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TAX INFORMATION

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REGULAR CONTRIBUTORS TO THE TIB

Office of the Chief Tax Counsel

The Office of the Chief Tax Counsel (OCTC) produces a number of statements and rulings, such as interpretation statements, binding public rulings and determinations, aimed at explaining how tax law affects taxpayers and their agents. The OCTC also contributes to the "Questions we've been asked" and "Your opportunity to comment" sections where taxpayers and their agents can comment on proposed statements and rulings.

Legal and Technical Services

Legal and Technical Services contribute the standard practice statements which describe how the Commissioner of Inland Revenue will exercise a statutory discretion or deal with practical operational issues arising out of the administration of the Inland Revenue Acts. They also produce determinations on standard costs and amortisation or depreciation rates for fixed life property used to produce income, as well as other statements on operational practice related to topical tax matters.

Legal and Technical Services also contribute to the "Your opportunity to comment" section.

Policy Advice Division

The Policy Advice Division advises the government on all aspects of tax policy and on social policy measures that interact with the tax system. They contribute information about new legislation and policy issues as well as the Orders in Council.

Litigation Management

Litigation Management manages all disputed tax litigation and associated challenges to Inland Revenue's investigative and assessment process including declaratory judgment and judicial review litigation. They contribute the legal decisions and case notes on recent tax decisions made by the Taxation Review Authority and the courts.

GET YOUR TIB SOONER ON THE INTERNET

This *Tax Information Bulletin (TIB)* is also available in PDF at **www.ird.govt.nz**

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

If you would prefer to get the *TIB* from **www.ird.govt.nz**, please email us at **tibdatabase@ird.govt.nz** and we will take you off our mailing list.

You can also email us to advise a change of address or to request a paper copy of the *TIB*.

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YOUR OPPORTUNITY TO COMMENT

Inland Revenue regularly produces a number of statements and rulings aimed at explaining how taxation law affects taxpayers and their agents. Because we are keen to produce items that accurately and fairly reflect taxation legislation and are useful in practical situations, your input into the process, as a user of that legislation, is highly valued.

A list of the items we are currently inviting submissions on can be found at **www.ird.govt.nz**. On the homepage, click on "Public consultation" in the right-hand navigation. Here you will find drafts we are currently consulting on as well as a list of expired items. You can email your submissions to us at **public.consultation@ird.govt.nz** or post them to:

Public Consultation
Office of the Chief Tax Counsel
Inland Revenue
PO Box 2198
Wellington

You can also subscribe to receive regular email updates when we publish new draft items for comment.

Below is a selection of items we are working on as at the time of publication. If you would like a copy of an item please contact us as soon as possible to ensure your views are taken into account. You can get a copy of the draft from **www.ird.govt.nz/public-consultation/** or call the Team Manager, Technical Services Unit on 04 890 6143.

Ref	Draft title	Description
XPB0038	Decision not to reissue rulings BR Pub 03/07 – BR Pub 03/10: Fishing quota and marine farming authorisations – secondhand goods input tax credits	This statement sets out the decision not to reissue the expired public rulings BR Pub 03/07 – BR Pub 03/10: Fishing quota and marine farming authorisations – secondhand goods input tax credits. These rulings expired on 12 November 2006. The issue addressed by these rulings was whether GST input tax credits were available to GST-registered persons who acquired fishing quota or marine farming authorisations from GST-unregistered persons.

IN SUMMARY

Binding rulings

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Subsidised transport provided by employers to employees – value for fringe benefit tax purposes

This statement advises that expired public ruling BR Pub 02/01 "Subsidised transport provided by employers to employees – value for fringe benefit tax purposes" will not be reissued, and the reason why.

Product ruling BR PRD 09/01

This ruling applies to scholarships provided by the New Zealand Māori Arts and Crafts Institute to students enrolled in a Diploma in Traditional Whakairo (Māori carving) course, for the purposes of covering students' living costs.

New legislation

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Orders in Council

Student loan scheme – interest rate for 2009–10

The student loan interest rate for the 2009–10 tax year has been set at 6.8%.

Student loan scheme – volunteer exemption

Four organisations have been added to volunteer exemption list with effect from 1 April 2009.

Use-of-money interest methodology and rate changes

The Taxation (Use of Money Interest Rates Setting Process) Regulations 2009 amend the prescribed process used in setting the use-of-money interest underpayment rate.

The Taxation (Use of Money Interest Rates) Amendment Regulations 2009 reduce the use-of-money interest underpayment and overpayment rates.

Drop in FBT rate for low-interest loans

Fringe benefit tax on low-interest, employment-related loans has dropped to 8.05%, effective from 1 January 2009.

Legislation and determinations

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2009 International tax disclosure exemption ITR20

Section 61 of the Tax Administration Act 1994 requires people to disclose interests they hold in foreign entities. The 2009 International tax disclosure exemption exempts some people from this requirement. The scope of the exemption is broadly the same as that of the 2008 exemption.

Determination E12: Persons excused from complying with section EA 3 of the Income Tax Act 2007

This determination cancels and replaces Determination E11: Persons not required to comply with section EF 1 of the Income Tax Act 1994.

Standard practice statements

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SPS 09/01: Compulsory deductions from bank accounts

This SPS sets out Inland Revenue's practice on the use of statutory notices (referred to in this statement as "deduction notices") which are from time to time issued to banks requiring them to make deductions from their customers' accounts.

IN SUMMARY (continued)

Questions we've been asked

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QB 09/01: Payments made in addition to financial redress under Treaty of Waitangi settlements – income tax treatment

This item addresses the income tax treatment of payments (based on interest for the period between settlement and payment) made to claimants under Treaty of Waitangi settlements and paid in addition to financial redress under the settlement.

Legal decisions – case notes

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The Commissioner is correct not to exercise statutory discretion

TRA 017/08 Decision 5/2009

The Commissioner was correct not to exercise his discretion at section 141KB to remit a short fall penalty.

Structured finance taxpayer's appeal dismissed

Westpac Banking Corporation v Commissioner of Inland Revenue

Taxpayer's appeal from High Court decision to strike out a cause of action dismissed.

Time of assessment by Commissioner not seen as justification to uphold judicial review

Amaltal Fishing Company Limited v Commissioner of Inland Revenue

The time of assessment is established by the facts of the case. In order for judicial review to apply, the taxpayer will need to establish exceptional circumstances and provide evidence of the effect on them.

Taxation Review Authority held relocation drivers are independent contractors and not employees

TRA Decision 4/2009

The taxpayer engaged drivers to relocate its cars to different places in New Zealand. The taxpayer filed PAYE returns on the basis that the drivers were independent contractors. The Commissioner disagreed. The Tribunal decided that the Commissioner was incorrect and held that the drivers were independent contractors.

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 their tax liability based on it.

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

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

SUBSIDISED TRANSPORT PROVIDED BY EMPLOYERS TO EMPLOYEES – VALUE FOR FRINGE BENEFIT TAX PURPOSES

BR Pub 02/01 applied from 1 July 2002 to 1 July 2007. It was a reissue of BR Pub 99/02, which applied from 1 July 1999 to 30 June 2002. Since the ruling was reissued, the Income Tax Act 1994 has been repealed and replaced with the Income Tax Act 2004, which has also now been repealed and replaced with the Income Tax Act 2007.

The provisions in the Income Tax Act 2007 (sections CX 2, CX 9, RD 33, RD 54 and the definition of "subsidised transport" in section YA 4) clearly provide the method for valuing the benefit for fringe benefit purposes where transportation or entitlement to transportation is provided by an employer to an employee, in circumstances where that employer carries on a business that consists of or includes transportation of the public. The 2007 legislation has clarified how the benefit is to be valued when it is provided by a third party under an arrangement with the employer.

As a result of these clarifications to the law, BR Pub 02/01 will not be reissued.

PRODUCT RULING – BR PRD 09/01

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 Māori Arts and Crafts Institute ("the Institute").

Taxation Law

All legislative references are to the Income Tax Act 2007 unless otherwise stated.

This Ruling applies in respect of section CW 36.

The Arrangement to which this Ruling applies

The Arrangement is the payment of a scholarship by the Institute to students enrolled in the "Te Wananga Whakairo Rakau O Aotearoa" or a Diploma in Traditional Whakairo course. Further details of the arrangement are set out in the paragraphs below:

1 The Institute was established by the New Zealand Māori Arts and Crafts Institute Act 1963. Under that Act, the purpose of the Institute is to operate as a showcase for Māoritanga with an emphasis on displaying aspects of Māori culture to tourists. It is also charged under the Act with furthering the development of carving in a traditional manner.

2 The Institute has awarded two types of certificate since 1967:
   - The New Zealand Māori Arts and Crafts Institute Diploma, and
   - The New Zealand Māori Arts and Crafts Institute Certificate.

3 In 1994 a "needs analysis" of the Institute was undertaken. It was decided to focus activities on training and educating Māori. Accordingly since 1996 the Institute has offered a three-year Diploma course in Māori carving (called "Te Wananga Whakairo Rakau O Aotearoa" or a Diploma in Traditional Whakairo). The content of the Diploma has been modularised and Certificates are awarded for the successful completion of each of the 14 modules. The 14 modules are:

Module 1 = Introduction to Māori Art
Module 2 = Tool Technology
Module 3 = Tool Care and Maintenance
Module 4 = Manufacture Patuki
Module 5 = Manufacture Tekoteko
Module 6 = Introduction to Māori Design
Module 7 = Tribal Styles
Module 8 = Nga Patu o te Riri (combat clubs)
Module 9 = Nga Rakau o te Riri (combat staffs)
Module 10 = Nga Waka Mauri
Module 11 = Taonga Whakatautau
Module 12 = Taonga Puoro (musical instruments)
Module 13 = Hanga Whare
Module 14 = Hanga Waka

4 The Institute has trained student carvers since 1967. Initially, between four to eight carvers were taken on but since 1983 the intake has been limited to three to five students per year.

The Scholarship Agreement ("the Agreement") and Scholarship Policy ("the Policy")

5 The Institute offers a limited number of scholarships to assist students ("Tauira") while they are undertaking their studies. The Scholarship Agreement entered into between the Institute and its Tauira has the following features:

- Each scholarship is for the amount of $18,200.00 per annum paid in weekly sums over a three-year term. The amount of the annual scholarship payments may be adjusted from time to time to reflect changes in the Consumer Price Index.
- The Agreement sets out the hours of class attendance required by the Tauira. Terms and study periods are also specified.
- The Agreement states that the Institute will provide a uniform and tools for the Tauira.
- Any carvings or other items produced by the Tauira in the course of their studies are the property of the Institute.

6 The scholarship payments aim to help cover the living costs of Tauira. Tauira have generally moved from their tribal area, are young and have very few assets. All costs of training, protective clothing, tools, equipment and raw materials are covered by the Institute.

7 The Institute also has a scholarship policy which is set out below:

Scholarship policy

i) The Māori Arts and Crafts Institute now offers student scholarships to successful applicants to Te Wananga Whakairo.

ii) Scholarships of three years' duration will be offered to successful applicants to Te Wananga Whakairo beginning in February of each calendar year. The number of whakairo students will be determined by the CEO.

iii) Scholarships will be awarded to a successful applicant for one year of studies upon recommendation of the interview panel.

iv) A review of year one will be undertaken encompassing the students' achievements and compliance with Te Wananga and New Zealand Māori Arts and Crafts Institute policies.

v) The scholarship awarded for all students is [$18,200.00 per annum] for three years.

vi) Award payments will be made weekly in an effort to assist students budget adequately for the year.

vii) Award payments will be direct credited to student BNZ bank accounts and record of payments identified through student bank statements.

viii) Te Wananga reserves the right to terminate a student's scholarship with one week's notice of such termination, for serious breaches of Wananga/ Institute policies and dismissal through misconduct.

a) Students will, for the first three months of their first year with Te Wananga, move through a probation period. During this time Te Wananga staff and students will determine suitability/ ability to cope with the course challenges.

b) Termination of a student's scholarship may also be the result of the student's inability to fully complete module assignments or practice tasks described within the Wananga's curriculum to prescribed standards and within given time-frames.

(c) students who wish to terminate their scholarships may do so either during the probation period or by giving one week's notice of such termination in writing.

8 The applicant notes that nine Tauira are now enrolled in carving courses.

How the Taxation Law applies to the Arrangement

The Taxation Law applies to the Arrangement as follows:

- Scholarship payments made by the Institute to a student pursuant to the Arrangement will be exempt income of the student under section CW 36.

The period for which this Ruling applies

This Ruling will apply for the period from 6 November 2008 to 5 November 2013.

This Ruling is signed by me on the 14th day of January 2009.

James Mulcahy
Sector Manager

NEW LEGISLATION

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.

ORDERS IN COUNCIL

STUDENT LOAN SCHEME – INTEREST RATE FOR 2009–10

The student loan scheme interest rate for the 2009–10 tax year has been set at 6.8% using the formula adopted in 2006. Details of the formula can be found in *Tax Information Bulletin*, Vol 18, No 3 (April 2006).

Student Loan Scheme (Total Interest Rate) Regulations 2009 (SR 2009/30)

STUDENT LOAN SCHEME – VOLUNTEER EXEMPTION

The following organisations have been added to the list of organisations that are "named" for the purposes of section 38AE(1)(b) of the Student Loan Scheme Act 1992, with effect from 1 April 2009:

- Australian Volunteers International
- Pioneers (New Zealand)
- Presbyterian Church of Aotearoa New Zealand
- Students Partnership Worldwide (Australia).

Campus Crusade for Christ, New Zealand, which was added to the list of "named" organisations last year, has changed its name to Tandem Ministries and its listing has been changed to reflect this.

The effect of being "named" is that student loan borrowers working overseas as a volunteer or for a token payment for these organisations may be granted an exemption, for a period of up to two years, from the requirement that they be present in New Zealand for 183 or more days to qualify for an interest-free loan.

Borrowers must be engaged in one or more of the following activities to qualify for the exemption:

- work to relieve poverty, hunger, sickness, or the ravages of war or natural disaster
- work to improve the economy of a developing country, or
- work to raise the educational standards of a developing country.

Student loan borrowers seeking the exemption should contact their local Inland Revenue office.

Student Loan Scheme (Charitable Organisations) Amendment Regulations 2009 (SR 2009/29)

USE-OF-MONEY INTEREST METHODOLOGY AND RATE CHANGES

The Taxation (Use of Money Interest Rates Setting Process) Regulations 2009, made on 2 February 2009, amend the prescribed process or methodology used in setting the use-of-money interest underpayment rate.

The process is set using the Reserve Bank of New Zealand's 90-day bank bill rate plus 450 basis points (4.5%). Previously, the process was contained in the Taxation (Use of Money Interest Rate Setting Process) Regulations 1997 and was set using the Reserve Bank of New Zealand's business base lending rate plus 200 basis points (2%).

The methodology for calculating the overpayment rate remains unchanged; it is also based on the Reserve Bank of New Zealand's 90-day bank bill rate, minus 100 basis points (1%).

The Taxation (Use of Money Interest Rates) Amendment Regulations 2009 also made on 2 February 2009 reduced the use-of-money interest underpayment rate from 14.24% to 9.73% and the overpayment rate from 6.66% to 4.23%. These rate changes apply from 1 March 2009.

These changes were part of the government's proposed assistance package for small and medium enterprises that was announced on 4 February 2009. Other initiatives in that package (other than the reduction in the FBT prescribed interest rate applying to low-interest, employment-related loans) are contained in the Taxation (Business Tax Measures) Bill introduced to Parliament on 10 February 2009.

Taxation (Use of Money Interest Rates Setting Process) Regulations 2009 (SR 2009/6)

Taxation (Use of Money Interest Rates) Amendment Regulations 2009 (SR 2009/7)

DROP IN FBT RATE FOR LOW-INTEREST LOANS

The prescribed rate used to calculate fringe benefit tax on low-interest, employment-related loans has dropped to 8.05%, down from the 10.90% rate which has applied since 1 October 2008.

The rate will apply retrospectively from 1 January 2009. This is because when this rate is lowered, the new rate applies from the start of the current quarter.

The rate is reviewed regularly to align it with the results of the Reserve Bank's survey of first home mortgage interest rates.

The new rate was set by Order in Council on 2 February 2009.

Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2009 (SR 2009/8)

LEGISLATION AND DETERMINATIONS

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2009 INTERNATIONAL TAX DISCLOSURE EXEMPTION ITR20

Introduction

Section 61 of the Tax Administration Act 1994 (TAA) requires disclosure of interests in foreign entities.

Under section 61(1) of the TAA, a person who has a control or income interest in a foreign company or an attributing interest in a foreign investment fund (FIF) at any time during an income year must disclose the interest held.[1] However, section 61(2) allows the Commissioner of Inland Revenue to exempt any person or class of persons from this requirement if disclosure is not necessary for the administration of the international tax rules (as defined by section YA 1) contained in the Income Tax Act 2007 (ITA).

To balance the revenue forecasting and risk assessment needs of the Commissioner with the compliance costs of taxpayers providing the information, the Commissioner has issued an international tax disclosure exemption under section 61(2) which applies for the income year corresponding to the tax year ended 31 March 2009. This exemption may be cited as "International tax disclosure exemption ITR20" and the full text appears at the end of this item.

Scope of exemption

The scope of the 2009 disclosure exemption is the same as for the 2008 exemption.

Interests held by residents

Disclosure is required by residents holding these interests:

1 an attributing interest in a FIF in respect of which FIF income or FIF loss arises where the:

  a) branch equivalent, accounting profits, deemed rate of return or cost method of calculation is used, or

  b) fair dividend rate or comparative value method of calculation is used and the resident is a "widely held entity", or

  c) fair dividend rate or comparative value method of calculation is used and the resident is not a widely held entity. In this case disclosure is required if the FIF in which there is an attributing interest is incorporated (in the case of a foreign company) or otherwise tax resident, in a country with which New Zealand does not have a double tax agreement in force as at 31 March 2009. The countries with which New Zealand does have a double tax agreement in force as at 31 March 2009 are listed below.

Australia	India	Russian Federation
Austria	Indonesia	Singapore
Belgium	Ireland	South Africa
Canada	Italy	Spain
Chile	Japan	Sweden
China	Korea	Switzerland
Czech Republic	Malaysia	Taiwan
Denmark	Mexico	Thailand
Fiji	Netherlands	United Arab Emirates
Finland	Norway	United Kingdom
France	Philippines	United States of America
Germany	Poland	

No disclosure is required by non-widely held taxpayers for attributing interests in FIFs that are incorporated or tax resident in a treaty country, if the fair dividend rate or comparative value methods of calculation are used.

A widely held entity for the purposes of this disclosure is one which is a:

- portfolio investment entity (this now includes a portfolio investment-linked life fund), or
- widely held company, or
- widely held superannuation fund, or
- widely held GIF.

Portfolio investment entity, widely held company, widely held superannuation fund and widely held GIF are all defined in section YA 1 of the ITA.

The disclosure required by widely held entities of attributing interests in FIFs which use the fair dividend rate or the comparative value method of calculation is that, for each calculation method, they disclose the end-of-year New Zealand dollar market value of investments split by the jurisdiction in which the attributing interest in a FIF is held

[1] In the case of partnerships, however, disclosure will need to be made by the individual partners in the partnership. The partnership itself is not required to disclose.

or listed. A split by the currency in which the investment is held, will be also accepted as long as it is a reasonable proxy – that is at least 90–95% accurate – for the underlying jurisdictions. For example, investments denominated in euros will not be able to meet this test and so euro-based investments will need to be split into the underlying jurisdictions.

2 an income interest of 10% or more held in a foreign company. The disclosure obligation applies in respect of all foreign companies regardless of the country of residence. For this purpose the following interests are counted:
   a) an income interest held directly in a foreign company
   b) an income interest held indirectly through any interposed foreign company
   c) an income interest held by an associated person (not being a controlled foreign company) as defined by the parts of subpart YB of the ITA that apply for the purposes of the "1988 version provisions".

For determining an income interest of 10% or more for controlled foreign companies, sections EX 14 to EX 17 of the ITA apply. For determining an income interest of 10% or more for entities that are not controlled foreign companies (CFCs), for the purpose of this exemption, sections EX 14 to EX 17 of the ITA are to be applied as if the foreign company were a CFC.

Foreign company interests

Under section 61, a resident who holds a control or income interest in a foreign company must disclose that interest, regardless of the company's country of residence. The 2009 international tax disclosure exemption also makes no distinction about residence for any interest in a foreign company which is an income interest of 10% or more. Disclosure is to be made on an IR 477 or IR 479 *Interest in a foreign company disclosure schedule* form.

The disclosure exemption makes no distinction on the residence of a foreign company with income interests of 10% or more for these reasons:

- attributed (non-dividend) repatriation rules apply to an income interest of 10% or more in a CFC regardless of the CFC's country of residence
- identifying tax preferences applied by the taxpayer (whether or not specified in Schedule 24, Part B of the ITA) in respect of an interest held in a foreign company which is resident in the "grey list", that is, a jurisdiction listed in schedule 24, Part A of the ITA (Australia, Canada, Federal Republic of Germany, Japan, Norway, Spain, United Kingdom and the United States of America).

Foreign investment fund interests

The types of interest that fall within the scope of section 61(1) of the TAA are:

- rights in a foreign company or anything deemed to be a company for the purposes of the ITA (eg, a unit trust)
- an entitlement to benefit from a foreign superannuation scheme
- an entitlement to benefit from a foreign life insurance policy
- an interest in an entity specified in schedule 25, part A of the ITA (no entities were listed when this TIB went to press).

However, the following interests are exempt (under sections EX 31 to EX 43) from being an attributing interest in a FIF and do not have to be disclosed:

- an income interest of 10% or more in a CFC (separate disclosure is required of this as an interest in a foreign company)
- certain interests in Australian resident companies listed on an approved index of the Australian Stock Exchange and required to maintain a franking account
- an interest in an Australian unit trust that has an RWT proxy with either a high turnover or high distributions
- an interest of 10% or more in a foreign company that is treated as resident in a country or territory specified in the grey list
- an interest in certain grey-list companies. Only interests in Guinness Peat Group plc qualify for this exemption
- an interest in an employment-related foreign superannuation scheme
- certain foreign pensions or annuities. See Inland Revenue's booklet *Overseas private pensions (IR 257)* for more information
- an interest in certain venture capital investments in New Zealand resident start-up companies that migrate to a grey list country
- an interest in certain grey list companies owning New Zealand venture capital companies
- an interest in certain grey list companies resulting from shares acquired under a venture investment agreement
- an interest in certain grey list companies resulting from the acquisition of shares under an employee share scheme
- an interest held by a natural person in a foreign entity located in a country where exchange controls prevent the person deriving any profit or gain or disposing of the interest for New Zealand currency or consideration readily convertible to New Zealand currency.

Interests in foreign entities held by a natural person not acting as a trustee also do not have to be disclosed if the total cost of the interests remains under $50,000 at all times during the income year. This disclosure exemption is made because no FIF income under section CQ 5 or FIF loss under section DN 6 arises in respect of these interests.

The respective forms to use for whichever FIF calculation method you apply are as follows:[2]

- IR 439 form for the accounting profits method
- IR 440 form for the branch equivalent method
- IR 443 form for the deemed rate of return method
- IR 445 form for the fair dividend rate method by widely held entities
- IR 446 form for the comparative value method by widely held entities
- IR 447 form for the fair dividend rate by individuals or non-widely held entities
- IR 448 form for the comparative value method by individuals or non-widely held entities
- IR 449 for the cost method.

Overlap of interests

A situation may arise where a person is required to furnish a disclosure for an interest in a foreign company which is also an attributing interest in a FIF. For example, a person with an income interest of 10% or greater in a foreign company which is not a CFC is strictly required to disclose both an interest held in a foreign company and an attributing interest held in a FIF.

However, to meet the disclosure obligations, only one disclosure return (either the IR 477 or IR 479 form, or the IR 439, IR 440, IR 443, IR 445, IR 446, IR 447, IR 448 or IR 449 form) is required for each interest, or group of interests in the case of fair dividend rate or comparative value method, a person holds in a foreign entity.

Here are the general rules for determining which disclosure return to file:

1. Use the appropriate IR 439, IR 440, IR 443, IR 445, IR 446, IR 447, IR 448 or IR 449 form to disclose all attributing interests in FIFs, and in particular:
   - an income interest of less than 10% in a CFC
   - an interest in a foreign life insurance policy or foreign superannuation scheme.
2. Use an IR 477 or IR 479 form to disclose:
   - an income interest of 10% or more in a foreign company (regardless of the country of residence) that is not being disclosed on an IR 439, IR 440, IR 443, IR 445, IR 446, IR 447, IR 448 or IR 449 form.

Disclosure is not required on any of the forms for an income interest of less than 10% in a foreign company (whether a CFC or not) which is also not an attributing interest in a FIF or is an attributing interest in a FIF in respect of which no FIF income or loss arises under sections CQ 5(1)(d) or DN 6(1)(d). Examples include an interest which is covered by the Australian listed company exemption from the FIF rules or interests held by a natural person, not acting in the capacity of a trustee, with a total cost of below $50,000.

Interests held by non-residents and transitional residents

Interests held by non-residents and transitional residents in foreign companies and FIFs do not need to be disclosed.

This would apply for example to an overseas company operating in New Zealand (through a branch) in respect of its interests in foreign companies and FIFs or to a transitional resident with interests in a foreign company or an attributing interest in a FIF.

The purpose of the international tax rules is to make sure that New Zealand residents are taxed on their share of the income of any overseas interests they hold. However, under the international tax rules non-residents and transitional residents are not required to calculate or attribute income under the CFC or FIF rules. The disclosure of non-residents' or transitional residents' holdings in foreign companies or FIFs is not necessary for the administration of the international tax rules.

Summary

The 2009 international tax disclosure exemption **removes** the requirement of a resident to disclose:

- a less than 10% interest in a foreign company that is not an attributing interest in a FIF or is an attributing interest in a FIF in respect of which no FIF income or loss arises
- where the taxpayer is not a widely held entity, an attributing interest in a FIF that does not constitute an income interest of 10% or more (ie, it is less than 10%) where the foreign entity is incorporated (in the case of a company) or otherwise tax resident in a treaty country, and the fair dividend rate or comparative value method of calculation is used

[2] In the case of forms IR 445 to 449 relating to the fair dividend rate, comparative value and cost method of calculation, the intention is that at a future date section 35 of the TAA will require mandatory electronic filing. For the time being, however, filing will still be paper-based for the IR 449 – cost method – and IR 447 and 448 – fair dividend rate and comparative value methods for non-widely held entities.

- where the taxpayer is a widely held entity, it limits disclosure to the end-of-year New Zealand dollar market value of investments split by the jurisdiction in which the attributing interest in a FIF is held or listed in cases where the fair dividend rate or comparative value method is used.

The 2009 disclosure exemption also removes the requirement for a non-resident or transitional resident to disclose interests held in foreign companies and FIFs.

Persons not required to comply with section 61 of the Tax Administration Act 1994

This exemption may be cited as "International Tax Disclosure Exemption ITR20".

1 Reference

This exemption is made under section 61(2) of the Tax Administration Act 1994. It details interests in foreign companies and attributing interests in foreign investment funds (FIFs) in relation to which any person is not required to comply with the requirement in section 61 of the Tax Administration Act 1994 to make disclosure of their interests, for the income year corresponding to the tax year ending 31 March 2009.

2 Interpretation

For the purpose of this disclosure exemption to determine an income interest of 10% or more, sections EX 14 to EX 17 of the Income Tax Act 2007 apply for interests in controlled foreign companies. In the case of attributing interests in FIFs, those sections are to be applied as if the FIF were a CFC.

The relevant definition of associated persons is contained in the parts of subpart YB of the Income Tax Act 2007 that apply for the purposes of the "1988 version provisions".

Otherwise, unless the context requires, expressions used have the same meaning as in section YA 1 of the Income Tax Act 2007.

3 Exemption

i) Any person who holds an income interest of less than 10% in a foreign company, including interests held by associated persons, that is not an attributing interest in a FIF, or that is an attributing interest in a FIF in respect of which no FIF income or loss arises under either section CQ 5(1)(d) or section DN 6(1)(d), is not required to comply with section 61(1) of the Tax Administration Act 1994 for that interest and that income year.

ii) Any person who is a portfolio investment entity, widely-held company, widely-held superannuation fund or widely-held GIF, who has an attributing interest in a FIF, other than a direct income interest of 10% or more in a foreign company that is not a foreign investment vehicle, and uses the fair dividend rate or comparative value calculation method for that interest, is not required to comply with section 61(1) of the Tax Administration Act 1994 in respect of that interest and that income year, if the person discloses the end-of-year New Zealand dollar market value of investments, in an electronic format prescribed by the Commissioner, split by the jurisdiction in which the attributing interest in a FIF is held or listed.

iii) Any person who is not a portfolio investment entity, widely-held company, widely-held superannuation fund or widely-held GIF, who has an attributing interest in a FIF, other than a direct income interest of 10% or more, and uses the fair dividend rate or comparative value calculation method is not required to comply with section 61(1) of the Tax Administration Act 1994 in respect of that interest and that income year, to the extent that the FIF is incorporated or tax resident in a country with which New Zealand has a double tax agreement in force at 31 March 2009.

iv) Any non-resident person or transitional resident who has an income interest or a control interest in a foreign company or an attributing interest in a FIF in the income year corresponding to the tax year ending 31 March 2009, is not required to comply with section 61(1) of the Tax Administration Act 1994 in respect of that interest and that income year if either or both of the following apply:
   - no attributed CFC income or loss arises in respect of that interest in that foreign company under sections CQ 2(1)(d) or DN 2(d) and/or
   - no FIF income or loss arises in respect of that interest in that FIF under sections CQ 5(1)(f) or DN 6(1)(f).

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

This exemption is signed on the 4th day of March 2009.

Tony Morris
Assurance Manager (Large Enterprises)

DETERMINATION E12: PERSONS EXCUSED FROM COMPLYING WITH SECTION EA 3 OF THE INCOME TAX ACT 2007

1 Explanation (which does not form part of this determination)

This determination cancels and replaces Determination E11: Persons not required to comply with section EF 1 of the Income Tax Act 1994.

2 Reference

This determination is made under section 91AAC of the Tax Administration Act 1994. It determines the extent to which a person is excused from complying with section EA 3 of the Income Tax Act 2007. This determination applies for a person's income years ending on or after 1 April 2009, until this determination is cancelled by the Commissioner.

3 Interpretation

1) This clause governs the interpretation of this determination, unless the context otherwise requires.

2) Terms not defined in this determination have the same meaning as in the Income Tax Act 2007.

3) In this determination:

audit fees, for a person and an income year, means fees incurred by the person in the preparation by a qualified person of a report, for financial reporting purposes, that relates to a financial statement for the person and the income year

balance date, for a person and an income year, means the last day of the person's income year

expiry date, in relation to expenditure incurred in an income year, means—

a) if the expenditure relates to payment for services, the date by which it is reasonably expected that performance of the service will be completed:

b) if the expenditure relates to payment for, or in relation to, a chosen action—

i) for a definite period, the last day of the period; or

ii) for an indefinite period, the day on which it is reasonably expected that the period will end

financial statement, in relation to a person—

a) means, subject to paragraph b),—

i) a balance sheet:

ii) a profit and loss account:

iii) group accounts:

iv) a financial statement within the meaning of that term in section 8 of the Financial Reporting Act 1993:

v) a group financial statement within the meaning of that term in section 9 of the Financial Reporting Act 1993:

vi) a supporting note or statement that accompanies the financial statement:

b) does not include—

i) a statement of production quality or production volume

ii) a statement prepared in relation to the exercise of any rights in respect of which royalties are payable

mandatory accounting costs, in relation to a person and an income year (the **reported year**), means expenditure incurred by the person for the purpose of meeting any requirement imposed on the person by operation of law to provide accounting, statistical, operational, sociological, or other information in respect of—

a) events occurring in the reported year:

b) a state of affairs in the reported year:

c) events occurring in, or a state of affairs in, the income year that immediately follows the reported year, if the events or state of affairs are required to be reported in the financial statements for the reported year

periodic charges means expenditure regularly incurred on a rated annual or more frequent basis, and includes local authority levies other than rates, licences and registrations

qualified person means—

a) a person qualified for appointment as an auditor of a company in terms of section 165 of the Companies Act 1955 or section 199 of the Companies Act 1993:

b) a person similarly qualified, according to the law in any other jurisdiction, for appointment as an auditor of a body corporate.

4 Determination

A person who, for an income year to which this determination applies, is allowed a deduction for an expenditure is excused from complying with section EA 3 of the Income Tax Act 2007 in respect of the expenditure and the income year to the extent to which—

a) the expenditure is described by a row in column 1 of the schedule; and

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b) the unexpired portion of the expenditure and the unexpired portions of all other expenditures also described by the row do not, in total, exceed the maximum total amount specified in column 2 of the relevant row of the schedule; and

c) the length of time between the balance date for the income year and the subsequent expiry date of the expenditure does not exceed the time period specified in column 3 of the relevant row of the schedule; and

d) in relation to expenditure on goods specified in column 1 of rows d) and k) of the schedule, the goods are in the possession of the person at balance date; and

e) the deduction of the expenditure has not been deferred to a subsequent income year for financial reporting purposes.

5 Expenditure incurred by partnership

For the purpose of applying this determination to partners and partnerships, section HG 2 of the Income Tax Act 2007 must be ignored, and expenditure must be treated as incurred by the partnership and not by the partners.

Schedule

	Description of expenditure	Maximum total amount of unexpired portions	Time period between balance date and expiry date
	Column 1	Column 2	Column 3
a)	rental for the lease of land or buildings relating to a period ending more than 1 month after balance date	$26,000	6 months
b)	rental for the lease of land or buildings other than rental dealt with elsewhere in this determination	–	1 month
c)	rental for the lease or bailment of livestock or bloodstock	$26,000	6 months
d)	payment for purchase of consumable aids	$58,000	unlimited
e)	insurance premiums under an insurance contract if the total amount of such expenditure incurred in the income year in respect of the contract does not exceed $12,000	–	12 months
f)	payment in respect of equipment service contracts or warranties if the consideration for the contract or warranty forms an inseparable and indeterminate part of the consideration for the asset or assets to which it relates	–	unlimited
g)	payment in respect of a contract for the service or maintenance of plant, equipment, or machinery if the total amount of such expenditure incurred in the income year in respect of the contract does not exceed $23,000	–	3 months
h)	payment for the use or maintenance of telephone and other communication equipment	–	2 months
i)	costs for services, other than those dealt with elsewhere in this determination	$14,000	6 months
j)	periodic charges, other than those dealt with elsewhere in this determination	$14,000	12 months
k)	purchase of stationery	–	unlimited
l)	subscriptions for a newspaper, journal, or other periodical, including for the maintenance or annotation of a documentary information service	–	unlimited
m)	motor vehicle registration and drivers' licence fees	–	unlimited
n)	subscriptions, or other fees (but excluding any payment in respect of a franchise agreement) entitling membership of any trade, professional, or other association if the amount of such expenditure incurred in the income year in respect of the association does not exceed $6,000	–	12 months
o)	costs on postal and courier services, including such expenditure for franking, private post boxes and private postbags, business reply post and freepost, and expenditure evidenced by the possession of postal stamps	–	unlimited
p)	rates made and levied under Part 3 of the Local Government (Rating) Act 2002 to the extent of the amount invoiced on or before balance date	–	unlimited

	Description of expenditure	Maximum total amount of unexpired portions	Time period between balance date and expiry date
Column 1		Column 2	Column 3
q)	advance bookings for travel and hotel or motel accommodation	$14,000	6 months
r)	cost of advertising	$14,000	6 months
s)	road-user charges	–	unlimited
t)	audit fees	–	unlimited
u)	mandatory accounting costs	–	unlimited
v)	expenditure described in section DB 3(1) of the Income Tax Act 2007 and not excluded by section DB 3(2) of that Act	–	unlimited
w)	direct claim settlement costs included in the outstanding claims reserve of a general insurer in relation to a contract of insurance, if the total gross claim cost (excluding GST) included in the outstanding claims reserve in relation to any 1 claim does not exceed $65,000 (excluding GST)	–	unlimited

This determination is signed by me on the 4th day of March 2009.

Robin Oliver

Deputy Commissioner, Policy, Inland Revenue.

STANDARD PRACTICE STATEMENTS

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

SPS 09/01: COMPULSORY DEDUCTIONS FROM BANK ACCOUNTS

Introduction

1 This Standard Practice Statement ("SPS") sets out Inland Revenue's practice on the use of statutory notices (referred to in this statement as "deduction notices") which are from time to time issued to banks requiring them to make deductions from their customers' accounts.

Application

2 This SPS applies to deduction notices issued under the following enactments:

- Tax Administration Act 1994 ("TAA")
- Goods and Services Tax Act 1985 ("GST Act")
- Child Support Act 1991 ("CS Act")
- Student Loan Scheme Act 1992 ("SLS Act")
- Gaming Duties Act 1971 ("GD Act")

3 This SPS applies to deduction notices issued from 12 March 2009. It replaces SPS RDC 3.1, published in TIB Vol 11, No 7 (August 1999), which is withdrawn with effect from the date of this SPS.

Legislation

4 The relevant sections and enactments are as follows:

- Section 157 of the TAA
- Section 43 of the GST Act
- Section 154 of the CS Act
- Section 46 of the SLS Act
- Section 12L of the GD Act.

Discussion

5 A deduction notice is an important debt collection tool for Inland Revenue. The relevant legislative provisions grant to the Commissioner of Inland Revenue ("Commissioner") wide powers to require a third party to make deductions from amounts that are payable, or will become payable by that third party, to a taxpayer who has tax arrears. The deduction notice may require deductions to be made by way of a lump sum or by instalments and will require the third party to forward the amount deducted to Inland Revenue by the date specified in the notice.

6 Inland Revenue will not issue a deduction notice in respect of tax arrears that are the subject of an instalment arrangement between the taxpayer and the Commissioner.

7 An amount payable by the third party includes money deposited with a bank to the credit of the taxpayer. It includes funds deposited on current account as well as funds on fixed and unfixed deposit. A deduction notice will apply to all deposits the bank receives from the day the deduction notice is received by the bank and will continue to apply until it is revoked or withdrawn.

8 A deduction notice may require deductions to be made to cover daily interest. The interest starts on the date of the deduction notice and ends on the day on which the amount required to be deducted, has been deducted. If interest is to be calculated the rate of interest will be advised in the deduction notice.

9 Deductions made by the bank are held in trust for the Crown until they are forwarded to Inland Revenue. Section 157(9) of the TAA, and sections 43(8) and 43(9) of the GST Act state that a bank is charged with holding in trust for the Crown amounts that become payable to a taxpayer from the time when the bank receives a deduction notice until the time when the deduction is required to be made by the notice. In addition, section 46 of the SLS Act refers back to the recovery provisions of section 156 to 165 of the TAA and will apply in respect of outstanding student loan debts.

10 If the deduction is not made by the bank, the amount required to be deducted is recoverable by Inland Revenue from the bank as if it were tax payable by the bank.

Standard practice

Joint accounts

11 In most cases, Inland Revenue is not able to issue a deduction notice to obtain funds from a joint account in respect of a tax debt owed by one of the joint bank account holders. The High Court case of *Commissioner of Inland Revenue v ANZ Banking*

Group (New Zealand) Limited (1998) 18 NZTC 13,643 concerned a deduction notice issued by Inland Revenue in respect of a joint account that the taxpayer held with his wife. In concluding that the bank was not required to make the deductions, the Court stated that the wife's rights in respect of the joint account could not be over-ridden unless by express statutory provision.

12 Notwithstanding the above, Inland Revenue reserves the right to issue a deduction notice in relation to a joint account where both parties jointly have tax arrears (for example, in a partnership) or where each party has separate tax arrears (and neither are under an instalment arrangement).

13 Further, Inland Revenue reserves the right to issue a deduction notice on a joint account that is being used by one of the account holders to hide funds with the intention to defeat attempts by Inland Revenue to recover tax arrears. For example, where Inland Revenue is able to demonstrate that cheques for a business have been deposited to a joint, non-business account. This will be restricted to cases where those funds can be separately identified from those of the other party of the account.

Overpaid Working for Families tax credits

14 Inland Revenue may also issue a deduction notice on a joint account where there has been an overpayment of a Working for Families tax credit. Where this has occurred the person who received the overpayment (the recipient) and their partner or spouse (if they were the partner or spouse throughout the income year to which the overpayment relates) are jointly and severally liable for the overpayment: section MF 5(2) Income Tax Act 2007. Inland Revenue is therefore able to issue a deduction notice for an account in the name of the partner or spouse or for a joint account in the name of the recipient and the partner or spouse.

Child support debts

15 Another situation where Inland Revenue may issue a deduction notice is in relation to child support debt. Section 128 of the CS Act provides that any amount of financial support payable under the CS Act is a debt due to the Crown. Similar to section 157 of the TAA, section 154 of the CS Act allows the Commissioner to issue a deduction notice to a third party requiring them to make deductions from money payable to liable parents for a child support debt. Any amount deducted under a deduction notice is deemed by section 167(2) of the CS Act to be held in trust for the Crown.

16 Section 155 of the CS Act extends this to money held in joint accounts in the name of the liable parent and one or more other persons, where the liable parent can draw from that account without the signature of the other person.

Gaming machine duty

17 Section 12K of the GD Act 1971 provides that any gaming machine duty is recoverable as a debt due to the Crown.

18 Section 12L of that Act allows the Commissioner to issue a deduction notice to a third party where a person is in default in payment of any gaming machine duty, and any amount deducted is to be paid to Inland Revenue by the date specified in the deduction notice. Any amount deducted under a deduction notice is deemed to be held in trust for the Crown until it is paid to Inland Revenue: section 12L(6)

Prosecution

19 If a bank fails to make the deductions required by the deduction notice, and there was an amount payable, or an amount became payable, Inland Revenue has the power to prosecute for not complying with the terms of the deduction notice under section 157A of the TAA.

Account monitoring

20 Under sections 6 and 6A of the TAA, the Commissioner has a responsibility to protect the integrity of the tax system and to collect the highest net revenue practicable over time while having regard to resources, the importance of promoting compliance and compliance costs faced by taxpayers. Inland Revenue acknowledges that compliance with a deduction notice results in costs to banks, especially if constant monitoring of their customers' accounts is required in all instances.

21 With this in mind, Inland Revenue will not usually require banks to conduct daily monitoring of their customers' accounts to comply with a deduction notice. Banks will only be required to check the account of their customer on receipt of a deduction notice and deduct any funds that are available at that time. If no funds are available, the bank will only need to advise Inland Revenue of this fact and will not be required to check the account any further.

22 However, Inland Revenue reserves the right to require daily monitoring of bank accounts where that is considered necessary. If Inland Revenue decides that daily monitoring is necessary, this will be communicated to the bank concerned at the time of issuing the deduction notice.

23 If daily monitoring is to be undertaken it will usually be for a maximum of 10 working days, although, from time-to-time Inland Revenue may request a bank to monitor an account over a longer period where it is considered necessary. The period of monitoring will be communicated to the bank at the time of issuing the deduction notice

Term investments

24 A deduction notice will apply to money that is held in a term investment whether or not that investment is due to mature.

Overdraft facilities

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

26 If Inland Revenue issues a deduction notice for an account which is in credit and the taxpayer attempts to avoid complying with that notice by transferring funds from that account so that it will go into overdraft then the deduction notice will take priority.

This Standard Practice Statement is signed on 12 March 2009.

Rob Wells
LTS Manager, Technical Standards

QUESTIONS WE'VE BEEN ASKED

QB 09/01: PAYMENTS MADE IN ADDITION TO FINANCIAL REDRESS UNDER TREATY OF WAITANGI SETTLEMENTS – INCOME TAX TREATMENT

Sections BD 3, CA 1(2), CC 3(1), CC 4(1) and EW 3 – definitions of "interest" and "money lent" – financial arrangement – income under ordinary concepts – Income Tax Act 2007.

Question

We have been asked whether an amount paid by the Crown in addition to Financial and Commercial Redress under a Treaty of Waitangi settlement, which is calculated on the agreed Financial and Commercial Redress (cash and commercial assets) and is described in the Deed of Settlement as "interest", is income. This amount is referred to in this item as "settlement interest".

Answer

Settlement interest is a capital receipt and not taxable.

Background

Settlements of claims in respect of historical breaches of the Treaty of Waitangi ("the Treaty") are generally conditional upon settlement legislation being passed, as legislation is necessary to ensure the finality of the settlement. This usually means that there will be a delay between agreement being reached as to the amount of the Financial and Commercial Redress (that is, cash and commercial assets) to be provided by the Crown, and payment of Financial and Commercial Redress being made to the claimants. In that event, a further payment, calculated on the amount of the agreed Financial and Commercial Redress for the period from the date on which the Deed of Settlement between the Crown and the claimants is signed to the date of payment of the Financial and Commercial Redress, may be paid by the Crown in addition to the agreed Financial and Commercial Redress. Some Deeds of Settlement have provided for the Crown to pay interest on the amount of the agreed Financial and Commercial Redress from the date of the Agreement in Principle until settlement. (An Agreement in Principle (which sets out the broad outline of the terms of settlement negotiated) is entered into before a Deed of Settlement. Following an Agreement in Principle, the details to be incorporated into the final Deed of Settlement are developed and agreed.) Interest on Financial and Commercial Redress is referred to in this item as "settlement interest".

Financial Redress under a Treaty settlement is a capital receipt: refer Interpretation Statement IS0043: "Income tax treatment of Treaty of Waitangi settlements" (*Tax Information Bulletin* Vol 16, No 10 (November 2004)). We have been asked whether settlement interest is income.

Unless otherwise stated, all legislative references are to the Income Tax Act 2007.

Whether settlement interest is income under a financial arrangement

As discussed in IS0043, a Treaty settlement is not a financial arrangement.

Treaty settlements that are conditional upon the passing of settlement legislation do not involve a debt or debt instrument (which are specifically included in the definition of "financial arrangement") as the obligation of the Crown to make payment is conditional: *Case Q2* (1993) 15 NZTC 5,005. A Treaty settlement is not a financial arrangement within the definition in section EW 3(2) as the payment made by the Crown is not "in consideration for" a benefit received by the Crown. Treaty settlement payments are made to compensate the claimants for past economic losses suffered as a result of the Crown's breaches of the Treaty rather than in return for anything provided to the Crown under a Treaty settlement. Such payments are not made for undertakings or agreements given by the claimants under a Treaty settlement, which are given as part of the process by which settlement is effected.

Therefore, settlement interest is not income under section CC 3(1).

Whether settlement interest is "interest" under the statutory definition

Settlement interest (as defined above) is not "interest" within the statutory definition, as it is not a payment "in respect of or in relation to money lent" by the claimants to the Crown: definitions of "interest" and "money lent" in section OB 1.

Money is not lent in any way by the claimants to the Crown under a Treaty settlement (paragraph (a) definition of "money lent"). As the claimants do not provide services, property or rights to property without requiring payment from the Crown, a Treaty settlement does not involve the giving of credit by the claimants (paragraph (b) of the

definition of "money lent"). A Treaty settlement does not involve an arrangement or obligation under which money is lent or credit is given by the claimants (paragraph (c) of the definition of "money lent"). Paragraph (d) of the definition of "money lent" does not apply to a Treaty settlement as an amount is not paid to the Crown in consideration for the Crown agreeing to pay a greater amount.

Therefore, settlement interest is not income under section CC 4(1).

Whether settlement interest is income under section CA 1(2)

In *CIR v Buis & Burston* (2005) 22 NZTC 19,278 the High Court held that the statutory definition of "interest" applied for the purpose of section CA 1(2). The court considered that as the statutory definition was exhaustive and as the payment in question (interest paid under section 72 of the Accident Rehabilitation and Compensation Insurance Act 1992) was not interest within the statutory definition, the payment was not income under ordinary concepts on the basis that it was interest under the common law.

The effect of the conclusion in Buis that the statutory definition of "interest" is exhaustive is that amounts that would have been income under ordinary concepts (being interest under the common law) may not be income. This result appears to be inconsistent with the relationship between section CA 1(2) and specific provisions defining income. The role of section CA 1(2) is to supplement specific provisions of the Act defining income: see *Tillard v C of T* [1938] NZLR 795; *Louisson v C of T* [1942] NZLR 30; Discussion Document on *Rewriting the Income Tax Act 1994* (September 1997). This result is also inconsistent with the purpose of the statutory definition of "interest" which was amended in order to widen rather than narrow the meaning of "interest" for income tax purposes: *Marac Life Assurance Ltd v CIR* (1986) 8 NZTC 5,086.

However, in *Buis* the court went on to consider whether the payment in question was income under ordinary concepts on any other basis, and found in that case that it was not income.

In *Reid v CIR* (1985) 7 NZTC 5,176 Richardson J set out three propositions on the meaning of income under ordinary concepts.

The first proposition was that income is something that comes in. This means that to be income, there must be either a payment in money, or a non-cash benefit, that is convertible into money; a saving in expenditure is not income: *Tennant v Smith* [1892] AC 150. Settlement interest is a payment of cash. Hence, it is "something that comes in".

The second proposition is that income imports the notion of periodicity, recurrence and regularity. Settlement interest is not paid periodically, recurrently or regularly. However, the periodicity, recurrence or regularity (or the absence of periodicity, recurrence or regularity) of payments is not determinative of itself as to whether the payment is income. It is necessary to consider the relationship between the payer and recipient and the purpose of the payment in order to decide whether the payment is income under ordinary concepts. The judgment of Richardson J in *Reid* makes this clear:

> The major determinant in many cases is the periodic nature of a payment (*FC of T v Dixon* (1952) 86 CLR 540; and *Asher v London Film Productions* [1944] 1 All ER 77). If it has that quality of regularity or recurrence then the payments become part of the receipts upon which the recipient may depend for his living expenses, just as in the case of a salary or wage earner, annuitant or welfare beneficiary. But that in itself is not enough and consideration must be given to the relationship between payer and payee and to the purpose of the payment, in order to determine the quality of the payment in the hands of the payee. (p. 5183)

To similar effect, in *FC of T v Dixon* (1952) 86 CLR 540 Fullager J commented:

> It seems to me that the appellant's receipts… must be regarded as having the character of income. They were regular periodical payments—a matter which has been regarded in the cases as having some importance in determining whether particular receipts possess the character of income or capital in the hands of the recipient… **This consideration, while not unimportant, is not decisive. What is, to my mind, decisive is that the expressed object and the actual effect of the payments made was to make an addition to the earnings, the undoubted income of the respondent…** (p. 567) [emphasis added]

In *FCT v Cooling* 90 ATC 4472 Hill J said:

> While the recurrent nature of transactions will suggest that the profit derived from them will be income, *Myer* at p. 210 makes it clear that the fact that a transaction is a one-off transaction will not preclude the profit generated being characterised as income. Similarly, while periodicity is a factor which leads to the conclusion that the periodical receipts are income: *F.C. of T. v. Dixon* (1952) 86 C.L.R. 540, the fact that a payment was received as a lump sum or as a once and for all payment will not necessarily result in the payment being received on capital account. Periodicity or the lack of it is but a factor to be taken into account. (p. 4480)

The third proposition is that whether a particular receipt is income depends on its quality in the hands of the recipient. This proposition means that it is necessary to determine the character of a receipt from the point of view of the recipient (and not the payer). In *McLaurin v FCT* (1961) 104 CLR 381 the High Court of Australia commented:

> … in point of law it would plainly be unsound to allow a determination of the character of a receipt in the hands of the recipient to be affected by a consideration of the uncommunicated reasoning which led the payer to agree to pay it. (p. 391)

In determining the character of a payment, it is necessary to consider the relationship between the parties and the purpose of the payment: see *Reid; The Federal Coke Company Ltd v FCT* 77 ATC 4255; *Riches v Westminster Bank Ltd* [1947] AC 390. The label given to the payment does not determine the true character of the payment: see *Buckley & Young Ltd v CIR* (1978) 3 NZTC 61,271.

Whether compensation is income or capital depends on whether it is paid to compensate for a loss of a capital or revenue nature: see *Case V8* (2001) 20 NZTC 10,092. Compensation for the damage, destruction or loss of a capital asset is capital: *CIR v McKenzies NZ Ltd* (1988) 10 NZTC 5,233. However, compensation for the loss of the right to use a capital asset is income, being compensation for loss of profits: *London and Thames Haven Oil Ltd v Attwooll* [1967] 2 QB 772.

The manner in which compensation is calculated does not determine its character. An amount paid to compensate for a loss of a capital nature that is calculated by reference to interest remains an amount of capital: *Glenboig Union Fireclay Co Ltd v IR Commrs* (1922) 12 TC 427; *Simpson v Executors of Bonner Maurice as Executor of Edward Kay* (1949) 14 TC 580.

The principle underlying land compensation cases such as *Marshall v Commissioner of Taxes* [1953] NZLR 335, *Public Trustee v CIR* [1960] NZLR 365 *Federal Wharf Co Ltd v Deputy Federal Commissioner of Taxation* 1 ATD 70 and *Haig v FCT* 94 ATC 5002 is that where a taxpayer has received "interest" by virtue of a statutory power in respect of a sum of money that they would have invested for income purposes, the "interest" is income under ordinary concepts because it compensates for the loss of use of a capital sum during a period in which it would otherwise have earned income. It represents the annual value or flow from that capital. In the *Federal Wharf Company* case Rich J said:

> In my opinion, the character of the interest payable under s. 26 is that of recompense for loss of the use of capital during a period of time in which it would earn income. It represents the annual value of capital. It is paid because the owner has been deprived of a capital asset which he had and has not received the fund which is to be substituted for the capital asset. The interest is the flow of that fund. In my opinion it is income. (p. 73)

In such circumstances, interest for the period before an award of compensation is made would be income under ordinary concepts.

In each case the purpose for which a payment described as "interest" was paid determines whether it is income. In the context of compensation for personal injury interest for the period from the date when the injury is suffered to the date of judgment (referred to in the judgment as "pre-judgment interest") is not regarded as compensation for loss of earnings as it is not paid in circumstances where the compensation would have been invested to derive income: *Whitaker v FCT* 98 ATC 4285. "Pre-judgment interest" in relation to compensation for personal injury does not relate to a foregone investment opportunity. It is an essential and integral element of compensation for the personal injury suffered by the taxpayer (being a payment "awarded for the period until the judgment takes effect which allows the plaintiff to be placed in or restored to the situation, as far as money can do, in which he or she would have been but for the defendant's negligence": *Haines v Bendall* (1991) 172 CLR 60). "Pre-judgment interest" is, therefore, a receipt of capital. However, interest for the period from judgment until payment (referred to in the judgment as "post-judgment interest") is income: *Whitaker v FCT*. "Post-judgment interest" is not paid to compensate the taxpayer for personal injury. The amount of compensation for personal injury was established by the judgment of the lower court in favour of the taxpayer. The court considered that "post-judgment interest" was paid because there was a delay between judgment being given, and payment being made.

The following principles can be drawn from the cases:

- To be income, there must be a payment in money or a non-cash benefit that is convertible into money: *Tennant v Smith* [1892] AC 150.
- Periodicity, recurrence and regularity may be a characteristic of income but periodicity, recurrence and regularity (or the absence of periodicity, recurrence or regularity) of payments is not determinative as to whether a payment is income: see *Reid v CIR* (1985) 7 NZTC 5,176; *FC of T v Dixon* (1952) 86 CLR 540; *FCT v Cooling* 90 ATC 4472.
- The character of a receipt is to be determined from the point of view of the recipient (and not the payer): *McLaurin v FCT* (1961) 104 CLR 381.
- In determining the character of a payment, it is necessary to consider the relationship between the payer and recipient and the purpose of the payment: see *Reid v CIR* (1985) 7 NZTC 5,176; *The Federal Coke Company Ltd v FCT* 77 ATC 4255. The label given to the payment does not determine the true character of the payment: *Buckley & Young Ltd v CIR* (1978) 3 NZTC 61,271.
- Whether compensation is income or capital depends on whether it is paid to compensate for a loss of a capital or revenue nature: *Case V8* (2001) 2 NZTC 10,092. Compensation for the damage, destruction or loss of a

capital asset is capital: *CIR v McKenzies NZ Ltd* (1988) 10 NZTC 5,233. However, compensation for loss of profits is income: *London and Thames Haven Oil Ltd v Attwooll* [1967] 2 QB 772.

- The manner in which compensation is calculated does not determine its character: *Glenboig Union Fireclay Co Ltd v IR Commrs* (1922) 12 TC 427; *Simpson v Executors of Bonner Maurice as Executor of Edward Kay* (1949) 14 TC 580.
- A payment made to compensate for the loss of the use of compensation, during a period in which the compensation would have been invested for income earning purposes, is income under ordinary concepts: *Federal Wharf Co Ltd v Deputy Federal Commissioner of Taxation* 1 ATD 70.
- In the context of compensation for personal injury, interest for the period from the date of injury until the date of judgment ("pre-judgment interest") is not regarded as compensation for lost earnings, as it is not paid in circumstances where the compensation would have been invested for income earning purposes. Pre-judgment interest does not relate to a forgone investment opportunity: *Whitaker v FCT* 98 ATC 4285.
- If there is no right to compensation, there is also no right to compensation for the loss of the use of compensation. In *Whitaker* (interest for the period from the date of judgment to payment) "post-judgment interest" was treated as income because there was a judgment debt owing. In *Marshall* it was accepted that if the Compensation Court had the power to award interest, the amount awarded was interest income for tax purposes. The majority considered that the Compensation Court had such a power. Therefore, for interest paid in the context of compensation to be income, it must be established that the interest accrued in respect of a period during which the taxpayer had an entitlement to compensation.

Nature of settlement interest

If settlement interest is part of the Treaty redress, settlement interest would be a capital receipt for the reasons outlined in IS0048. Settlement interest is not part of the financial redress (as defined) under Deeds of Settlement. However, the description used in the deed does not conclusively determine the nature of settlement interest. In determining the character of a payment, the starting point is the document embodying the transaction. The nomenclature used by the parties does not necessarily determine the nature of a payment and it is appropriate to take into account the surrounding circumstances in order to determine the character of the payment: *Buckley & Young Ltd v CIR* (1978) 3 NZTC 61,271, 61,273-61,274. Therefore, it is appropriate to consider the context in which Treaty settlements are made in order to determine whether settlement interest constitutes part of the Treaty redress.

Under the Treaty the Crown guaranteed to Māori "the full exclusive and undisturbed possession of their Lands and Estates Forests Fisheries and other properties which they may collectively or individually possess so long as it is their wish and desire to retain the same in their possession". The Crown has accepted that this obligation was breached in some instances and that land was acquired from Māori in ways that breached the principles of the Treaty. Most historical Treaty claims relate to land loss in circumstances involving a breach of the Crown's obligations under the Treaty. See *Healing the Past, Building a Future: A Guide to Treaty of Waitangi Claims and Negotiations with the Crown* 2nd ed (2002), Wellington: Office of Treaty Settlements ("the OTS publication").

The redress under a Treaty settlement includes the acknowledgement and apology made by the Crown for the wrongs done to the claimant and cultural redress (which is intended to meet the cultural interests of the claimants) as well as redress for economic losses.

The overall value of the redress and the form in which redress for economic losses is provided (cash or property) is a matter entirely for negotiation between the claimants and the Crown. The main factors taken into account in determining the overall redress quantum are the amount of land lost by the claimants, the seriousness of the Crown's breaches and the benchmarks set by previous settlements: the OTS publication p. 89.

The OTS publication notes that full compensation for all economic losses resulting from historical Treaty breaches is not possible given the difficulty of calculating the losses resulting from the Crown's Treaty breaches (due to the time that has elapsed, the complexity of identifying the effects of various causes on the present economic status of the claimant group and overlaps between many claimant groups) and the high burden that full compensation or the "damages" approach to redress would place on present and future generations of taxpayers (p. 89). The aim of financial and commercial redress is to "contribute to re-establishing an economic base as a platform for future development" (p. 87). The OTS publication says (p. 95):

> If settlement legislation is required to make a settlement complete, there may be a significant delay between signing the Deed of Settlement and the payment of cash or transfer of other assets. Depending on the expected length of the delay, the Crown and claimant groups may need to negotiate whether the Deed should provide for interest on the redress

> quantum from the date of the Deed to when it is actually paid. This will maintain the value of the settlement to the claimant group. *Interest is paid in a lump sum with the settlement quantum, but does not form part of the redress quantum. This is because it is a transaction cost rather than redress.* If the Crown agrees to pay interest, the rate of interest will depend on market conditions and, as with any interest receipt, tax may be payable. [emphasis added]

Once the overall value of the redress is agreed, negotiations are carried out in respect of the form in which redress is to be provided (cash or assets). Treaty settlements are intended to be full and final settlements of historical claims and the settlement of historical grievances is intended to put the relationship between the Crown and claimants on a new footing based on the principles of the Treaty: OTS publication p. 84. The Crown recognises that unless settlements are fair and remove the sense of grievance, they will not be durable: OTS publication p. 28.

The terms of the settlement between the claimants and the Crown are recorded in a formal Deed of Settlement that sets out the rights and obligations of the Crown and the claimants. Generally a Deed of Settlement and the settlement itself are conditional on the enactment of settlement legislation and the establishment of a governance entity to receive Financial and Commercial Redress. However, some provisions in a Deed of Settlement (such as the obligation to take steps to enable the conditions in the Deed of Settlement to be satisfied) are binding on execution of the Deed.

No rights arise under a Treaty settlement until settlement legislation is enacted. The enactment of settlement legislation is part of the process by which claimants become entitled to receive redress.

The Commissioner accepts that the true nature of settlement interest is that it is an economic or present value adjustment to maintain the value of the agreed redress. Settlement interest is an integral element in the calculation of compensation for a loss of a capital nature. The payment of settlement interest maintains the economic value of the agreed principal amount. Settlement interest is part of the price for securing settlement. Without such an adjustment to the principal amount to compensate for the delay in payment following settlement being reached between the parties, the claimants' grievances may not be completely addressed.

Therefore, the Commissioner considers that given these factors and the unique nature of the treaty settlement process, settlement interest is a capital receipt, being a further instalment of compensation for a capital loss.

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 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.

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

THE COMMISSIONER IS CORRECT NOT TO EXERCISE STATUTORY DISCRETION

Case	TRA 017/08 Decision 5/2009
Decision date	24 February 2009
Act	Tax Administration Act 1994
Keywords	Section 141KB

Summary

The Commissioner was correct not to exercise his discretion at section 141KB to remit a short fall penalty.

Impact of decision

Limited as section 141KB has since been repealed.

Facts

The taxpayer partnership sold property as part of its GST activity. This was thought to be zero rated but was in fact subject to GST. The purchaser paid the GST portion. The taxpayers' solicitor sent numerous items of correspondence referring, indirectly, to this. However, the taxpayers failed to account for GST. Although they blamed this on their office manager, it appears the correspondence from their solicitor was not provided by the taxpayers to their office manager.

Upon being contacted by the Department the taxpayers executed an agreed adjustment. The Commissioner took the view that a shortfall penalty for an unacceptable tax position was appropriate. The taxpayer was entitled to a "good behaviour discount". The shortfall penalty was not disputed.

Subsequently the taxpayers asked the Commissioner to exercise his discretion under section 141KB of the Tax Administration Act 1994 (TAA). The Commissioner declined to do so, on the basis that the taxpayers did not satisfy the conditions of that section.

The taxpayers commenced a dispute and ultimately a challenge to the Taxation Review Authority (TRA).

Decision

The TRA found for the Commissioner saying:

> (42) I agree with Mr. Wallace that the disputants do not meet the cumulative criteria found at section 141KB (2) of the Act which would allow the Commissioner to consider exercising the discretion found at section141KB(1) of the Act.
>
> (43) The Commissioner accepts that there was a "clear mistake or simple oversight" by the disputants within the meaning of section 141KB(2)(1). This pre-condition in the section is not in dispute.
>
> (44) However, the disputants failed to make a voluntary disclosure of the tax shortfall within the meaning of section 141G(1) of the Act. I understand that the disputants accept that no voluntary disclosure was made, and do not rely upon this ground in section 141 KB (2)(a)(ii). As section 141 KB (2) (a)(ii) contains two alternative criteria, the disputants' failure to satisfy this criterion is not necessarily fatal to the exercise of the discretion in that section. That other criterion is that the tax shortfall is "temporary" under section 141I(3). I consider that the disputants' tax shortfall was not a temporary tax shortfall within the meaning of section 141I of the Act as it was not permanently reversed or corrected before the disputants were first notified of a pending tax audit or investigation on 26 March 2005.
>
> (47) I agree that the taxpayer fails to meet the element of section 141I(3)(d) that the tax shortfall was permanently reversed or corrected before the taxpayer was first notified of a pending tax audit or investigation.
>
> (48) Also, I agree with Mr. Wallace (and I explain below) that it is not appropriate in this particular case, that the taxpayer not be liable for the shortfall penalty. Accordingly, the disputants failed to satisfy section 141KB(2)(a)(iii).

(at paragraph [44] the last line should refer to 26 May 2005).

The Judge considered section 141KB (2) (a) (iii) stating in paragraph (66):

> (66) The Act does not identify what factors should be considered when determining whether or not it is appropriate to remit a shortfall penalty on the taxpayer, but the Act seems to focus upon the circumstances of the case relating to the particular taxpayer for whom remission is to be considered. Here, the disputants were appropriately subject to the shortfall penalty for the following reasons:
>
> a) They had the benefit of legal advice in respect of the GST implications of the sale of the property.

b) They were sent reporting letters from their lawyers (dated 27 January 2005 and 28 January 2005) regarding the property sale.

c) They were sent a final statement from their lawyer showing the deposit of $1,097,864.24 to their bank account and showing a precise break down of that sum. This settlement shows, on even a cursory glance, the payment of $997,375.00 (and a deposit of $97,500.00) being much greater than the agreed sum in the sale and purchase agreement of $975,000.00 (dated 2 February 2005). It was made clear that the GST on the sale had been collected from the purchasers.

Barber J then considered whether or not there were grounds for the exercise of sections 6 and 6A of the TAA. He concluded at paragraph [76] that:

> "while it is possible that the overarching role of sections 6 and 6A could be a relevant consideration regarding the application of section141KB (2)(a)(111) when considering if it is appropriate to remit the penalty, on the facts of this case, I find that it is not appropriate to do so. The factors in section 141KB are cumulative. Satisfying section 141KB (2)(a)(111) even with the aid of section 6 and section 6A, will not assist the disputants if, they cannot meet the other criteria for cancellation under section 141KB."

His Honour considered that, given the actual knowledge of the taxpayers and the imputed knowledge from their solicitor, using the section would be against the perceptions of integrity (par [77]).

STRUCTURED FINANCE TAXPAYER'S APPEAL DISMISSED

Case	Westpac Banking Corporation v Commissioner of Inland Revenue
Decision date	20 February 2009
Act	Sections 109 and 114 of the Tax Administration Act 1994
Keywords	Judicial review, escalation regime

Summary

Taxpayer's appeal from High Court decision to strike out a cause of action dismissed.

Impact of decision

A useful judgment discussing the role of judicial review in the tax context. The Court of Appeal favoured a narrow approach based upon the statutory provisions (considerable emphasis was placed upon sections 109 and 114 of the Tax Administration Act 1994 (TAA)) and the need for truly exceptional circumstances before any judicial review would be allowed to continue (emphasis was placed upon par [62–64] quoted in below).

Facts

This is part of the Structured Finance (SF) litigation.

It was an appeal from a decision of Harrison J (reported (2008) 23 NZTC 21,694).

The taxpayer entered into a number of international SF deals. The earliest of these deals ("First Data") was subject to a positive binding ruling and the taxpayer took the view that the subsequent deals conformed in all material senses with that ruling.

The Commissioner (primarily large Enterprises or Corporates as it then was) considered there were material factual differences and reassessed the subsequent deals relying upon section BG1. In reaching this decision the Commissioner's internal escalation process was not fully complied with.

The taxpayer sought to argue the validity of the assessments made, arguing the assessments were invalid for a number of reasons. The Commissioner sought to strike out the cause of action in the taxpayer's claim raising the validity issue arguing the claim could not succeed.

The Commissioner was successful at the High Court and the taxpayer appealed.

Decision

The Court of Appeal dismissed the taxpayer's appeal.

In giving the judgment of the Court, William Palmer P noted that the basis upon which the validity point was advanced had changed since Justice Harrison's decision [par 5].

In the course of reviewing the background [par 12–42] it was noted that the Corporates Unit and the Adjudication Unit had differing views of the facts between the First Data ruling and the facts in the subsequent deals entered into [par 27–30]. It was also noted that the internal escalation process in this particular case was not observed consistently with the escalation memorandum [par 31–38].

The Court, before reviewing the development of judicial review in England, Australia and New Zealand, emphasised the role of sections 190 and 114 of the TAA describing these as providing "a particularly inauspicious statutory context for judicial review (ie outside of the challenge process provided for by the TAA)." [at par 47].

In reviewing the New Zealand position the Court recorded:

> [53] The New Zealand authorities support the proposition that it is open to a taxpayer to challenge what purports to be an assessment which in fact does not represent the genuine assessment of the Commissioner as to the tax position of the taxpayer, cf *Commissioner of Inland Revenue v Canterbury Frozen Meat Co Ltd* [1994] 2 NZLR 681 (CA). Generally the Courts have accepted that the correctness of a tax assessment can only be challenged in challenge proceedings

> (see *Commissioner of Inland Revenue v Lemmington Holdings Ltd* [1982] 1 NZLR 517 (CA) and *Miller v Commissioner of Inland Revenue* [1995] 3 NZLR 664 (CA)) and that challenge by way of judicial review is reserved for exceptional cases, see *Miller v Commissioner of Inland Revenue* [2001] 3 NZLR 316 at [18] (PC). The cases are not particularly specific as to what circumstances are sufficiently exceptional as to warrant judicial review proceedings.

The Court also noted the existence of section 6A and the rulings regimes as being pointers in opposite directions with section 6A being "conducive" to a board approach to judicial review but the rulings regime being the opposite [par 56].

Thus the Court concluded that:

> [59] We think it appropriate to continue to apply the established principles as to judicial review in tax cases. We accept that judicial review is available where what purports to be an assessment is not an assessment. Associated with this, we accept that judicial review is available in exceptional cases and thus may be available in cases of conscious maladministration (as was recognised in *Futuris*). We can reconcile this with sections 109 and 114 on the basis that in such cases (ie no genuine assessment or conscious maladministration) what is challenged is either not an assessment, or at the least, not the sort of assessment which the legislature had in mind in enacting those sections. On this basis we see the availability of judicial review as depending on the claimant establishing exceptional circumstances of a kind which results in the amended assessment falling outside the scope of sections 109 and 114 and thereby not engaging those sections.

The Court found that a board approach to judicial review was inconsistent with section 109 and said:

> [61] We also consider that the broad approach contended for by Westpac places too much emphasis on the assessment as an exercise of a statutory power of decision. An assessment should reflect the correct tax position and a taxpayer's liability to pay tax exists independently of the assessment. If the assessment is correct, it is hard to see why complaints about process should result in the taxpayer not paying tax on a correct basis. Where there are very large sums of tax at stake (as there are here), this raises fairness considerations in relation to other taxpayers who have met their liabilities for the tax year concerned. If the assessment is wrong, it can be corrected in later challenge proceedings. If it is correct, the tax should be paid. It is frankly difficult to see what is unfair in this approach.
>
> [62] Further, it is perfectly clear that allowing collateral challenge to assessments through judicial review can provide scope for gaming and diversionary behaviour.
>
> [63] In the past taxpayers going down the judicial review route have often sought to delay the statutory processes (whether prior to, or after, assessment) until the judicial review proceedings are completed; this on the ostensibly sensible ground that until the judicial review claim is determined it is premature to proceed with the statutory process. The response of the courts has been to require the review claim to be brought in the same proceedings as the challenge. But this is not necessarily an answer to the potential for judicial review to lead to delay, as illustrated by an unsuccessful attempt by Westpac in this case to have its validity cause of actions heard first.
>
> [64] Collateral challenge involves not just delay but also diversion of effort and resources. The challenge proceedings between Westpac and the Commissioner will be complex and will fully engage the attention and resources of the Commissioner and the Court. The validity cause of action involves an attempt by Westpac to turn the case back onto the Commissioner. If it goes to trial, considerable resources which might otherwise have been devoted to the primary issue between the parties will be diverted to an inquiry into the internal processes of the Inland Revenue Department. This inquiry will throw up questions which are on the one hand difficult and nuanced (as to the subtleties of the differences of approach adopted by Rulings and Corporates) but on the other entirely irrelevant to whether Westpac owes the tax it has been assessed to pay which in the end will turn on the Judge's approach to section BG 1.

It was noted that the escalation regime is not statutory and that the Commissioner could depart from it depending upon the circumstances [par 71]. The Court then turned to the taxpayer's complaints and dismissed each in turn, applying the Court's view as articulated in the paragraphs quoted above and concluding there were no exceptional circumstances such as to justify judicial review (see for example [par 74]).

Returning to the escalation process and whether these gave raise to exceptional circumstances, it was said:

> [94] Although the escalation process and its resolution were causally connected to the amended assessment, we take the view that it would be inconsistent with the policy underlying sections 109 and 114 to allow the associated complaints of Westpac to be relied on in support of a validity challenge. To allow taxpayer litigants to trawl through processes which were antecedent to the issuing of an assessment (and the pre-assessment disputes procedure) with a view to identifying and then relying on perceived departures from internal department procedures is inconsistent with the orderly and efficient resolution of tax disputes. Such breaches could hardly be regarded as exceptional (in the sense of being rare) and to allow them to invalidate later assessments would leave very little scope for sections 109 and 114. Common-sense suggests that Inland Revenue Department officers will sometimes take shortcuts, perhaps occasionally with the knowledge that in doing so they are not conforming to, or are departing from, what is provided for in the departmental manual. Advertent departures from departmental procedures can hardly be exceptional (again in the sense of being rare). And in a situation in which the officer issuing an assessment believes that it is well founded on the facts and law, and that there is no legal impediment to it being issued, we take the view that an advertent departure is not conscious maladministration and in any event is not an exceptional circumstance in the relevant sense of excluding the operation of sections 109 and 114. This is all the more so where, as here, the alleged departure from department procedures is entirely collateral to the accuracy or otherwise of the assessment.

[95] In reaching this view we have had regard to a number of overlapping policy considerations:

(a) First and foremost the statutory policy reflected in sections 109 and 114;

(b) Secondly, the general undesirability of allowing judicial review in tax litigation (see [62], [63] and [64]);

(c) Finally, we see it as contrary to the need to treat taxpayers equally to permit a taxpayer to rely on a departure (advertent or otherwise) from a department procedure to defeat an assessment where the departure is irrelevant to the accuracy of the assessment. If this were permitted, it would amount to a judicially conferred dispensation for that taxpayer from the requirement to pay taxes which are owed and thus necessarily unfair to those taxpayers who do meet their obligations.

TIME OF ASSESSMENT BY COMMISSIONER NOT SEEN AS JUSTIFICATION TO UPHOLD JUDICIAL REVIEW

Case	Amaltal Fishing Company Limited v Commissioner of Inland Revenue
Decision date	3 February 2009
Act	Sections 109 and 138D(2) of the Tax Administration Act 1994
Keywords	Judicial review

Summary

The time of assessment is established by the facts of the case. In order for judicial review to apply, the taxpayer will need to establish exceptional circumstances and provide evidence of the effect on them.

Impact of decision

The decision confirms the findings in *Golden Bay Cement, Miller and Abbattis Properties Limited* relating to when an assessment is made. It also confirms the criteria for judicial review after assessment.

Facts

This is a judicial review by Amaltal Fishing Company (AFC) in respect of assessments made by the Commissioner in April 2006. The assessments related to income earned in the 1994 and 1995 years.

In 1994 and 1995 AFC was a wholly owned subsidiary of Amaltal Corporation Limited (ACL). In June 1996, AFC and ACL together with a third company in the Amaltal group filed tax returns for the 1994 and 1995 years. Each company was a separate entity. A request was made to have the three returns transferred as a group assessment in the name of ACL. A technical error was made when entering the AFC returns into the first system in June 1996. The error resulted in the returns going into a suspense-type account pending resolution of the error. In September 1996 the group assessment was made. However in order to resolve the error a "reassessment to nil" was entered into the first system against AFC. As a result nil notices of assessment were issued to AFC for the 1994 and 1995 years.

In November 1997 an investigation was commenced into ACL and AFC. The investigation focus was on the 1994 and 1995 tax years. It was concluded that an adjustment was required to AFC's taxable income. The issue was disputed and in March 2001 an amended assessment was issued to ACL for the 1994 year. An amended assessment was issued to ACL for the 1995 year in May 2001. The assessments incorporated AFC's income and tax. In May 2001, ACL lodged a notice of claim in relation to the amended 1994 assessment with the Taxation Review Authority (TRA). One of the grounds was that the Commissioner did not have the power to jointly assess AFC and ACL. The 1995 amended assessment was opposed on the additional ground that it was time- barred. The Commissioner accepted that the amended assessment for ACL for 1995 was time-barred. However the Commissioner then issued a Notice of Proposed Adjustment (NOPA) dated 3 September 2001 to AFC indicating an intention to increase AFC's 1995 tax. AFC issued a Notice of Response (NOR) on 6 November 2001.

On 7 August 2002, the TRA declared the 1994 amended joint assessment (under ACL) to be invalid and re-assessed ACL's tax for the 1994 year. This left the adjustments to be made to AFC for 1994, to be dealt with separately. A NOPA was issued to AFC for the 1994 year on 20 October 2004. The proposal was to increase AFC's tax. AFC's NOR was issued on 25 November 2004. On 27 April 2006 the Commissioner issued new assessments to AFC in relation to the 1994 and 1995 tax years. AFC failed to challenge the assessments within the prescribed time period. The TRA ruled that there were no "exceptional circumstances" under section 183D of the TAA 1994 (Case Y7, (2007) 23 NZTC 13,066) as did the High Court (*Amaltal Fishing Co Ltd v CIR* (2007) 23NZTC 21,639). In June 2007 AFC filed for an application in the High Court for a judicial review.

Decision

Justice Mallon initially considered section 109 of the Tax Administration Act 1994 (TAA) which deems disputable decisions correct except in proceedings. She concluded that after cases such as *Golden Bay Cement Co Ltd v CIR* [1996] 2 NZLR 665(CA; *Miller v CIR* [2001] 3 NZLR 316 (PC); and *CIR v Abattis Properties Ltd* (2002) 20NZTC 17,805 (CA) the established rules were:

a) The correctness of an assessment that has been made can only be challenged in proceedings on objection.

b) The legitimacy of the process adopted by the Commissioner and the validity of the outcome may be challenged in judicial review proceedings.

c) If a judicial review challenge is available the court has a discretion whether to grant relief by way of judicial review.

d) When an objection procedure is available it will only be in an exceptional case that the court will exercise its discretion to grant relief by way of judicial review.

Justice Mallon considered the submission by AFC that judicial review was available whenever there had been a "fatal flaw that affects the vires of a decision". That is, because the TRA and High Court found no exceptional circumstances existed ACL could not get a hearing and therefore there was no other remedial action for what it considered to be the unlawful actions of the Commissioner. At paragraph [28] of the decision she said:

> [28] I do not accept AFC's submission that its unsuccessful application to pursue its objections to the assessment through the statutory procedure point in favour of exercising my discretion to grant judicial review relief. It may be a relevant factor in some cases combined with other factors **but it is not a decisive factor in itself. The timeframe for exercising challenge rights under the statutory procedure would be too easily thwarted if that were the case…**

Nor did she agree with the Commissioner's submission that exceptional circumstances in relation to the judicial review could not be established because the TRA and High Court had already said in relation to section138D(2) of the TAA that exceptional circumstances (for allowing appeal outside time period) did not exist. Continuing on in paragraph [28] she said:

> [28] To bring a challenge under the statutory procedure outside the required timeframe an applicant must establish "exceptional circumstances" defined as being an event or circumstances beyond the control of the applicant that provides the applicant with a reasonable justification for not commencing the challenge in the required timeframe (section138D(2) Tax Administration Act 1994). **The test is narrower than matters that are potentially relevant to my discretion to grant relief on judicial review.**

Justice Mallon then visited the individual grounds upon which AFC based its application for the judicial review.

Ground one – time bar

Justice Mallon found that this was an issue which could have been decided had ACL challenged the assessment within the appropriate time period. She also found that there were no additional circumstances to justify her making a ruling that exceptional circumstances for a judicial review existed. However for completeness she went on to decide on the issue of whether or not the 2006 assessments were time barred. The legislation involved at the time was section 21D of the Inland Revenue Department Act 1974 (effective from 17 December 1992) which read:

> **21D Assessments and Determinations Made by Electronic Means**
>
> Any assessment or determination made for the purpose of any of the Inland Revenue Acts that is made automatically by a computer or any other electronic means in response to or as a result of information entered or held in the computer or other electronic medium shall be treated as an assessment or determination made by or under the properly delegated authority of the Commissioner.

Section 25 of the Income Tax Act 1974 dictates the time period for altering an assessment. It reads:

> **25 Limitation of time for amendment of assessment**
>
> (1) When any person has made returns and has been assessed for income tax for any year, it shall not be lawful for the Commissioner to alter the assessment so as to increase the amount thereof after the expiration of 4 years from the end of the year in which the **notice of original assessment was issued.**

In paragraph [44] Justice Mallon noted that:

> [44] An assessment is "the process by which the Commissioner carries out his statutory obligation to ascertain the amount on which tax is payable and the amount of tax": *Lloyds Bank Export Finance Limited v Commissioner of Inland Revenue* [1992] 2 NZLR 1 at [20].

Her Honour confirmed that amendments to the legislation were only made to clarify that time ran from the notice, and not from when the assessment was made. Her Honour could not see any distinction between the facts in AFC and *Paul Finance* and *Golden Bay*.

Mallon J then considered the evidence of the person responsible for the entry into the first system and determined that it was never her intention to make an assessment. Her honour was of the view that the four-year time period in section 25(1) of the Income Tax Act did not commence from 3 September 1996 and that notices issued on that day were issued in error.

Ground two – conditional assessment

This ground related to the failure of the Commissioner to include a deduction for depreciation in the 1995 year after he reassessed revenue expenditure as capital expenditure in the 1994 year. The contention being that the assessment for the 1995 year could not have been what the Commissioner honestly believed was correct. While he believed depreciation was available, he also believed he could not allow depreciation until the disputed issue of whether or not the 1994 assessment was correct (capital/revenue distinction) was decided. Despite agreeing with *Miller* and stating that the issue should have been dealt with in disputes proceedings, Mallon J at paragraph [60] found

that the Commissioner was in error in issuing an assessment which created a liability when the Commissioner's view was that if his opinion was upheld in relation to the 1994 assessment, he would then need to amend his 1995 assessment. Despite ruling that the issue should have been addressed in disputes proceedings Her Honour adjourned this aspect of the proceedings to allow the Commissioner 14 days to amend the assessments to reflect a depreciation allowance.

The Commissioner has since complied with the directions of the Court.

Ground three – section 27(1) of the Bill of Rights Act 1990

Section 27(1) of the Bill of Rights Act 1990 (BOR) concerns the observance of the principals of natural justice. AFC submitted that assessments were *Ultra Vires* because they were not made within a reasonable time. The Commissioner submitted that the BOR did not apply and also that there was no unreasonable delay resulting in AFC suffering any prejudice as a result of the delay.

Justice Mallon referred to *Combined Beneficiaries Union Incorporated v Auckland City COGS Committee* [2008] NZCA 423 which held that section 27(1) did not require that the determination be adjudicative in nature. The determination applied to decisions "to which natural justice ordinarily applies". Justice Mallon again recognised that there was a procedure which a taxpayer could apply in order to challenge an assessment but also recognised that section 27(1) may still apply. She then proceeded on the basis that section 27(1) may apply. The question then to be answered was "whether the principles of natural justice required that an assessment under the Income Tax Act be made without delay?" AFC relied on *Unitec Institute of Technology v Attorney-General* [2006] 1 NZLR 65 to argue that natural justice required that a decision be made within a reasonable time. The Commissioner submitted that on the facts in this case there was no evidence of unreasonable delay.

Justice Mallon then found that "there is doubt as to whether the right to natural justice in this context included the right to a determination (the assessments) without unreasonable delay." At paragraph [73] she concluded:

> [73] Turning to general principal, in broad terms natural justice requires that a person affected by a determination receives a fair hearing. What that entails in any particular case depends on the circumstances and the nature of the determination assessed in light of any relevant statutory provision.

Her Honour then followed the sequence of events and determined that in this case the delay did not cause any breach in natural justice. In isolation the 10-year period for assessment looked like a long time; however, both parties thought that the joint assessments applied in the beginning could be made. This mistake counted for a period of five years. Periods of delay after the five years were seen as undesirable but not particularly lengthy when taken in context. Justice Mallon also found that there was no financial prejudice to AFC because penalties and interest applied to the core tax and could be offset against the depreciation which would now be allowed.

Ground four – arbitrary and unreasonable adjustment

This ground relates to a decision of the investigator to assess a portion of an insurance payout to AFC as recovered expenditure rather than as capital profit. The ground raised by AFC was that the Commissioner took irrelevant considerations into account when re-assessing. The claim also alleged an error of law although the error itself was not identified. Justice Mallon found that the grounds for the review "clearly challenge the correctness of the decision". The issue of the correctness of the decision should have been dealt with under traditional statutory review grounds. The only exceptional circumstance which could justify a review was the fact that AFC was time barred, but that alone was not enough to convince her that exceptional circumstances did exist.

Justice Mallon also noted that while AFC may have convinced a hearing authority that the Commissioner was wrong she was not convinced that the Commissioner acted in an unlawful or irrational manner.

TAXATION REVIEW AUTHORITY HELD RELOCATION DRIVERS ARE INDEPENDENT CONTRACTORS AND NOT EMPLOYEES

Case	TRA Decision 4/2009
Decision date	11 February 2009
Act	Income Tax Act
Keywords	PAYE; independent contractor; employee

Summary

The taxpayer engaged drivers to relocate its cars to different places in New Zealand. The taxpayer filed PAYE returns on the basis that the drivers were independent contractors. The Commissioner disagreed. The Tribunal decided that the Commissioner was incorrect and held that the drivers were independent contractors.

Impact of decision

The usual tests were applied to determine employer/employee relationship. This case was largely dependent on its facts.

Facts

The taxpayer is a vehicle rental operator and engages drivers to relocate its cars to different places in New Zealand.

All the drivers entered into an agreement with the taxpayer which described them as independent drivers and not employees of the taxpayer. The agreement was labelled as "Relocation Driver Contract".

The taxpayer filed PAYE returns for the period 31 December 2002 to 31 August 2006 on the basis that the drivers were independent contractors. On 25 September 2006, the taxpayer was assessed $1,823,033.69 for PAYE for those periods on the basis that the drivers were employees.

Decision

Barber J held that the drivers were independent contractors for the following reasons:

1. The drivers' work is not an integral part of the taxpayer's business.
2. The performance of the driver's task, as set out in the agreement, provides for the efficiency and safety of the drivers. It does not constitute control of the task.
3. The work and remuneration for the drivers are more consistent with the lifestyle of the drivers as independent contractors.
4. The influencing factor is the agreement between the taxpayer and the drivers: It truly expresses the intention of the parties [paragraphs 32, 36–37, 87–88].
5. The agreement is not a sham [paragraph 39].