dividend equal to the amount of the bonus issue which is not redeemed in each and every year during the term of the Arrangement.

3. The Board of the Company has been considering ways to maintain the Company distribution policy without reducing its equity base (i.e. ways to make distributions without negatively impacting cashflow). Maintenance of the equity base is a high priority for the Company at the current time due to recent expansion activity undertaken by the Group, including the acquisition of interests in casinos located in Christchurch and Darwin, Australia, an increase in its shareholding in SkyCity Leisure and Riverside Casino, as well as the development of its Adelaide facilities.

4. On 21 February 2005 the Company announced that it would introduce a new dividend reinvestment plan (DRP) under which shareholders may choose to reinvest all or part of their cash dividends in additional shares in the Company. The DRP was available in respect of the interim dividend for the 2005 financial year paid on 1 April 2005. Additional shares issued under the DRP were issued at their market price but in terms of the Offer Document dated 9 March 2005 the Board may determine that the shares will be issued at a discount. The Company has issued 1,212,484 new shares to shareholders under the DRP in respect of the dividend of $0.12 per share paid on 1 April 2005. These new shares represent 0.289 percent of the ordinary shares in the Company.

5. The Board has been considering an alternative mechanism that would encourage share uptake while still giving those shareholders who require a cashflow a mechanism by which to receive cash. Under the proposed plan bonus shares will be issued to all shareholders. The default option under the plan would be that shareholders retain the shares. It is intended that the Arrangement would continue in effect for an indefinite period in order to build up the shareholder equity base to a satisfactory level.

6. The estimated maximum amount which would be paid by the Company in respect of the redemption of shares under each bonus issue would be 5 percent of the market value of all shares in the Company.

Details of proposed bonus issue

7. The Company will issue a notice to shareholders informing them that they will be issued with bonus shares. The shares will be ordinary shares. The number of shares that a shareholder would receive would be based on:

   (i) the net amount the shareholder would have received if the Company had declared and paid a cash dividend rather than proceeding with the bonus issue; and

   (ii) the weighted average of the Company's share price for the five trading days following the relevant record date, less a discount of not more than 5% (and excluding brokerage fees). The discount will be included in the calculation to encourage share retention.

8. The number of bonus shares to be issued to a shareholder would be calculated in accordance with the following formula:

$$\text{Number of shares} = \frac{S \times A}{P \times D}$$

where:

S is the number of ordinary shares in the Company held by the shareholder before the bonus issue;

A is the amount per share (expressed in cents and fractions of cents (after deduction of any amounts of resident withholding, or other, taxes, if any)) which would have been distributed to the shareholder if the Company had instead made a cash distribution;

P is the weighted average sale price for the Company's shares (expressed in cents and fractions of cents) based on trades of those shares on the NZSX on the five trading days immediately following the relevant record date; and

D is calculated as (1 – Discount) expressed as a decimal.

(A mechanism for "roundings" will also be included in the above calculation.)

9. At the same time shareholders will be notified that the Company will provide an off-market facility available to allow shareholders to make an election to redeem their bonus shares for the equivalent cash value. The option to redeem will be made available at the time of notification of the issue of the bonus shares. The aggregate buyback price for a shareholder's bonus shares would be the number of shares issued to the shareholder multiplied by "(P x D)" in the above calculation.

10. The discount to be applied will depend on the market at the time of the announcement and will consequently be flexible depending on anticipated market reaction. The higher the discount the more likely shareholders will retain the shares. Conversely where the discount is too low there is less incentive to retain the shares. The Directors, in determining the level of discount, have sought to be fair to all shareholders by determining a rate which favours retention but does not appear to harshly penalise shareholders (through dilution) who have primarily invested for the regular cash flow.

11. The approximate timetable for each bonus issue and buy back (based on NZ Companies Act and NZSX Listing Rule requirements) would be as follows:

Day 1

Notice to NZX and ASX of proposed bonus issue (Appendix 7 NZSX Rules and ASX equivalent) including notice of value of bonus shares to be issued (as a $ value per share held).

Day 15 (first Friday at least 10 business days after Day 1)

Record date for Bonus Share entitlement.

Day 22 (5 business days after Day 15)

Determination of strike price for determining number of bonus shares to issue and resulting bonus share ratio.

Day 26 (say 4 days after day 22)

Details of bonus shares to be issued and buyback offer sent to shareholders. Shareholders given 14 days to elect whether to accept buy back offer.

Day 41 (15 days after Shareholders notified)

Date for shareholder acceptances of buy back offer.

Day 43

Issue of Bonus Shares and completion of buyback.

Day 45

Holding statements and payment cheque distributed.

Reasons for the structure of the Arrangement

12. The commercial advantages which the Company seeks to achieve from the Arrangement are as follows:

a) The reduction of the amount of the net cash outflow:

b) The maintenance as much as possible of the Company's equity base in light of the recent and planned business expansions;

c) The maintenance of the Company's policy of making two distributions a year to shareholders;

d) The provision of a mechanism for those shareholders who wish their share of profits to be retained within the Company:

e) The prevention of any negative impact on the Company's share price;

f) Due to the decrease in the dividends paid by the Company, the reduction of the amount of imputation credits used.

g) The provision of a mechanism for those shareholders who wish to receive cash.

13. The Company considers that, as with many New Zealand stock exchange listed companies, its dividend policy and perceptions of its dividend

policy has a direct impact on the share price of the Company. The Company has historically maintained a bi-annual high yield dividend policy. As a result investors who require an income stream from their investments may be attracted to invest in the Company. The level of capital growth in the Company, however also may make it attractive to shareholders who are seeking a capital gain. The Company considers that if the redemption option were not available material numbers of shareholders, requiring income from their shares, might seek to exit the stock, thereby having a negative impact on share price. Historically where a Company has reduced its dividend payout ratio this has had a negative impact on the share price.

14. The share issue has been structured to maximise the proportion of shares retained. The Arrangement operates so as to issue shares to all shareholders and give them the option of redeeming within a set period. Shareholders would have two weeks to decide whether to accept the offer to redeem the shares. The Company considers that if shareholders are required to apply for redemption of the shares, the level of share uptake should increase as the default result for shareholders who do not act will be that they retain the shares.

15. The Company also considers that a bonus issue in lieu would be less well received by its shareholders and the investment market in general than the Arrangement. The Company considers, on reasonable grounds, that denying shareholders who do not respond to the notice of a bonus issue within a specified timeframe the opportunity to receive cash is unlikely to be viewed favourably by shareholders.

16. The market reaction to the change in policy is unknown but the Company would anticipate that approximately 40–50 percent of the amount of the bonus issue would be retained by shareholders.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

a) The Company will not elect that the bonus issue will be treated as a “taxable bonus issue” (as defined in section OB 1).

b) For the purpose of the Companies Act 1993 and the NZX Listing Rulings the Arrangement is a pro rata bonus issue to all existing shareholders followed by an acquisition by the Company of its own shares.

c) The total amount paid by the Company on account of a redemption of shares under the Arrangement will be less than 15 percent of the market value of all shares in the Company at the time that the Company first notifies shareholders of the redemption.

d) During the period of this Ruling the Company will have sufficient imputation credits in its imputation credit account at the end of each imputation year to have fully imputed a cash dividend equal to the amount of the bonus issue which is not redeemed in each and every year during the term of the Arrangement.

e) The advantages that the Company is seeking to obtain from implementing the Arrangement are as set out in paragraph 12 of this Ruling.

f) The primary reason that the Company has chosen to implement this Arrangement as compared to other similar arrangements, such as its existing DRP, is that it considers, on reasonable grounds, that it will result in materially more shares being retained by shareholders, and thus greater funds retained by the Company, than under alternative available arrangements, and the Company has no advice or information contrary to or inconsistent with this that has not been disclosed to the Rulings Unit. This has the purpose of enabling the Company to retain profits for the expansion of its business and encouraging and maximising the retention of bonus shares while preventing any negative impact on the Company’s share price and preventing any negative perceptions by the market of the Company’s profit distribution policy.

g) The Company has not taken individual shareholders’ tax consequences into account in deciding to implement this Arrangement.

h) The Company has disclosed to the Rulings Unit all advice, analysis or other documentation relating to the purposes and advantages of implementation of this Arrangement.

How the Taxation Laws apply to the Arrangement

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

- The bonus issue is a non-taxable bonus issue (as defined in section OB 1) and does not constitute dividends as defined in sections CD 3(1), CD 4(1) and CD 5(1).
- Amounts paid to shareholders who elect to redeem the bonus shares are dividends under sections CD 3(1), CD 4(1) and CD 5(1).
- Shareholders who are residents and who receive redemption amounts with imputation credits attached are entitled by section LB 2(1) to claim a credit of tax equal to the amount of the imputation

credits attached to redemption amounts, subject to the restrictions in section LB 1 and LB 2.

- Where the full redemption amount is taxable as a dividend and where a shareholder continues to hold, after the redemption, shares of the same class the redemption amount is not gross income under sections CB 1, CB 2, CB 3 or CB 4 and the bonus issue will not affect the cost of the remaining shares held by a shareholder.
- Section GC 22 does not apply to the Arrangement.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 5 December 2005 and ending on 31 March 2009.

This Ruling is signed by me on the 5th day of December 2005.

Howard Davis
Senior Tax Counsel

PRODUCT RULING – BR PRD 05/09

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 SkyCity Consolidated Group – IRD No 63-352-039

Taxation Laws

All legislative references are to the Income Tax Act 2004 unless otherwise stated.

This Ruling applies in respect of:

- Section CB 2,
- Section CB 3;
- Section CB 4;
- Section CD 2;
- Section CD 3(1);
- Section CD 4(1);
- Section CD 5(1);
- Section EA 1;
- Section EA 2.

The Arrangement to which this Ruling applies

The Arrangement is the issue of bonus shares by SkyCity Entertainment Group Ltd ("the Company") and the offer by the Company of an option to redeem the shares under which shareholders elect to retain the shares and then sell the shares. Further details of the Arrangement are set out in the paragraphs below.

1. The Company, a member of the SkyCity Consolidated Group ("the Group"), is a public company. The Company was incorporated in New Zealand. The Company has in excess of twenty thousand ordinary shareholders, a very small percentage of whom are likely to be taxable at the 39% marginal income tax rate.

2. The Company typically distributes two dividends a year to shareholders—an interim dividend paid in April and a final dividend paid in October. Until April 2005 dividends were paid in cash without a reinvestment option. The Company has previously fully imputed all dividends paid and will continue to do so in the period for which this Ruling applies. At the time the Company pays dividends it has often not had sufficient imputation credits in its imputation credit account to fully impute the dividends. In these circumstances it has paid further income tax sufficient to ensure there is not a debit balance in its imputation credit account at year end and it will continue, if necessary, to pay further income tax during the period for which this Ruling applies so that it will have sufficient imputation credits in its imputation credit account at the end of each imputation year to have fully imputed a cash dividend equal to the amount of the bonus issue which is not redeemed in each and every year during the term of the Arrangement.

3. The Board of the Company has been considering ways to maintain the Company distribution policy without reducing its equity base (i.e. ways to make distributions without negatively impacting cashflow). Maintenance of the equity base is a high priority for the Company at the current time due to recent expansion activity undertaken by the Group, including the acquisition of interests in casinos located in Christchurch and Darwin, Australia, an increase in its shareholding in SkyCity Leisure and Riverside Casino, as well as the development of its Adelaide facilities.

4. On 21 February 2005 the Company announced that it would introduce a new dividend reinvestment plan (DRP) under which shareholders may choose to reinvest all or part of their cash dividends in additional shares in the Company. The DRP was available in respect of the interim dividend for the 2005 financial year paid on 1 April 2005. Additional shares issued under the DRP were issued at their market price but in terms of the

Offer Document dated 9 March 2005 the Board may determine that the shares will be issued at a discount. The Company has issued 1,212,484 new shares to shareholders under the DRP in respect of the dividend of $0.12 per share paid on 1 April 2005. These new shares represent 0.289 percent of the ordinary shares in the Company.

5. The Board has been considering an alternative mechanism that would encourage share uptake while still giving those shareholders who require a cashflow a mechanism by which to receive cash. Under the proposed plan bonus shares will be issued to all shareholders. The default option under the plan would be that shareholders retain the shares. It is intended that the Arrangement would continue in effect for an indefinite period in order to build up the shareholder equity base to a satisfactory level.

6. The estimated maximum amount which would be paid by the Company in respect of the redemption of shares under each bonus issue would be 5 percent of the market value of all shares in the Company.

Details of proposed bonus issue

7. The Company will issue a notice to shareholders informing them that they will be issued with bonus shares. The shares will be ordinary shares. The number of shares that a shareholder would receive would be based on:

   (i) the net amount the shareholder would have received if the Company had declared and paid a cash dividend rather than proceeding with the bonus issue; and

   (ii) the weighted average of the Company's share price for the five trading days following the relevant record date, less a discount of not more than 5% (and excluding brokerage fees). The discount will be included in the calculation to encourage share retention.

8. The number of bonus shares to be issued to a shareholder would be calculated in accordance with the following formula:

$$\text{Number of shares} = \frac{S \times A}{P \times D}$$

where:

S is the number of ordinary shares in the Company held by the shareholder before the bonus issue;

A is the amount per share (expressed in cents and fractions of cents (after deduction of any amounts of resident withholding, or other, taxes, if any)) which would have been distributed to the shareholder if the Company had instead made a cash distribution;

P is the weighted average sale price for the Company's shares (expressed in cents and fractions of cents) based on trades of those shares on the NZSX on the five trading days immediately following the relevant record date; and

D is calculated as (1 – Discount) expressed as a decimal.

(A mechanism for "roundings" will also be included in the above calculation.)

9. At the same time shareholders will be notified that the Company will provide an off-market facility available to allow shareholders to make an election to redeem their bonus shares for the equivalent cash value. The option to redeem will be made available at the time of notification of the issue of the bonus shares. The aggregate buyback price for a shareholder's bonus shares would be the number of shares issued to the shareholder multiplied by "(P x D)" in the above calculation.

10. The discount to be applied will depend on the market at the time of the announcement and will consequently be flexible depending on anticipated market reaction. The higher the discount the more likely shareholders will retain the shares. Conversely where the discount is too low there is less incentive to retain the shares. The Directors, in determining the level of discount, have sought to be fair to all shareholders by determining a rate which favours retention but does not appear to harshly penalise shareholders (through dilution) who have primarily invested for the regular cash flow.

11. The approximate timetable for each bonus issue and buy back (based on NZ Companies Act and NZSX Listing Rule requirements) would be as follows:

Day 1

Notice to NZX and ASX of proposed bonus issue (Appendix 7 NZSX Rules and ASX equivalent) including notice of value of bonus shares to be issued (as a $ value per share held).

Day 15 (first Friday at least 10 business days after Day 1)

Record date for Bonus Share entitlement.

Day 22 (5 business days after Day 15)

Determination of strike price for determining number of bonus shares to issue and resulting bonus share ratio.

Day 26 (say 4 days after day 22)

Details of bonus shares to be issued and buyback offer sent to shareholders. Shareholders given 14 days to elect whether to accept buy back offer.

Day 41 (15 days after Shareholders notified)

Date for shareholder acceptances of buy back offer.

Day 43

Issue of Bonus Shares and completion of buyback.

Day 45

Holding statements and payment cheque distributed.

Reasons for the structure of the Arrangement

12. The commercial advantages which the Company seeks to achieve from the Arrangement are as follows:

    a) The reduction of the amount of the net cash outflow:

    b) The maintenance as much as possible of the Company's equity base in light of the recent and planned business expansions;

    c) The maintenance of the Company's policy of making two distributions a year to shareholders;

    d) The provision of a mechanism for those shareholders who wish their share of profits to be retained within the Company:

    e) The prevention of any negative impact on the Company's share price;

    f) Due to the decrease in the dividends paid by the Company, the reduction of the amount of imputation credits used.

    g) The provision of a mechanism for those shareholders who wish to receive cash.

13. The Company considers that, as with many New Zealand stock exchange listed companies, its dividend policy and perceptions of its dividend policy has a direct impact on the share price of the Company. The Company has historically maintained a bi-annual high yield dividend policy. As a result investors who require an income stream from their investments may be attracted to invest in the Company. The level of capital growth in the Company, however also may make it attractive to shareholders who are seeking a capital gain. The Company considers that if the redemption option were not available material numbers of shareholders, requiring income from their shares, might seek to exit the stock, thereby having a negative impact on share price. Historically where a Company has reduced its dividend payout ratio this has had a negative impact on the share price.

14. The share issue has been structured to maximise the proportion of shares retained. The Arrangement operates so as to issue shares to all shareholders and give them the option of redeeming within a set period. Shareholders would have two weeks to decide whether to accept the offer to redeem the shares. The Company considers that if shareholders are required to apply for redemption of the shares, the level of share uptake should increase as the default result for shareholders who do not act will be that they retain the shares.

15. The Company also considers that a bonus issue in lieu would be less well received by its shareholders and the investment market in general than the Arrangement. The Company considers, on reasonable grounds, that denying shareholders who do not respond to the notice of a bonus issue within a specified timeframe the opportunity to receive cash is unlikely to be viewed favourably by shareholders.

16. The market reaction to the change in policy is unknown but the Company would anticipate that approximately 40–50 percent of the amount of the bonus issue would be retained by shareholders.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

a) The Company will not elect that the bonus issue will be treated as a "taxable bonus issue" (as defined in section OB 1).

b) For the purpose of the Companies Act 1993 and the NZX Listing Rulings the Arrangement is a pro rata bonus issue to all existing shareholders followed by an acquisition by the Company of its own shares.

c) During the period of this Ruling the Company will have sufficient imputation credits in its imputation credit account at the end of each imputation year to have fully imputed a cash dividend equal to the amount of the bonus issue which is not redeemed in each and every year during the term of the Arrangement.

d) The advantages that the Company is seeking to obtain from implementing the Arrangement are as set out in paragraph 12 of this Ruling.

e) The primary reason that the Company has chosen to implement this Arrangement as compared to other similar arrangements, such as its existing DRP, is that it considers, on reasonable grounds, that it will result in materially more shares being retained by shareholders, and thus greater funds retained by the Company, than under alternative available arrangements, and the Company has no advice or information contrary to or inconsistent with this that has not been disclosed to the Rulings Unit. This has the purpose of enabling the Company to retain profits for the expansion of its business and encouraging and maximising the retention of bonus shares while preventing any negative impact on the Company's share price and preventing any negative perceptions by the market of the Company's profit distribution policy.

f) The Company has not taken individual shareholders' tax consequences into account in deciding to implement this Arrangement.

g) The Company has disclosed to the Rulings Unit all advice, analysis or other documentation relating to the purposes and advantages of implementation of this Arrangement.

How the Taxation Laws apply to the Arrangement

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

- The bonus issue is a non-taxable bonus issue (as defined in section OB 1) and does not constitute dividends as defined in sections CD 3(1), CD 4(1) and CD 5(1).
- Amounts derived by shareholders from the sale of bonus shares are not gross income under sections CB 2, CB 3, CB 4 or CB 5 where each of the following apply:

  a) The shareholder is not dealing in shares; and

  b) The sale of shares is not part of any business carried on by the shareholder; and

  c) The shareholder did not acquire the shareholder's original shares for the purpose of sale and at the time the original shares were acquired, the shareholder did not know that bonus shares would be issued by the Company.
- The bonus shares will have a nil cost for the purposes of Part E and section EA 2. No deduction will be allowable to shareholders in respect of the bonus shares unless:

  - Bonus shares are trading stock or revenue account property of a shareholder; and
  - The value of the bonus shares is taken into account in determining the shareholder's opening stock for the purpose of section EA 1(2) and (3) or in allocating an allowable deduction under section EA 2.

  in which event a deduction will be allowable to the extent that a cost is attributed to the bonus shares, from the cost basis of other shares held by the shareholder, under one of the cost flow methods specified in section EB 7.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 5 December 2005 and ending on 31 March 2009.

This Ruling is signed by me on the 5th day of December 2005.

Howard Davis
Senior Tax Counsel

LEGISLATION AND DETERMINATIONS

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

LIVESTOCK VALUES – 2006 NATIONAL STANDARD COSTS FOR SPECIFIED LIVESTOCK

The Commissioner of Inland Revenue has released a determination, reproduced below, setting the national standard costs for specified livestock for the 2005/2006 income year.

These costs are used by livestock owners as part of the calculation of the value of livestock on hand at the end of the income year, where they have adopted the national standard costs (NSC) scheme to value any class of specified livestock.

Farmers using the scheme apply the one-year NSC to stock bred on the farm each year, and add the rising two-year NSC to the value of the opening young stock available to come through into the mature inventory group at year-end. Livestock purchases are also factored into the valuation of the immature and mature groupings at year-end, so as to arrive at a valuation reflecting the enterprise's own balance of farm bred and externally purchased animals.

NSCs are developed from the national average costs of production for each type of livestock farming based on independent survey data. Only direct costs of breeding and rearing rising one-year and two-year livestock are taken into account. These exclude all costs of owning (leasing) and operating the farm business, overheads, costs of operating non-livestock enterprises (such as cropping) and costs associated with producing and harvesting dual products (wool, fibre, milk and velvet).

For bobby calves, information from spring 2005 is used while other dairy NSCs are based on survey data for the year ended 30 June 2005. For sheep, beef cattle, deer and goats, NSCs are based on survey data for the year ended 30 June 2004 which is the most recent available for those livestock types at the time the NSCs are calculated.

For the 2005-2006 income year there has been a slight increase (in dollar terms) in the NSC for sheep and beef cattle. This is partly due to the lower lambing and calving percentages for these types of livestock. These lower percentages mean that the overall farm production costs have to be spread over less lambs or calves, hence a higher NSC for the younger animals.

The values for dairy cattle rising one-year and rising two-year animals have only slightly changed from the previous year. This is mainly due to an update to the NSC formula for this class of livestock to reflect improvements to milk production since the scheme was first introduced in 1992. The formula now recognises that milk production is measured in milksolids rather than the former milkfat measure existing when the formula was first introduced. For the current year, more of the farm production costs have been assigned to milk production and less to calf production.

The NSC values for the other livestock types (deer, meat and fibre goats and pigs) have remained relatively static with only minor changes in dollar terms. The values for dairy goats have increased by 8.0% due mainly to increased feed costs for kids. Dairy bred bobby calves values also increased due to the increase in feed costs.

The new NSCs struck each year only apply to that year's immature and maturing livestock. Mature livestock valued under this scheme effectively retain their historic NSCs until they are sold or otherwise disposed of, albeit through a FIFO or inventory averaging system as opposed to individual livestock tracing. It should be noted that the NSCs reflect the average costs of breeding and raising immature livestock and will not necessarily bear any relationship to the market values (at balance date) of these livestock classes. In particular, some livestock types, such as dairy cattle, may not obtain a market value in excess of the NSC until they reach the mature age grouping.

One-off movements in expenditure items are effectively smoothed within the mature inventory grouping, by the averaging of that year's intake value with the carried forward values of the surviving livestock in that grouping. For the farm-bred component of the immature inventory group, the NSC values will appropriately reflect changes in the costs of those livestock in that particular year.

The NSC scheme is only one option under the current livestock valuation regime. The other options are market value, the herd scheme and the self assessed cost (SAC) option. SAC is calculated on the same basis as the NSC but uses a farmer's own costs rather than the national average costs. There are restrictions in changing from one scheme to another and before considering such a change livestock owners may wish to discuss the issue with their accountant or other adviser.

National Standard Costs for Specified Livestock Determination 2006.

This determination may be cited as "The National Standard Costs for Specified Livestock Determination, 2006".

This determination is made in terms of section EC 23 of the Income Tax Act 2004. It shall apply to any specified livestock on hand at the end of the 2005-2006 income year where the taxpayer has elected to value that livestock under the national standard cost scheme for that income year.

For the purposes of section EC 23 of the Income Tax Act 2004 the national standard costs for specified livestock for the 2005-2006 income year are as set out in the following table.

Table

Kind of livestock	Category of livestock	National standard cost
		$
Sheep	Rising 1 year	23.90
	Rising 2 year	15.80
Dairy cattle	Purchased bobby calves	139.00
	Rising 1 year	678.00
	Rising 2 year	87.10
Beef cattle	Rising 1 year	233.40
	Rising 2 year	133.10
	Rising 3 year male non-breeding cattle (all breeds)	133.10
Deer	Rising 1 year	71.50
	Rising 2 year	35.30
Goats (meat and fibre)	Rising 1 year	18.50
	Rising 2 year	12.70
Goats (dairy)	Rising 1 year	115.30
	Rising 2 year	18.50
Pigs	Weaners to 10 weeks of age	78.90
	Growing pigs 10 to 17 weeks of age	61.10

This determination is signed by me on the 30th day of January, 2006.

Martin Smith
Chief Tax Counsel

QUESTIONS WE'VE BEEN ASKED

This section of the *TIB* sets out answers to some enquiries we've received. We publish these as they may be of general interest to readers. A general similarity to items published here will not necessarily lead to the same tax result. Each case should be considered on its own facts.

FBT – VALUE OF BROKERAGE PROVIDED BY SHAREBROKERS TO EMPLOYEES

Income Tax Act 2004—section ND 1K(1)(a)—FBT—value of services

All references are to the Income Tax Act 2004.

We have been asked to consider what is the value for FBT purposes of brokerage services provided by sharebrokers to their employees. In an item in *Public Information Bulletin* No 161 ("PIB 161"), the Commissioner accepted that, for FBT purposes, the value of brokerage services provided to employees would be the lowest value of brokerage that would be charged to preferred clients of a sharebroker. The correctness of this item has now been questioned.

Valuation rule

Section ND 1K(1)(a) applies to value brokerage provided to employees by a sharebroker (being services of a type normally provided by sharebrokers as part of their business). Under section ND 1K(1)(a) the value of brokerage is the price charged by the employer for the "same or similar" services to the public in the open market in New Zealand on ordinary trade or professional terms between buyers and sellers independent of each other.

Meaning of "the public"

The expression "the public" means the community as a whole or a member of the community: *Evans v Lee* [1964] SASR 219; *Jennings v Stephens* [1936] Ch 469. In this context the expression "the public" includes any member of the community who may seek the sharebroking services of a sharebroker.

Are brokerage services provided to employees similar to services provided to the public?

"Similar" does not mean "exactly the same": see *Mays v Roberts* [1928] SASR 217; *Greenleaf v Goodrick* 101 US 278; *NZ Central Region etc Local Government Officers' Union v Lower Hutt City Council* (1992) 1 ERNZ 558. Whether the services provided to employees of sharebrokers are similar to the service provided to members of the general public depends on what the essential features of the service provided to the general public are and whether the services provided to employees have those characteristics.

In order to buy or sell listed securities investors must place orders through a sharebroker. Sharebrokers may provide additional advisory services to some clients for an increased fee but the essential features of the basic brokerage service provided by sharebrokers are:

- The placement of orders for the sale or purchase of listed securities; and
- The settlement of transactions for the sale and purchase of securities

on behalf of their clients through the NZX's electronic trading system or the electronic trading system of another stock exchange. These services may be accessed either electronically or by telephone.

Under the NZX Participation Rules, employees of sharebrokers are subject to a number of restrictions such as minimum holding periods for shares, preference being given to client orders, the inability to participate in Initial Public Offers, priority being given to orders given by members of the public and the inability to trade through sharebrokers other than their employers. However, the Commissioner considers that the restrictions do not alter the essential nature of the brokerage services provided. These restrictions affect the timing, number and nature of the security transactions that employees may undertake and may limit access to the brokerage services. It is acknowledged that potentially the restrictions may affect the price at which securities may be bought or sold as employees, but the provision of the service would still result in the employee either obtaining securities or selling securities. The fact that employees of sharebrokers are not able to trade through a sharebroker other than their employer also does not affect the nature of the service provided. The brokerage services provided to employees (the purchase and sale of securities on behalf of the employees) are similar to the brokerage services normally provided by sharebrokers to the public. In each case the service provided is the sale or purchase of securities in accordance with instructions given to the sharebroker.

What is the value of brokerage provided to employees?

The value of brokerage for FBT purposes is the rate that would be charged by the employer to a member of the general public. Generally brokerage rates are calculated on a graduating scale based on the size of each trade (that is, the brokerage is a percentage of the order amount) subject to a minimum charge. Sharebrokers may also apply a "trader rate" to customers who have traded in excess of a specified amount of brokerage. A lower rate may also be charged for on-line brokerage services.

The value of brokerage provided by sharebrokers to their employees is to be determined on a transaction by transaction basis according to the scale of charges applied by the particular sharebroker. If a lower rate of brokerage would have been available to an employee even if the employee was not employed by the sharebroker, for example, because of the volume of transactions undertaken by the employee, the lower rate would be the value of the brokerage provided to the employee for FBT purposes.

In the light of the above, in the Commissioner's view, the item in PIB 161 does not correctly reflect the law. Accordingly, the item is withdrawn from 31 March 2006 and from that date should not be considered to be an expression of the Commissioner's view of the law. This statement now represents the Commissioner's view on the value of brokerage services provided by sharebrokers to their employees.

THE MEANING OF "BENEFIT" FOR FBT PURPOSES

Income Tax Act 2004—section CX 2—fringe benefit

All references are to the Income Tax Act 2004.

We have been asked whether a benefit would be provided for FBT purposes if: (a) an employee paid market value for the goods or services provided, and/or (b) the employer also receives a benefit from the provision of goods or services to an employee. These issues are fundamental to the interpretation of the FBT regime, in that they raise the question of what is a "benefit" and, therefore, what can give rise to a "fringe benefit" in terms of the scheme and purpose of the legislation.

Scheme of the legislation

FBT is payable by an employer who has provided or granted a fringe benefit: section ND 1(1). Under the definition of "fringe benefit" in section CX 2, there is a fringe benefit where:

- A benefit is provided by an employer to an employee in connection with their employment; and
- The benefit arises in a way described in any of sections CX 6, CX 8, CX 9, CX 11 to CX 15 or is an "unclassified benefit"; and
- The benefit is not excluded from being a fringe benefit by any provision of subpart CX.

The value of the fringe benefit is determined in accordance with the rules set out in sections ND 1A to ND 1R. FBT is calculated on the taxable value of a fringe benefit: section ND 1(2). In calculating the taxable value, the value of the benefit is reduced by payments made by the employee for receiving the fringe benefit: section ND 1S.

Therefore, in order to determine whether an employer has an FBT liability, it is necessary to establish:

- First, whether a benefit (either one of the specific types of benefit referred to in the legislation or any other benefit) has been provided by the employer to an employee in connection with their employment and none of the specific exclusions from the definition of "fringe benefit" applies. If so, a "fringe benefit" is "provided";
- Secondly, the value of the fringe benefit in accordance with specific and detailed rules set out in the legislation;
- Thirdly, the taxable value of the fringe benefit. In order to calculate the taxable value of a fringe benefit, amounts paid by an employee for the benefit must be deducted from the value of the fringe benefit determined under the FBT rules.

Would a benefit be provided if the employee had paid the market value of the benefit?

For a benefit to be provided, it is not necessary to establish that the employee has received a profit (that is, a surplus above the amount paid by the employee for the benefit). In terms of the scheme of the FBT regime, a "benefit" means what is received by the employee, without regard to any contribution made by the employee. However, in order to calculate the taxable value of the fringe benefit provided, amounts paid by the employee for the fringe benefit (other than an employment-related loan) are deducted from the value of the fringe benefit (determined under sections ND 1A to ND 1L).

The taxable value of a fringe benefit is the value of the benefit determined under those provisions: section ND 1S(1). The value of the benefit (other than an employment-related loan) provided to an employee is reduced by any amount paid by the employee for receiving the fringe benefit: section ND 1S(2). Therefore, the effect of section ND 1S(2) is that if the amount paid by the employee for a benefit (other than an employment-related loan) equals the value of the benefit for FBT purposes, the taxable value of the benefit would be nil so that FBT would not be payable in respect of the benefit.

Some commentators have suggested that a fringe benefit does not arise where an employee has paid market value for the fringe benefit and that the issue of whether a benefit is a gross or net concept is of no practical significance as there will be no FBT liability where an employee pays the market value of the benefit provided by the employer. However, the Commissioner considers that it is not possible to establish that there is no FBT liability unless the steps outlined above are carried out. For example, the legislation contains special rules relating to the valuation of the benefit arising from the provision of a car for private use which may not necessarily be the exact market value of the benefit. The McCaw Task Force (which recommended the introduction of FBT) considered that the value of benefits consisting of the provision of a car for private use should be determined on the basis of a specified formula because of difficulties in determining the value of such benefits on a case-by-case basis: *Report of the Task Force on Tax Reform* (April 1982). The Task Force considered that as a general rule the value to an employee of a fringe benefit consisting of the provision of a car for private use was equal to the amount by which the employee's need to meet private outgoings was reduced: see para 6.A3. Under the current valuation rules the formula is based on the original cost of the vehicle and on the assumption that vehicles are kept for an average of five years.

Is a benefit provided "in connection with" the employment of the employee, where an employee pays market value for the benefit provided?

In *Smith v FCT* 87 ATC 4883 it was held that a benefit was "in respect of, or for or in relation to" the employment where there was a connection between the benefit received and the employment. It was considered that in determining whether there was a connection between the benefit and the employment relationship it was appropriate to consider the reason for the provision of the benefit. Where the employment is a substantial reason for the provision of the benefit, there would be a relationship between the benefit and the employment. The phrase "in connection with" also requires a relationship between two things: *Claremont Petroleum NL v Cummings* (1992) 110 ALR 239; *Strachan v Marriott* [1995] 3 NZLR 272. The Commissioner considers that a benefit is provided "in connection with" the employment relationship if the employment relationship is the reason for, or at least a substantial reason for, the provision of the benefit.

Whether a benefit for which market value is paid by an employee is "in connection with" an employment relationship depends on the facts in each case. If the employer's business does not include the provision of goods or services of the type provided to the employee, it is unlikely that the goods or services would have been provided to the employee if not for the employment relationship. However, if the goods or services provided to an employee are of a type which the employer customarily makes available to the general public, and the goods and services are provided at the same price and on the same terms as the price and terms available to a member of the general public, it is likely that the goods or services would be provided because the employee has paid for such goods or services, rather than because of the employment relationship.

Example

An employee of a supermarket selects goods off the shelves of the supermarket, queues at the checkout to pay for the goods and pays the shelf price for the goods. Regardless of whether the checkout operator is aware that the employee is a staff member a benefit would not be provided to the employee "in connection with their employment" as the employee receives the goods on the same terms and conditions as any other customer.

If by showing a staff card the employee obtained a discount on the goods, a benefit would be provided to the employee "in connection with the employment" as the employee is entitled to purchase goods at a discount only because of the employment relationship.

A benefit would also be provided to employees "in connection with their employment" if employees were entitled to a rebate where their total purchases exceeded a certain level and such a rebate was not available to the public.

Would a benefit be provided where the employer also receives a benefit from the provision of goods or services?

Whether a fringe benefit is provided does not depend on whether employees consider that they have received an advantage or benefit: *Case M9* (1990) 12 NZTC 2,069. The definition of "fringe benefit" contains specific exclusions relating to situations where goods or services are provided to an employee for the purpose of performing employment duties: see sections CX 17 and CX 26(1) and the provisos to the definition of "private use or enjoyment" in section OB 1. An inference can be drawn from these specific exclusions that it was contemplated that a benefit would be provided where both the employer and the employee derive a benefit from the provision of goods or services to the employee. The specific exclusions relate to:

- Any benefit, to the extent to which it removes a need that would otherwise exist for the employer to pay the employee an allowance that reimburses the employee for transport costs that would have been incurred both in connection with their employment and for the benefit of the employer in travelling between home and work, such transport costs being attributable to any one or more of the following factors:

  - the day or time of day when the work duties are performed;
  - the need to transport any goods or material for use or disposal in the course of the employee's work;
  - the requirement to fulfil a statutory obligation;
  - a temporary change in the employee's place of work while in the same employment;
  - any other condition of the employee's work;
  - the absence of an adequate public passenger transport service that operates fixed routes and a regular timetable for the employee's place of work (section CX 17);
- The provision of "distinctive work clothing" (section CX 26(1));
- The use of a vehicle for emergency calls: section CX 6(2); definition of "emergency call" in section CX 28. The use of a vehicle for travel from the employee's home would not be private use where the vehicle is used for an emergency call.
- The use of a work-related vehicle (including the use of such a vehicle for private use that is travel to and from the employee's home that is necessary in and is a condition of their employment or other private use where the travel arises in the course of their employment during which the travel arises incidentally to the business use): section CX 6(2), definition of "work-related vehicle" in section CX 32.

RECORDS FOR CONTROLLED FOREIGN COMPANIES OR FOREIGN INVESTMENT FUNDS TO BE AVAILABLE IN ENGLISH

We have been asked to clarify Inland Revenue's position as to whether taxpayers are required to provide financial and other underlying records, including evidence of foreign tax paid, in English for any controlled foreign companies ("CFCs") or foreign investment funds ("FIFs") they may hold when using the branch equivalent tax calculation method.

Background

There have been a number of instances when verification by the Commissioner of branch equivalent tax calculations has been affected by taxpayers not being able to provide the underlying records in English. This issue has highlighted that some taxpayers are not aware of their obligation, to keep in New Zealand, sufficient records in the English language, to enable the Commissioner to readily ascertain their attributed income.

Practice

The legislation requires that any taxpayer that holds interests in any CFC or FIF, where the branch equivalent tax calculation method is adopted, has an obligation to provide upon request financial and other underlying records, for that entity, in English.

Application of Section 22 of the Tax Administration Act (TAA) 1994

Section 22 (2) of the TAA states as follows:

> "…every person who –
>
> (a) Carries on any business in New Zealand:
>
> (b) Carries on any other activity (not being the carrying on of employment as an employee) in New Zealand for the purpose of deriving assessable income;…
>
> (d) **Makes, holds, or disposes of, for the purpose of deriving assessable income, any investment;…**
>
> (f) Is a company that is… a branch equivalent tax account company…
>
> **shall keep in New Zealand sufficient records in the English language to enable the ascertainment readily by the Commissioner, or any officer authorised by the Commissioner** in that behalf, of –
>
> (g) The assessable income derived by that person from the carrying on of that business, or the carrying on of that other activity, or the making or holding or disposing of that investment; and
>
> (h) The allowable deductions of that person in the carrying on of that business, or the carrying on of that other activity, or the making or holding or disposing of that investment; and …
>
> (k) Every credit and debit to the…branch equivalent tax account;…
>
> and shall retain in New Zealand all such records for a period of at least 7 years…" (emphasis added)

The Commissioner's position is that should the records of the various CFCs and FIFs not be provided in the English language, the attributed CFC or FIF income (being assessable income) or attributed CFC or FIF losses (being allowable deductions) cannot be readily ascertained. Nor is the Commissioner in the position of being able to readily ascertain the accuracy in such situations of the resulting entries to the branch equivalent tax account.

Where the financial and other underlying records, including evidence of foreign tax paid, are not maintained in English, the Commissioner considers that upon request there is a requirement for taxpayers to provide such information in English in a timely manner, to ensure the Commissioner can readily ascertain the matters referred to above.

Exception

The exception to such a requirement is under section 22(2) of the TAA 1994:

> "… the Commissioner may, on application in writing being made to the Commissioner in that behalf, authorise any such person, by notice, to keep and retain outside New Zealand or as the case may be, in a language other than the English language, such of those records as the Commissioner determines".

Such applications will be considered on a case by case basis, taking into account the degree of difficulty which maintaining records in a language other than English would cause for Inland Revenue, the compliance history of the taxpayer, whether alternative sources of relevant information are available and the relative cost to the taxpayer in meeting their obligation.

NEW LEGISLATION

ORDER IN COUNCIL: STUDENT LOAN SCHEME – REPAYMENT AND INTEREST WRITE-OFF THRESHOLDS FOR THE 2006–07 TAX YEAR

The student loan scheme repayment and interest write-off thresholds are reviewed annually in December. They have been inflation adjusted according to the annual movement in the September 2005 CPI and the repayment threshold rounded up so that it is divisible into whole dollars on a weekly basis.

Repayment threshold

The student loan scheme repayment threshold, which sets the income level at which compulsory repayments begin, will increase from its current level of $16,588 to $17,160 for the 2006–07 tax year.

Interest write-off threshold

Under the new interest-free policy which comes into effect from 1 April 2006, borrowers will receive a full interest write-off only if they are present in New Zealand for 183 or more days.

Example

Janis ceases studying on 30 November 2006 and leaves New Zealand for two years on 31 January 2007. Her income for the 2006–07 tax year is $15,000. Under the interest-free policy, her entitlement to a full interest write-off would cease from 1 February 2007.

However, under existing provisions, part-time or part-year students with low income receive a full interest write-off until the end of the tax year in which they studied.

The full interest write-off threshold has therefore been retained to ensure that part-time or part-year students are no worse off than they were before the interest-free policy was introduced. The threshold will increase from its current level of $26,799 to $27,699 for the 2006–07 tax year.

In the example, Janis would continue to receive the full interest write-off until 31 March 2007.

Student Loan Scheme (Repayment Threshold) Regulations 2005

Student Loan Scheme (Income Amount for Full Interest Write-off) Regulations 2005

LEGAL DECISIONS – CASE NOTES

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

We've given full references to each case, including the citation details where it has already been reported. Details of the relevant Act and section will help you to quickly identify the legislation at issue. Short case summaries and keywords deliver the bare essentials for busy readers. The notes also outline the principal facts and grounds for the decision. Where possible, we have indicated if an appeal will be forthcoming.

These case reviews do not set out Inland Revenue policy, nor do they represent our attitude to the decision. These are purely brief factual reviews of decisions for the general interest of our reader.

REINSTATEMENT OF CANCELLED GST REGISTRATION UPHELD BY COURT OF APPEAL

Case:	Lopas and McHerron v The Commissioner of Inland Revenue
Decision date:	30 November 2005
Act:	Goods and Services Tax Act 1985, Interpretation Act 1999
Keywords:	Cancellation of GST registration, amount specified for purposes of section 51, thresholds for registration and deregistration

Summary

The Court of Appeal determined the Commissioner had correctly reinstated the cancellation of a GST registration which had been made in error. The Court found that where total cessation of a taxable activity is intended, taxpayers should apply for cancellation of registration on that basis under section 52(3), and not on the basis the activity will involve supplies under the threshold (section 52(1)) as had been done in this case.

Facts

The taxpayers were the partners in a partnership which registered for GST purposes on 1 October 1992 with a taxable activity of forestry. In its first GST return the partnership claimed an input tax credit on the purchase of a property.

On 4 October 1999, the partnership applied to cancel its GST registration with effect from 30 September 1999, on the basis that its taxable supplies for the next 12 months would be less than $30,000.

The application form prepared by the partnership's accountant stated that the partnership would be keeping some of its business assets when the registration ceased, namely land valued at $115,000 inclusive of GST, being the lesser of cost or market value.

The Commissioner cancelled the GST registration from 30 September 1999. The taxpayers took the view that section 5(3) of the GST Act deemed the land, being an asset of the taxable activity, to be supplied immediately before the cessation of the registration. They considered that section 10(8) deemed the consideration to be the lesser of cost or market value. As a consequence, the partnership's return for the period ended 30 September 1999 returned GST output tax on $115,000, which was the cost price of the land.

On 8 October 1999, the taxpayers entered into a sale and purchase agreement with the Jeffrey Lopas Family Trust and Lorraine McHerron Family Trust Partnership ("the trusts partnership") to sell the property for $375,000. Possession was to be given on 1 November 1999 and the purchase price was to be satisfied by a mortgage back to the vendors. The purchase price was based on a registered valuer's report.

The two family trusts were created by deeds of trust dated 20 September 1999. On 5 October 1999, the Commissioner received an application to register the trusts partnership for GST purposes from 1 October 1999. An application had been made in the name of the trusts partnership on 26 July 1999 to the Banks Peninsula District Council for permission to subdivide the land. The application was approved on 13 October 1999.

The Commissioner became aware of the sale to the trusts partnership. He considered the sale was an action done in the termination of a taxable activity and that section 6(2) of the GST Act applied to deem the sale to be a supply carried out in the course or furtherance of the taxpayer's taxable activity. As a consequence he considered GST to be payable on the $375,000 purchase price. That being so, the Commissioner took the view the taxpayers made taxable supplies of more than $30,000 in the relevant period.

In light of this additional information, and after an opportunity had been provided for the taxpayers to respond, the Commissioner amended the partnership's deregistration date from 30 September 1999 to 30 November 1999. The decision to amend the date was disputed, and led to this litigation.

Decision

The Court had no difficulty in concluding that the phrase "the amount specified for the purposes of section 51(1) of this Act" refers to the $30,000 or any substituted figure set out in section 51(1)(a). It rejected the taxpayer's submission that the word "amount" imports not only the monetary sum in section 51(1)(a) but also the methods of calculating the amount in a particular case, including the exclusions in sections 51(1)(c) and (d).

The Court also accepted that there is no compelling policy reason for holding that the purpose of the reference to section 51(1) in section 52(1) must have been to ensure the same thresholds for registration and deregistration. It accepted a submission for the Commissioner that there are plausible policy reasons for there to be a difference between the thresholds for registration and deregistration, and it would defeat the purpose of having a threshold if unregistered persons were brought within the GST net at the moment they were ceasing a taxable activity. On the other hand, those deregistering are already in the GST net and seeking to be removed. In such circumstances there is no compelling policy reason to exclude any taxable supplies from the calculation that are in contemplation in the period after deregistration from the threshold calculation.

The Court also accepted a submission for the Commissioner that when total cessation of a taxable activity is intended, taxpayers should apply for deregistration under section 52(3) and not section 52(1). If that had been done, then deregistration would have been deferred until cessation of the activity and thus any sales made in the course of ceasing the taxable activity would have been subject to section 6(2).

The Court also observed the Commissioner was acting under the erroneous impression that the supplies would be under the threshold. For this reason, it was appropriate in terms of section 13 of the Interpretation Act 1999 that he re-exercise his discretion and set a new GST cancellation date once he was in possession of the full facts.

STRIKE OUT OF JUDICIAL REVIEW

Case:	Ron West Motors (Otahuhu) Ltd v TRA and The Commissioner of Inland Revenue
Decision date:	14 December 2005
Act:	Income Tax Act 1976
Keywords:	Judicial Review, Strike Out, Objection, Track A assessments

Summary

Commissioner's strike out application was granted because the High Court considered the judicial review proceedings could not be seriously argued.

Facts

This is a Russell related matter.

The taxpayer had been assessed under what is known as the Track A approach to the Russell template. After hearings at the TRA and the High Court, in which the taxpayer was unsuccessful, its appeal to the Court of Appeal was deemed abandoned and the tax litigation at an end.

Subsequently the taxpayer made what it considered to be a late objection to the assessments which had been affirmed in the tax proceedings. In essence the taxpayer argued that the Commissioner's subsequent assessments of another taxpayer (Mr Russell personally, under the Track C, D and E basis) made the assessments affirmed by the Courts incorrect. This argument was supported by reference to section 99(4) ITA 1976.

The Commissioner declined to accept the late objection on the basis he lacked any ability to amend the assessments after the Court process was completed.

The taxpayer sought judicial review and the Commissioner sought to strike out the proceedings.

Decision

Simon France J considered that the judicial review could not possibly succeed and should be struck out.

The Judge considered that section 99(4) was no impediment to having two concurrent assessments of the same taxable income (if such was the case here) provided the position was harmonised by amending one assessment to avoid any element of double taxation (at par [13]). His Honour:

> "[15] In my view, there can be no sensible answer to this other than it is the Track A assessment, confirmed as correct by the Taxation Review Authority and the High Court, that cannot be amended. If the subsequent track C assessment is inconsistent, section 99(4) operates as a bar to that later track C assessment"

Thus the Court concluded that the late objection on the Track A assessments cannot succeed.

On the facts of this particular case, the Court further rejected the taxpayer's argument that the potential inconsistency was not known to the taxpayer or the Court at the time of the High Court's decision (at par [21] to [24]).

Justice Simon France added:

> "…Further I do not consider it seriously arguable that the Commissioner should facilitate the recommencement of the objection process in relation to assessments that are 20 years old, and which have been the subject of full consideration before the Taxation Review Authority and the High Court." par [26]

TAXPAYER APPEAL AGAINST CAPITAL EXPENDITURE DECISION

Case:	Fullers Bay of Islands v The Commissioner of Inland Revenue
Decision date:	28 November 2005
Act:	Income Tax Act 1994
Keywords:	Capital Expenditure, Deductibility, Income Revenue Distinction

Summary

The taxpayer was unsuccessful in appealing the High Court decision that legal fees expenditure was in respect of a capital asset and therefore not deductible.

Facts

Fullers Bay of Islands Limited provides sea and land transport services, engages in the tourist industry and provides a range of services in New Zealand and overseas. In March 1996, Fullers decided to look at ways of expanding its business in the Auckland area and made enquiries to the Auckland Regional Council ("ARC") about opportunities. Fullers became aware that a significant passenger ferry service run between Devonport and Auckland City was to be offered for public tender which closed on 9 April 1996. At that time the Devonport Ferry service was being run by a competitor, Fullers Group Limited ("FGL") (unrelated).

Fullers found out that this ferry run was highly profitable and so submitted a tender because it considered it could run the service without suffering significant infrastructure expansion costs and could use existing vessels. Fullers made the offer on the basis of a ratepayers' subsidy, as it was understood that the current operator, FGL, operated on a subsidy of $250,000.00. Fullers' offer was for an enhanced service at a reduced subsidy of $10,000.00. Fullers understood that, if successful, it would have a monopoly for the duration of the five year ferry service contract. It did not make an offer that included no subsidy at all, known as a Commercial Registration, because Fullers considered that offer would be unsuccessful, as the service could not run profitably on that basis.

At first, ARC found Fullers' offer attractive and notified Fullers that it was the preferred bidder. However prior to final notification of the results of the tender process, FGL submitted a Commercial Registration which was accepted by ARC, so that FGL won the tender. Fullers was not given the opportunity to submit a Commercial Registration which it considered to be unfair, particularly as they had received assurance from ARC that Commercial Registrations would not be accepted.

Fullers commenced proceedings against ARC and FGL, having received legal advice that their case was strong. In the fifth amended Statement of Claim filed in those proceeding, three causes of action were set out. These were:

(a) That ARC breached contractual obligations regarding confidentiality, consideration of a Commercial Registration and fairness. The remedies sought were declarations that had ARC not breached those obligations, Fullers would have obtained the Devonport Ferry contract. It also claimed damages for $6.2 million plus interests, being the discounted value of future cash flows which would have been realised from the Devonport Ferry contract. The TRA found that, if the cashflow projections were correct, Fullers' marine division would have increased by 50%, but subsequently the High Court and Court of Appeal found that actually the Devonport contract would have doubled the marine division's operating revenue at that time.

(b) That ARC had engaged in misleading and deceptive conduct which resulted in the loss of the contract. The remedy sought was damages of the same amount.

(c) That ARC mismanaged the tender process in a number of ways. Remedies sought were declarations including a declaration that, if ARC had properly managed the process, Fullers would have been awarded the contract, and an order that Fullers did hold the contract for five years from the date of the order.

(d) That FGL's Commercial Registration was invalid. Remedy sought was an injunction to stop them acting in accordance with that registration and, in a second cause of action against ARC under this head, seeking damages for alleged interference with Fullers' contractual rights.

In a judgment dated 4 June 1999, Paterson J dismissed all claims made by Fullers against ARC and FGL. The legal fees that Fullers paid were shown as an extraordinary item in Fullers' accounts and Fullers claimed a deduction of $612,792.14 in the 1999 income year which the Commissioner disallowed.

Decision

The Court of Appeal gave a judgment in favour of the Commissioner.

Fullers argued that, at the High Court, Baragwanath J had applied the wrong conceptual framework so that his decision was wrong in law. His Honour had concluded that the purpose of the litigation was overall to secure a capital asset. Fullers submitted that the purpose of the litigation, and thus the legal fee expenditure, was threefold. Firstly to establish that there was a preliminary contract between Fullers and the ARC, secondly to prove that contract was breached, and finally to obtain a remedy for that breach.

Fullers' first submission was that it was not correct to ignore the first two key purposes of the litigation and concentrate only on the third. Since a significant amount of the litigation expenditure was spent on those two issues, the expense was revenue in nature. It is important to note that this submission did not plead apportionment but rather sought that the Court find the legal fees in their entirety were on revenue account.

Their second submission was that, since the Devonport Ferry service contract would have required no significant infrastructure expenditure by Fullers, it was temporary in duration (five years in length, but tender would arise again in two years), and would sit alongside other services already being run by Fullers, the contract—if the Court found it was the purpose of the litigation—was not structural.

The last submission for Fullers was that Baragwanath J had wrongly applied the legal tests to determine whether the damages would have been on capital or revenue account. His Honour had endorsed the Commissioner's argument that the damages were based on a lost opportunity to earn profits and if they had been won, would have been on capital account. Fullers submitted that if awarded, the damages would constitute a "hole in the profits" and so would have been on revenue account.

The Commissioner submitted that:

(a) Fullers' focus on what was intended to be achieved by the litigation was incorrect as it focused on the relief that could be expected. To do so is a focus on the juristic rights rather than the business objective of Fullers, which is contrary to the *Hallstroms* and *BP Australia* decisions.

(b) The correct test for whether an item of expenditure is capital or revenue is the one set out in the *Hallstroms* decision, which is by reference to what the expenditure is calculated to effect from a practical and business point of view.

(c) Legal fees can either be capital or revenue depending upon the purpose for which they were incurred. Here the purpose was to secure a monopolistic contract which would have been a major addition to Fullers' business. Whether or not that objective was achieved is irrelevant to the characterisation of the item of expenditure.

(d) In this case the Court was not required to descend into the balancing and weighing exercise that is appropriate in borderline cases. However even if one did weigh up the factors, the result is that the expenditure was clearly to secure a capital asset.

The Court confirmed the reasoning by Baragwanath J at the High Court and endorsed the Commissioner's submission. Fullers' submissions were rejected on the basis that they consider the matter too narrowly when examining the objective of the litigation. From a practical business point of view the objective was either to enforce the process contract, as a step to secure the contract itself or the damages equivalent to it. Therefore there was no substantive difference between the process contract and the Devonport Ferry contract itself.

The Court considered it "incontrovertible" that the ferry contract would have been on capital account "in the particular (and rather unusual) circumstances of this case" because it was a long-term monopolistic contract which would have contributed some 60% to Fullers' revenue. The success or otherwise of this objective was irrelevant. The damages were for the loss of a capital asset, the ferry contract. It is not relevant that income from the contract would have been on revenue account because all income from capital assets is on revenue account.

REGULAR FEATURES

DUE DATES REMINDER

March 2006

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

20 **Employer deductions**

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

31 **GST return and payment due**

April 2006

7 **End-of-year incme tax**

2005 end-of-year income tax due for clients of agents with a March balance date

20 **Employer deductions**

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 calendars 2005–2006* and *2006–2007*. These calendars reflect the due dates for small employers only—less than $100,0000 PAYE and SSCWT deductions per annum.