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TAX INFORMATION Bulletin

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Inland Revenue
Te Tari Taake

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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 you 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 type/title	Description/background information
XPB0039	Provision of benefits by third parties – fringe benefit tax consequences – section CX 2(2)	This public ruling considers the application of section CX 2(2) of the Income Tax Act 2007 to the receipt of a benefit by an employee from a third party where there is an arrangement between the employer and the third party, and where the benefit would be subject to FBT if it had been provided by the employer. This Ruling is a reissue of public ruling BR Pub 04/05, published in *Tax Information Bulletin* Vol 16, No 5 (June 2004), which applied for the period from 20 May 2004 until 19 May 2007.

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This determination sets out the standard-cost household service that has been provided as childcare services by taxpayers, who are natural persons, in their own domestic accommodation. It sets out the components of expenditure for this service, determines a figure for costs incurred and prescribes a calculation method.

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This determination sets the national average market values to apply to specified livestock on hand at the end of the 2008–2009 income year.

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TRA allows deduction for GST input tax on legal services provided in trusts 21

The Taxation Review Authority (TRA) held that trustees can claim a deduction for legal fees on a GST input return basis through the trust when the trust is carrying out a taxable activity even if the fees are paid for by a third party.

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The High Court dismissed the application for a stay on the basis that the taxpayer's case for establishing "exceptional circumstances" was not strong, and confirmed that judicial review proceedings cannot be used except in exceptional circumstances.

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Taxpayer failed to establish that expenditure incurred was significant in connection with her determined assessable income and therefore was non-deductible under section DJ(5)(a).

Scope of judicial review limited in tax cases 26

The Supreme Court declined the taxpayer's application for appeal to appeal the Court of Appeal's judgment limiting the scope of judicial review against the Commissioner.

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**

PUBLIC RULING BR PUB 09/02: FEDERAL INSURANCE CONTRIBUTIONS ACT (FICA) – FRINGE BENEFIT TAX (FBT) LIABILITY

Note (not part of ruling): The key issue considered by this Ruling is whether employer contributions made by an American employer, to the United States Federal Government in accordance with the US Federal Insurance Contributions Act, give rise to fringe benefit tax under the 2007 Income Tax Act. The conclusion is that such contributions do not give rise to fringe benefit tax. This Ruling replaces public ruling BR Pub 07/02 which was published in *Tax Information Bulletin* Vol 19, No 3 (April 2007). BR Pub 07/02 applies until 30 June 2009 and is a reissue of Pub 01/05 published in *Tax Information Bulletin* Vol 13, No 7 (July 2001). This new Ruling is essentially the same as the previous Ruling. However, the new Ruling has been updated and applies the Income Tax Act 2007, which came into force on 1 April 2008, instead of the equivalent provisions in the Income Tax Act 2004. The changes between the provisions in the Income Tax Act 2004 and the Income Tax Act 2007 do not affect the conclusions previously reached. BR Pub 09/02 applies for an indefinite period beginning on 1 July 2009.

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

Taxation laws

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

This Ruling applies in respect of sections CX 13, CX 14 and CX 37.

The Arrangement to which this Ruling applies

The Taxation Laws apply to the Arrangement as follows:

- Employer contributions paid under FICA do not give rise to a "fringe benefit" under section CX 13 as the contributions are not made for the benefit of employees.
- Employer contributions paid under FICA do not give rise to a "fringe benefit" under section CX 14. As trust funds established for the purpose of paying disability benefits or Medicare and funded by contributions under FICA were not established for the benefit of employees and have not been approved by the Commissioner, they are not "sickness, accident or death benefit funds" as defined in section YA 1.
- Employer contributions paid under FICA do not give rise to an "unclassified benefit" in terms of section CX 37 as a benefit is not provided by employers in connection with the employment of employees through the payment of employer contributions under FICA.
- Employee contributions required to be deducted from wages and paid under FICA do not give rise to an "unclassified benefit" as such contributions represent part of the assessable income of employees and are expressly excluded from the definition of "fringe benefit" by section CX 4.

Therefore, payments required under FICA are not subject to fringe benefit tax ("FBT").

The period or income year for which this Ruling applies

This Ruling will apply for an indefinite period beginning on 1 July 2009.

This Ruling is signed by me on the 30th day of April 2009.

Susan Price
Director, Public Rulings

COMMENTARY ON PUBLIC RULING BR PUB 09/02

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusions reached in public ruling BR Pub 09/02 ("the Ruling").

Background

The Federal Insurance Contributions Act (FICA) is the part of the US Internal Revenue Code under which employers and employees are required to make payments for the funding of social security benefits. In some circumstances an employer who employs an employee to provide services in New Zealand is required to comply with obligations under the FICA legislation. FICA applies when an "American employer" pays wages for services performed as an employee by a US citizen outside the US: sections 3101 and 3111 and the definition of "employment" in section 3121 Internal Revenue Code (Title 26 of the US Code (USC)). "American employer" means the US Government or its instruments, residents of the US or companies that are organised under the laws of the US.

If FICA applies, employers must make deductions from wages payable to an employee in respect of Old Age, Survivors and Disability Insurance ("OASDI") and Hospital Insurance (known as "Medicare"), and must pay the deductions to the Internal Revenue Service. In addition, employers are required to make payments for OASDI and Medicare (employer contributions) at the same rate. The current rate in respect of OASDI is 6.2% and in respect of Medicare the rate is 1.45%. An employer who fails to make the required payments or fails to make the payments on time is liable for a penalty.

Under FICA, amounts deducted from wages payable to employees are deemed to have been paid to employees at the time of deduction (USC Title 26–Internal Revenue Code, Chapter 21, section 3123). FICA does not provide for recovery of OASDI or Medicare payments imposed on employees from an employee where the employer has failed to make deductions.

Payments collected under FICA are paid into the US Treasury's General Fund and are appropriated to three separate funds: the Federal Hospital Insurance Trust Fund; the Federal Old-Age and Survivors Insurance Trust Fund; and the Federal Disability Insurance Trust Fund. Amounts held in these funds are not held for any particular individual.

A person must be a US citizen or legally resident in the US to be entitled to social security benefits (Public Law 104-193; Personal Responsibility and Work Opportunity Reconciliation Act of 1996).

Under the US social security legislation (USC Title 42–Public Health and Welfare Code, Chapter 7) a person must hold not less than 40 credits to be entitled to a retirement benefit. The amount needed to gain a credit changes from year to year. For the year 2009, a credit is gained for every quarter in which an employee earns more than $1090 from employment. No more than four credits can be gained in respect of a year. The minimum age to qualify for a retirement benefit depends on when a person was born.

However, a person could qualify for a disability benefit with fewer credits, depending on their age. To be entitled to a disability benefit:

- a person must have a medical condition that meets the definition of "disability" in the social security legislation; and
- 20 of the 40 credits required to qualify for a disability benefit must have been earned in the 10 years ending in the year in which the person became disabled.

If a person who is covered by social security dies, their surviving spouse or dependent children can receive a survivors benefit. The right to retirement, survivors and disability benefits cannot be assigned or transferred.

The amount of the monthly benefit paid depends on the person's earnings during the person's working life and the age at which the person retires. The amount of the benefit is calculated according to a formula in the legislation.

People aged 65 or older are entitled to receive Medicare benefits if they:

- receive a social security benefit;
- have worked long enough to be eligible for a social security benefit;
- would be entitled to a social security benefit based on their spouse's work record and their spouse is aged at least 62; or
- have worked long enough in a federal, state or local government job to be insured for Medicare.

People aged under 65 who receive disability benefits or who have permanent kidney failure may qualify for Medicare.

Legislation

"Fringe benefit" is defined in section CX 2(1) as follows::

> A **fringe benefit** is a benefit that—
>
> (a) is provided by an employer to an employee in connection with their employment; and
>
> (b) either—
>
> (i) arises in a way described in any of sections CX 6, CX 9, CX 10, or CX 12 to CX 16; or
>
> (ii) is an unclassified benefit; and

(c) is not a benefit excluded from being a fringe benefit by any provision of this subpart.

Section CX 13 provides:

(1) A fringe benefit arises when an employer contributes to a superannuation scheme for the benefit of an employee.

(2) This section does not apply if the contribution is an employer's superannuation contribution.

Section CX 14 provides:

A fringe benefit arises when an employer makes a contribution for the benefit of an employee to a sickness, accident, or death benefit fund.

"Unclassified benefit" is defined in section CX 37 as follows:

Unclassified benefit means a fringe benefit that arises if an employer provides an employee with a benefit in connection with their employment that is—

(a) not a benefit referred to in any of sections CX 6 to CX 16; and

(b) not a benefit excluded under this subpart.

Section CX 4 provides:

To the extent to which a benefit that an employer provides to an employee in connection with their employment is assessable income, the benefit is not a fringe benefit.

"Superannuation scheme" is defined in section YA 1 as follows:

Superannuation scheme—

(a) means—

(i) a trust or unit trust established by its trust deed mainly for the purposes of providing retirement benefits to beneficiaries who are natural persons or paying benefits to superannuation funds; or

(ii) (repealed)

(iii) a company that is not a unit trust, is not resident in New Zealand, and is established mainly for the purpose of providing retirement benefits to members or relatives of members who are natural persons; or

(iv) an arrangement constituted under an Act of the Parliament of New Zealand, other than the Social Security Act 1964, mainly for the purpose of providing retirement benefits to natural persons; or

(v) an arrangement constituted under the legislation of a country, territory, state, or local authority outside New Zealand mainly for the purpose of providing retirement benefits to natural persons; and

(b) for a superannuation scheme that is a trust, means the trustees of the scheme.

The definition of "arrangement" in section YA 1 reads as follows:

Arrangement means an agreement, contract, plan or understanding, whether enforceable or unenforceable, including all steps and transactions by which it is carried into effect.

The definition of "sickness, accident or death benefit fund" in section YA 1 reads as follows:

Sickness, accident, or death benefit fund means a sickness, accident, or death benefit fund that is—

(a) established for the benefit of—

(i) employees; or

(ii) the members of an incorporated society; or

(iii) the surviving spouses and dependants of those employees or members; and

(b) approved by the Commissioner.

Application of the legislation

Liability for FBT

Whether an employer is required to pay fringe benefit tax (FBT) in respect of either employer or employee contributions made under FICA depends on whether the employer has provided a "fringe benefit" (section RD 26(1)). There will be a "fringe benefit" where:

- a benefit arises in a way described in any of section CX 6, section CX 9, section CX 10 or sections CX 12 to CX 16 or a benefit of any other type is provided by an employer to an employee in connection with their employment (an "unclassified benefit"); and
- the benefit is not excluded from being a fringe benefit by any provision of subpart CX.

In Australian cases, in the FBT context, the courts have considered that a fringe benefit will not be provided unless there is a link between the benefit and a particular employee: see *Essenbourne Pty Ltd v Commissioner of Taxation* (2002) ATC 5201; *Walstern v Commissioner of Taxation* (2003) ATC 5076; *Cameron Brae Pty Ltd v FCT* (2006) ATC 4433. The Commissioner considers that this principle also applies in the New Zealand context. As with the Australian legislation, the wording of the legislation suggests that it contemplates a benefit provided to a particular employee. The definition of "fringe benefit" in section CX 2(1) refers to "a benefit that is provided by an employer to an employee in connection with their employment". Sections CX 13 and CX 14 also refer to "a contribution for the benefit of an employee". As with the Australian legislation, under the valuation provisions any payment made by the employee is to be taken into account in determining the taxable value of the fringe benefit. The need for a link between the benefit and an employee is consistent with the purpose of the FBT provisions. FBT was intended to apply to non-cash remuneration provided to an

employee and although liability for FBT is imposed on the employer, the theoretical basis for the imposition of FBT is that it is payable in respect of amounts that are essentially (or would be) income of an employee.

Contributions to superannuation scheme: section CX 13

Under section CX 13, a fringe benefit arises when an employer makes a contribution to a superannuation scheme (other than an employer's superannuation contribution) for the benefit of an employee.

The definition of "superannuation scheme" in section YA 1 includes an arrangement constituted under the legislation of a country, territory, state or local authority outside New Zealand mainly for the purpose of providing retirement benefits to natural persons (paragraph (a)(v) of the definition).

Superannuation scheme

The definition of "superannuation scheme" specifically includes an arrangement constituted under legislation.

FICA requires employer and employee contributions to fund social security benefits, including retirement benefits. The US social security legislation contains the provisions relating to eligibility for retirement benefits and the payment of retirement benefits. These two pieces of legislation together establish a system for the funding and payment of social security benefits, including retirement benefits. Therefore, there is an arrangement that is constituted under US legislation (the US social security legislation and FICA).

The Federal Old-Age and Survivors Insurance Trust Fund and Federal Disability Insurance Trust Fund were established under USC Title 42–Public Health and Welfare Code, Chapter 7 Social Security, Subchapter II, section 401). Under the US social security legislation an amount equal to 100% of the amount collected from employees and employers in respect of OASDI is appropriated to those trust funds (42 USC, section 401). Monthly retirement benefits and survivors benefits are paid out of the Federal Old-Age and Survivors Insurance Trust Fund and benefits to disabled workers and their families are paid out of the Federal Disability Insurance Trust Fund. The social security legislation sets out the conditions for entitlement to retirement benefits and provides for the payment of retirement benefits (42 USC, section 402).

For paragraph (a)(v) of the definition of "superannuation scheme" to apply, the arrangement must be mainly for the purpose of providing retirement benefits.

Payments under FICA are appropriated to the Federal Old-Age and Survivors Insurance Trust Fund and are to be used for the purpose of funding retirement benefits. Survivors benefits are also paid out of the fund to the widows, widowers and children of people who would have been entitled to receive a retirement benefit (that is, benefits could be paid out of the trust fund to people who have not reached retirement age). However, such people would be entitled to receive a benefit only if a person who qualifies for a retirement benefit has died. The principal object of creating the trust fund is to provide for the payment of retirement benefits.

FICA is part of a legislative scheme for the provision of social security benefits by the US Federal Government, which is the equivalent of provision of benefits under the New Zealand Social Security Act 1964. In *Roe v Social Security Commission* (10 April 1987) (unreported, High Court, Wellington, M 270/86, Davison CJ) the plaintiff was the recipient of a social security retirement benefit paid by the US Government. The issue was whether the benefit formed part of a programme providing benefits, pensions or periodical allowances for any of the contingencies for which benefits, pensions or allowances could be paid under the New Zealand Social Security Act. Davison CJ commented:

> The US retirement benefit is clearly on the evidence a benefit paid by the US Government of the same type as a NZ national superannuation benefit. Both are paid by the respective Governments and both are part and parcel of programmes for assistance to age-related beneficiaries. (p. 8)

The Commissioner considers that payments made under FICA and appropriated to the Federal Old-Age and Survivors Insurance Trust Fund are paid under an arrangement constituted under US legislation mainly for the purpose of providing retirement benefits to natural persons. Therefore, there is a superannuation scheme that is constituted under the social security legislation and FICA in terms of paragraph (a)(v) of the definition of "superannuation scheme". This differs from the view expressed in the Commissioner's first ruling on this issue (BR Pub 01/05). However, for section CX 13 to apply, payments made by employers under FICA must be contributions for the benefit of an employee.

Whether contributions are for the benefit of employees

Payments employers are required to make under section 3111(a) of FICA are tax. Section 3111(a) imposes on every employer "an excise tax, with respect to having individuals in his employ". An excise tax is "a tax upon an activity" (CCH *Federal tax guide reports*, paragraph 21,001); in this case a tax imposed in respect of employment (*Helvering v Davis* 57 SC 904).

However, a payment by an employer could be a contribution although the employer has a statutory obligation to make the payment. In *Case M9* (1990) 12

NZTC 2069 it was held that the predecessor of section CX 13 applied to contributions made by a local authority to the National Provident Fund, although the employer did not have a choice about making the contributions. Judge Bathgate considered that the focus of the FBT legislation was whether the contributions could be regarded as a benefit from the employees' point of view. Judge Bathgate said:

> The objector's claim that the superannuation payments by the objector on behalf of its employees compulsorily paid by it under the National Provident Fund Act, are not benefits because it had no choice as to whether to make the payments is to an extent understandable, from the employer's point of view. A benefit is often regarded as being given voluntarily, rather than compulsorily. A benefit may however be given under compulsion in some circumstances — *Yates v Starkey* [1951] 1 All ER 732. From the employees' point of view, and after all Pt XB of the Income Tax Act is only concerned with benefits received by employees, albeit from employers, the contributions to the superannuation fund can be considered as a benefit. (p. 2073)

In *Yates v Starkey*, referred to by Judge Bathgate, the Court of Appeal held that a person who had been ordered by the court to pay his wife an annual amount in trust for his children had provided funds for the purpose of the settlement of a trust. Jenkins LJ commented:

> I do not agree that the words "has provided" necessarily connote an exercise of free will. It seems to me that the taxpayer here if asked "Who is providing for the maintenance for your children?" could with perfect accuracy have replied "I am doing so under an order of the court". (p. 479)

However, for section CX 13 to apply, the contribution must be for the benefit of an employee. In *Case M9*, although the employer was required by the National Provident Fund Act to make contributions, the objective of the contributions was to provide a benefit to employees under the National Provident Fund.

In *NZI Bank Ltd v Euro-National Corporation Ltd* [1992] NZLR 528 Richardson J made the following comments in respect of the interpretation of the phrase "for the benefit of employees":

> It is not sufficient to satisfy para (b) that the shares are to be held on trust for employees. The shares must be held "for the benefit" of employees. "For" in that context means with the object and purpose of benefiting employees and the "benefit" to employees must be discernible and real. As in the case of the exercise of trustees' powers to make advances for a person's benefit, it must confer an advantage which can be enjoyed by employees. It must be of value to employees. An arrangement does not qualify as being "for the benefit of employees" unless employees actually stand to benefit. (p. 544)

Hence, for a contribution to be "for the benefit of an employee" in terms of section CX 13, the contribution must be made for the purpose of benefiting the employee and the contribution must provide something of real value to the employee.

Employer contributions required under FICA are not held in trust for any employee. The US Social Security system for the payment of retirement benefits is a pay-as-you-go scheme under which current employer and employee contributions are used to fund the payment of retirement benefits to current recipients of retirement benefits. Neither employer nor employee contributions are allocated to, or held for, individual employees.

Payments that an employer must make under FICA are not attributable to any particular employee. Excise tax is calculated on the total wages paid by the employer. Employees are not entitled to receive a refund of payments made either by employers or employees under FICA. The entitlement of employees to a retirement benefit does not depend on whether the employer has paid the excise tax imposed on the employer under FICA. To qualify for a retirement benefit, a person must be a "fully insured individual" (42 USC, section 402(a)(1)). To be a "fully insured individual" a person must hold sufficient credits (that is, a minimum of 40 credits). The number of credits earned is based on the amount of the employees' earnings over their working life and not on the payment of employer contributions. Payments made by employers under FICA also do not affect the amount of the benefit payable. The amount of the retirement benefit is based on average earnings over a person's working life, indexed to account for changes in average wages.

Employees cannot transfer or assign their right to any future benefit (42 USC, section 407). *Flemming v Nestor* 363 US 603 establishes that a person who makes payments under FICA does not as a consequence acquire a right to a benefit analogous to a property right.

The Commissioner considers that payments of excise tax under FICA are not made by employers for the benefit of any particular employee as:

- employee contributions are not held in trust for any individual employee;
- employees are not entitled to receive any part of the contributions made by employers;
- employees do not obtain the right to a retirement benefit as a consequence of the payments made by employers; and
- the payment of employer contributions by employers does not affect the amount of the benefit payable to employees.

Therefore, such payments do not give rise to a fringe benefit in terms of section CX 13.

Contributions to sickness, accident or death benefit fund: section CX 14

Under section CX 14, a fringe benefit arises when an employer makes a contribution for the benefit of an employee to a sickness, an accident or a death benefit fund.

The definition of "sickness, accident, or death benefit fund" in section YA 1 refers to a sickness, an accident, or a death fund that is:

- established for the benefit of employees, the members of an incorporated society, or the surviving spouses and dependants of those employees; and
- approved by the Commissioner.

Under the US social security legislation, separate funds are established for the payment of disability benefits and Medicare (the Federal Disability Insurance Trust Fund and the Hospital Insurance Trust Fund). Self-employed people can also earn credits so that they are entitled to receive disability benefits or Medicare. The funds are not limited to the employees of a particular employer or to employees in general. They were established to fund the payment of government-provided disability benefits and hospital and medical benefits that are available to all people who earn sufficient credits to qualify for benefits and satisfy the other conditions set out in the US legislation. Payments by employers do not directly affect employees' entitlement to disability benefits or Medicare. Whether the employer pays employer contributions does not affect the employees' entitlement to disability benefits or Medicare or the amount of the benefit.

The Commissioner considers that neither the Federal Disability Insurance Trust Fund nor the Hospital Insurance Trust Fund was established for the benefit of employees. The funds were not established for the benefit of a particular employer's employees and were not established for the benefit of employees alone. Employees do not obtain a right to receive Medicare or disability benefits as a consequence of the payments made by their employer.

To be a sickness, an accident or a death fund within the statutory definition, a fund must also be approved by the Commissioner. As the Commissioner has not approved either the Federal Disability Insurance Trust Fund or the Hospital Insurance Trust Fund, the funds cannot be sickness, accident or death benefit funds for the purpose of section CX 14.

Therefore, the Commissioner considers that a benefit does not arise in terms of section CX 14 as a consequence of payments required to be made by employers in respect of the Federal Disability Insurance Trust Fund or the Hospital Insurance Trust Fund under FICA as these funds are not sickness, accident or death funds as defined in section YA 1.

Unclassified benefit: section CX 37

The definition of "unclassified benefit" in section CX 37 refers to a benefit an employer provides to an employee "in connection with their employment" other than the benefits referred to in any of sections CX 6 to CX 16.

"Benefit" is not defined for FBT purposes. Therefore, the ordinary meaning of "benefit" applies. In *CIR v Dick* (2001) 20 NZTC 17,396 Glazebrook J commented as follows on the meaning of "benefit":

> [48] *The New Shorter Oxford Dictionary* (1993 ed) defines benefit (in relevant part) as: a favour, gift, a benefaction, an advantage, a good, pecuniary profit. Likewise the definition of advantage is: a favouring circumstance, something which gives one a better position, benefit. Looking at the dictionary meaning of those words it would appear that something may not be a benefit or advantage if it has been acquired through the provision of services or goods at market value. This, therefore, is in contrast to the definition of income.

The Commissioner considers that in the FBT context, a "benefit" is an advantage, a material acquisition that confers an economic benefit on an employee. As outlined in "QB 0043: The meaning of 'benefit' for FBT purposes" (published in *Taxation Information Bulletin* Vol 18, No 2 (March 2006)), in considering whether a benefit has been provided to an employee it is not relevant that the employee made a payment for what is provided.

For there to be a "fringe benefit", the benefit must be provided by an employer to an employee in connection with their employment. The meaning of the phrase "in connection with" was considered in *Claremont Petroleum NL v Cummings* (1992) 110 ALR 239. Wilcox J said:

> The phrase "in connection" is one of wide import, as I had occasion to observe in a different context in *Our Town FM Pty Ltd v Australian Broadcasting Tribunal* (1987) 16 FCR 465 at 479–80; 77 ALR 577 at 591–592:
>
> > The words "in connection with".... do not necessarily require a causal relationship between two things: see Commissioner for *Superannuation v Miller* (1985) FCR 153 at 154, 160, 163; 63 ALR 237 at 238, 244, 247. They may be used to describe a relationship with a contemplated future event, see *Koppen v Commissioner for Community Relations* (1986) 11 FCR 360 at 364; 67 ALR 215; *Johnson v Johnson* [1952] P47 at 50–1. In the latter case the United Kingdom Court of Appeal applied a decision of the British Columbia Court of Appeal, *Re Nanaimo Community Hotel Ltd* [1945] 3 DLR 225, in which the question was whether a particular court, which was given "jurisdiction to hear and determine

all questions that may arise in connection with any assessment made under this Act", had jurisdiction to deal with a matter which preceded the issue of an assessment. The trial judge held that it did, that the phrase "in connection with" covered matters leading up to, or which might lead up to an assessment. He said:

> "One of the very generally accepted meanings of 'connection' is 'relation between things one of which is bound up with or involved in another', or again 'having to do with'. The words include matters occurring prior to as well as subsequent to or consequent upon so long as they are related to the principal thing. The phrase 'having to do with' perhaps gives as good a suggestion of the meaning as could be had."

This statement was upheld on appeal. (p 280)

Hardie Boys J made the following comments on the meaning of "in connection with" in *Strachan v Marriott* [1995] 3 NZLR 272:

> "In connection with" may signify no more than a relationship between one thing and another. The expression does not necessarily require that it be a causal relationship: *Our Town FM Pty Ltd v Australian Broadcasting Tribunal* (1987) 16 FCR 465, 479 per Wilcox J. But, as Davies J warned in *Hatfield v Health Insurance Commission* (1987) 15 FCR 487, at p. 491:
>
> > Expressions such as 'relating to', 'in relation to', 'in connection with' and 'in respect of' are commonly found in legislation but invariably raise problems of statutory interpretation. They are terms which fluctuate in operation from statute to statute ... The terms may have a very wide operation but they do not usually carry the widest possible ambit, for they are subject to the context in which they are used, to the words with which they are associated, and to the object or purpose of the statutory provision in which they appear. (pp. 279–281)

In *The Queen v Savage* [1983] CTC 393 Dickson J in the Supreme Court of Canada commented:

> 23 … Our Act contains the stipulation, not found in the English statutes referred to, "benefits of any kind whatever ... in respect of, in the course of, or by virtue of an office or employment" … Further, our Act speaks of a benefit "in respect of" an office or employment. In *Nowegijick v The Queen* [1983] CTC 20, 83 DTC 5041, this Court said, at 25 [5045], that:
>
> > **The words "in respect of" are, in my opinion, words of the widest possible scope. They import such meanings as "in relation to", "with reference to" or "in connection with".** The phrase "in respect of" probably the widest of any expression intended to convey some connection between two related subject matters.
>
> See also *Paterson v Chadwick* [1974] 2 All ER 772 (QBD) at 775.
>
> [Emphasis added]

Therefore, the phrase "in connection with" is used to describe a relationship between two things, but not necessarily a causal relationship. The phrases "in connection with", "in relation to" and "in respect of" have similar meanings. These expressions are capable of having a very wide meaning. The degree of the relationship required depends on the context in which the expression is used.

In the Australian FBT context, the courts have considered that it cannot be said that any causal relationship between the benefit and the employment is a sufficient relationship for FBT purposes and that a sufficient or material rather than a causal connection or relationship between the benefit and the employment must be established: see *J & G Knowles & Associates Pty Ltd v FCT* (2000) ATC 4151. In that case, the court considered that it was helpful to consider whether the benefit is a product or incident of the employment. The Commissioner considers that this approach would also be appropriate in the New Zealand context, given that FBT was intended to apply to non-cash remuneration provided to employees.

The Commissioner considers that where the employment is a substantial reason for the provision of the benefit, there would be a sufficient relationship between the benefit and the employment (see "QB 0043: The meaning of 'benefit' for FBT purposes" (published in *Taxation Information Bulletin* Vol 18, No 2 (March 2006))).

Employer contributions

The Commissioner considers that employer contributions do not give rise to a benefit that is provided by the employer in connection with the employment of any employee. It is not possible to establish a link between a benefit arising from the payment of employer contributions and any particular employee. The reasons are as follows:

- Employees do not obtain a benefit in the form of an entitlement to receive payments made by employers under FICA. Employees have no beneficial entitlement to amounts paid by them or by their employer under FICA.
- An employee's right to receive a social security benefit is conditional on the employee satisfying the eligibility requirements in the social security legislation. When the right to receive payment from a fund is conditional, a benefit would not be provided when payment is made to the fund (*Constable v Commissioner of Taxation* 5 ATD 83). In *Constable* the taxpayer was the member of a provident fund established for the employees of the Shell group of companies. Both employer and employee contributions were paid to the fund. The fund's regulations permitted members to withdraw the amount held on their behalf if an amendment was made to the regulations that curtailed their rights. Such an amendment was made with effect from 30 September 1947. The taxpayer

withdrew amounts held to his credit (including the employer's contributions and interest earned on the amount contributed). The High Court of Australia held that these amounts did not constitute an allowance, a gratuity, compensation, a benefit, a bonus or a premium in respect of or for or in relation to the taxpayer's employment or services rendered by him. Dixon CJ and McTiernan, Williams and Fullager JJ in their joint judgment commented:

> It appears to us that the taxpayer becomes entitled to a payment out of the fund by reason of a contingency (viz an alteration of the regulations curtailing the rights of members) which occurred in the year enabling him to call for the amounts shown by his account. It was a contingent right which became absolute. The happening of the event which made it absolute did not, and could not amount to an allowing, giving or granting to him of any allowance, gratuity, compensation, benefit, bonus or premium. The fund existed as one to a share in which he had a contractual, if not a proprietary title. All that occurred in the year of income with respect to the sums in question was that the future and contingent or conditional right became [a] right to present payment and payment was made accordingly.
>
> ....
>
> It is not of course, a matter which arises for decision in the present case, but to avoid misunderstanding it is we think desirable to say that on the frame of the regulations we find it by no means easy to see how the sums so contributed can be regarded as allowed, granted or given to the employee when they are paid to the Administrators of the Fund. It is only after the Administrators have exercised their discretion that the moneys paid to the special account are reflected in the member's (employee's) account and even then that does not mean that the member becomes presently entitled to the moneys credited to that account. (pp. 95–96)

- A benefit (either in the form of a social security benefit or the right to receive a social security benefit) would not be provided when payments are made by the employer under FICA. Employees must satisfy the statutory criteria (including citizenship or residence requirements, reaching retirement age, disability, earning the minimum number of credits) before a benefit would be paid to the employees. *Fleming v Nestor* 363 US 603 confirms that a right to receive future benefits does not accrue as a consequence of payments made by the employer under FICA.
- The substantial reason for payment or the provision of retirement, disability or Medicare benefits to an employee is that the employee satisfies the statutory criteria for eligibility to receive the benefit. The amount of any benefit paid is not related to the payments made under FICA. The amount depends on a person's earnings history (whether as an employee or a self-employed person). Therefore, there is an insufficient relationship between the payment of a social security benefit and payments made by the employer under FICA.

Employee contributions

The Commissioner considers that the deduction of employee contributions from wages and the payment of such contributions under FICA also do not give rise to a benefit in connection with the employee's employment. As employee contributions form part of the salary or wages paid to employees, employee contributions are assessable income of employees in terms of section CE 1(a). That being the case, such contributions are specifically excluded from the definition of "fringe benefit" by section CX 4. In *Case 207* CTBR(NS) 91 it was accepted that deductions made under FICA from the salary paid to an Australian resident who was a visiting professor at a university in the US was assessable income of the taxpayer. The issue was whether the amount deducted under FICA was exempt income (on the basis that a liability for income tax in the US had been paid).

Summary

For there to be an FBT liability, the employer must have provided a "fringe benefit" to an employee.

- Employer contributions paid under FICA do not give rise to a "fringe benefit" under section CX 13 as the contributions are not made for the benefit of employees.
- Employer contributions paid under FICA do not give rise to a "fringe benefit" under section CX 14. As trust funds established for the purpose of paying disability benefits or Medicare and funded by payments under FICA were not established for the benefit of employees and have not been approved by the Commissioner, the funds are not "sickness, accident or death benefit funds" as defined in section YA 1.
- Employer contributions under FICA do not give rise to an "unclassified benefit" in terms of section CX 37 as a benefit is not provided by employers in connection with the employment of employees through the payment of employer contributions under FICA.
- Employee contributions do not give rise to an "unclassified benefit". Employee contributions required to be deducted from wages and paid under FICA represent part of employees' assessable income and are expressly excluded from the definition of "fringe benefit" by section CX 4.

Therefore, payments required under FICA are not subject to FBT.

LEGISLATION AND DETERMINATIONS

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

DETERMINATION DET 09/02: STANDARD-COST HOUSEHOLD SERVICE FOR CHILDCARE PROVIDERS

This determination may be cited as "Determination DET 09/02: Standard-Cost Household Service for Childcare Providers".

Explanation (which does not form part of the determination)

1. This determination sets out the standard-cost household service that has been provided as childcare services by taxpayers, who are natural persons, in their own domestic accommodation.
2. It also sets out the components of expenditure that are generally incurred in the provision of the standard-cost household service by these taxpayers.
3. This determination determines a figure for a cost or costs that for the purpose of the Tax Administration Act 1994 may be treated as being incurred by a taxpayer in deriving:
    a) exempt income; and
    b) gross income.
4. This determination also prescribes a method of calculating such a figure, as set out in paragraph 3.

Reference

5. This determination is made pursuant to section 91AA of the Tax Administration Act 1994.

Scope of determination

6. Except where its application is specifically excluded in another determination or a fresh determination pursuant to section 91AA(5) of the Tax Administration Act 1994, this determination shall apply to all natural persons who are not registered for goods and services tax purposes and who have provided childcare services in their own domestic accommodation. In addition, this determination will only apply to persons who provide childcare in accordance with the Education (Home-based Care) Order 1992 and/or the Licensing Criteria for Home-based Education and Care Services 2008.
7. This determination replaces the Commissioner's practice published in the former determination DET 001 which is withdrawn with effect from 1 April 2008. This determination shall apply to the 2009 and subsequent income years until it is replaced but will be subject to an adjustment based on the annual movement of the Consumers Price Index, as at 31 March each year.

Interpretation

8. In this determination, unless the context otherwise requires, expressions used have the same meanings as those in sections CW 61 and YA 1 of the Income Tax Act 2007 and section 91AA of the Tax Administration Act 1994—
9. "Childcare provider" means a natural person who carries on an activity of providing a standard-cost household service in their own domestic accommodation:
10. "Childcare service" means a service that is provided by a childcare provider:
11. "Consumers Price Index" means the application of the annual movement of the All Groups Consumers Price Index to the variable standard-cost component and the administration and record-keeping fixed standard-cost component, but not the domestic accommodation fixed standard-cost component, of the standard-cost household service for childcare providers:
12. "Standard-cost household service for childcare providers", in relation to any childcare service, means the standard-cost that has been determined by the Commissioner of Inland Revenue for the purpose of the Income Tax Act 2007 and the Tax Administration Act 1994:
13. "Order" means the Education (Home-based Care) Order 1992 and/or the Licensing Criteria for Home-based Education and Care Services 2008.

Determination

Provision of childcare service

14. A childcare service shall be a standard-cost household service where:
    a) the childcare provider is a natural person; and
    b) the childcare service requires the use of the childcare provider's domestic accommodation; and

c) the childcare service involves activities that commonly occur in a family household; and

d) the childcare service provided is a kind specified in the Order.

Standard-cost for childcare providers

15. Where applicable, the standard-cost for childcare providers shall be inclusive of goods and services tax ("GST"). Persons who are registered for GST may be required to make an adjustment to their GST return to the extent that they have claimed GST back on goods and services which are subsequently used in providing homeshare services, ie, as these costs would not have been incurred in the course or furtherance of their taxable activity.

16. A childcare provider who in an income year derives gross income from providing a childcare service may elect to deduct the expenditure as set out in this determination.

17. Where a childcare provider makes such an election, they shall not deduct any additional cost of providing the childcare service, if the additional cost relates to a type of expenditure that is covered in this determination.

    (a) Variable standard-cost

    Variable standard-cost shall be $3.09 per hour per child. This shall cover expenditure on items such as electricity/fuel, food, wear and tear, outings and associated transport costs, laundry, educational resources, modification costs, equipment and first aid.

    (b) Fixed standard-cost

    Fixed standard-cost shall be calculated on an annual basis and shall not vary in relation to the number of children under care. Fixed standard-cost shall comprise two categories, namely administration and record keeping, and domestic accommodation.

18. Administration and record-keeping fixed standard-cost shall be $301.00 per annum and shall include such items as the use of telephone, postage and stationery, the use of computers and other incidental administration costs.

19. The determination of domestic accommodation fixed standard-cost shall depend on whether the childcare provider owns or rents their domestic accommodation. Additionally, where the childcare provider is entitled to an accommodation supplement, the annual deduction calculated shall be reduced by the amount of the accommodation supplement received.

Childcare provider who owns their domestic property

20. Where the childcare provider owns their domestic property, the domestic accommodation fixed standard-cost shall be determined in accordance with the following formula:

$$[(a \times 5\%) - b] \times 50\% \times 33.33\%$$

where–

a is the purchase price of the domestic property; and

b is the annualised amount of accommodation supplement received by the childcare provider (ie, weekly amount received x 52 weeks); and

5% represents the expenditure normally incurred in owning a domestic property, including depreciation of the building and outgoings such as rates, insurance, mortgage interest cost; and

50% represents the usage factor that is based on usage by area such as bedrooms, kitchen, laundry, toilet/bathroom, other living areas and the use of outdoor areas pursuant to the Order; and

33.33% represents the availability factor that is based on a 7.30 am/5.30 pm drop-off/pick-up for Mondays to Fridays, and a 7.30 am/12.30 pm for Saturdays/Sundays, totalling 55 hours per week.

Childcare provider who rents their domestic property

21. Where the childcare provider rents their domestic property, the domestic accommodation fixed standard-cost shall be determined in accordance with the following formula:

$$(a - b) \times 50\% \times 33.33\%$$

where–

a is the annualised rental payment (ie, weekly rent paid x 52 weeks); and

b is the annualised amount of accommodation supplement received by the childcare provider (ie, weekly amount received x 52 weeks); and

50% represents the usage factor that is based on usage by area such as bedrooms, kitchen, laundry, toilet/bathroom, other living areas and the use of outdoor areas pursuant to the Order; and

33.33% represents the availability factor that is based on a 7.30 am/5.30 pm drop-off/pick-up for Mondays to Fridays and a 7.30 am/12.30 pm for Saturdays/Sundays, totalling 55 hours per week.

Exempt income

22. The sum of the variable standard cost and the fixed standard cost calculated in accordance with this determination, relevant to the childcare provider's circumstances, shall be treated as exempt income or expenditure incurred in providing the services.

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

This determination is signed on the 21st day of April 2009.

Rob Wells
LTS Manager, Technical Standards

COMMENTARY ON DETERMINATION DET 09/02

1. This commentary and its appendices do not form part of the determination. They are intended to provide assistance in the understanding and application of the determination.

Standard-cost basis and actual-cost basis

2. In accordance with section 91AA(3) of the Tax Administration Act 1994, a childcare provider who uses the standard-cost basis set by the Commissioner in determining their income tax liability has elected this basis to be appropriate for their circumstances.
3. A childcare provider who elects to use the standard-cost basis determined by the Commissioner must use this basis to calculate their income tax liability for the elected income year.
4. The childcare provider must adopt either the standard-cost basis or the actual-cost basis, but not both, for an income year with the exception of one-off costs actually incurred (refer to the commentary on additional costs).
5. As the use of the standard-cost basis is optional, childcare providers will not be precluded from adopting the actual-cost basis or from opting in and out of the standard-cost basis for any subsequent income year.
6. A childcare provider who does not elect to use the standard-cost basis set by the Commissioner in determining their income tax liability must use the actual-cost basis. In electing to use the actual-cost basis, the childcare provider must ensure that they have adhered to all the record-keeping requirements for verifying the costs.

Income tax implications and filing of tax returns

7. The following income tax implications apply to a childcare provider who provides childcare service and elects to use the standard-cost basis set out in the determination.
   a) Section CW 61 of the Income Tax Act 2007 will treat any income received by a childcare provider as being exempt income, to the extent to which the standard cost applies to the childcare provider's gross income.
   b) Standard-cost expenditure that exceeds payments received is not available as expenditure against other income for any income year, nor can it be carried forward to future income years.
   c) In accordance with section 33A of the Tax Administration Act 1994, a service provider would not be required to file a tax return for that income if:
      i) after deducting the amount of standard-cost under the determination, the service provider has zero income tax liability; and
      ii) the service provider did not have any other income where tax has not been deducted at source.

Consumers Price Index

8. To assist childcare providers, Inland Revenue will publish the effect of the annual movement of the All Groups Consumers Price Index as at 31 March on the variable standard-cost component and the administration and record-keeping fixed standard-cost component. The revised standard-cost components will be published in Inland Revenue's *Tax Information Bulletin* in May of each year.
9. The changes in the annual movement of the All Groups Consumers Price Index will not be applied to the domestic accommodation fixed standard-cost component. This is because the basis for this component is either historical (where a childcare provider owns their domestic accommodation) or market related (where a childcare provider rents their domestic accommodation).
10. The first such annual adjustment will be for the income year 1 April 2009–31 March 2010.

Goods and services tax (GST)

11. As the annual turnover from childcare services is expected to be well below the registration threshold for GST, it is presumed that few childcare providers will be registered for GST. Therefore, the standard-cost components determined by the Commissioner have been prepared on a GST-inclusive basis.

Purchase price of domestic property

12. The purchase price of a domestic property will include any subsequent cost of improvement to the domestic property. Childcare providers will be required to provide verification of such additional costs incurred.

Receipt of accommodation supplement by a childcare provider

13. A childcare provider may be entitled to an accommodation supplement. The Ministry of Social Development assesses each applicant's entitlement based on a set of guidelines. The assessment of entitlement takes into account such factors as accommodation costs, income and assets, family status, employment status and residential location. Where a childcare provider is entitled to an accommodation supplement, the amount of annual domestic accommodation fixed standard-cost calculated will be reduced by the annual amount of the accommodation supplement received. The examples in Appendix B illustrate how the receipt of an accommodation supplement affects the calculation of the annual domestic accommodation fixed standard-cost.

Additional costs

14. Where a childcare provider has incurred additional one-off costs, which have not been taken into account by the Commissioner in arriving at the standard-cost in the determination, such costs will be allowed as an additional deduction. The childcare provider must however demonstrate to Inland Revenue that such costs have been incurred for the childcare service they provide. An example may be expenses incurred to comply with the training requirements of the Order.

Reimbursements

15. Where a parent or guardian reimburses a childcare provider for specific costs incurred, these costs are not allowed as deductions against their gross income. For example, the childcare provider may choose to take the children in their care to the zoo as an outing, but asks the parents to pay the admission fee charged by the zoo. The money received from the parents for the admission fee to the zoo is not regarded as gross income. The admission fee to the zoo will not be allowed as a deduction to the childcare provider.

APPENDIX A

Weekly variable standard-cost items

The basis of $3.09 per child per hour has been calculated in relation to their operation on a weekly basis.

Item of expenditure	Cost ($)
Electricity/fuel	11.59
Food	17.38
Wear and tear	11.59
Outings and associated transport costs	20.86
Laundry	9.27
Educational resources	8.11
Modification costs	5.79
Equipment	6.95
First aid	1.16
Total	**92.70**
Based on 30 hours per week (rounded to the nearest cent)	**3.09**

Explanation of weekly variable standard-cost items

Electricity/fuel – This covers the use of all appliances including the cost of heating, lighting and hot water. It includes other heating fuels such as gas, wood and coal.

Food – This covers the cost of food that is supplied and includes basics such as bread, milk, fruit juice, biscuits and special dietary needs. The cost of baking involved/provided for children is also included in this figure. It also covers incidentals such as tea and coffee consumed by childcare providers and parents/guardian.

Wear and tear – These cover all related expenses and include such expenses as the cleaning of carpets, repairing/replacing furnishings (eg, rugs, linen), repairs and maintenance of equipment and appliances.

Outings and associated transport costs – These cover the costs of actual outings, such as swimming pool or other administration/user costs for a particular activity. In addition, motor vehicle costs in transporting the children to these locations and other travel costs associated with picking up from a play group/kindergarten are also included. Owning/hiring of car seats for small children under the age of five is also a statutory requirement and is therefore included in this component. As mentioned in paragraph 15 of the determination, the costs covered by parent contributions are not allowed as deductions against the caregivers gross income, and the contributions from parents are not regarded as income.

Laundry – This not only covers obvious cleaning and laundry products but also rubber gloves, wet wipes, toilet paper and other similar items.

Educational resources – These cover all related expenses and include items such as paper, paints, crayons, books, and other stationery items.

Modification costs – The Order sets out the minimum requirements for caregivers to be eligible to provide childcare. These include fencing, fireguards, window locks, and other safety features and cover the initial cost plus ongoing costs necessary to comply with the required standard.

Equipment – This covers the cost of providing indoor and outdoor equipment, such as video tapes, swings, puzzles and games.

First aid – This covers the requirement to have a first aid cabinet equipped to the standard set by the Ministry of Health/District Health Boards.

APPENDIX B

Application of the standard-cost basis as determined by the Commissioner for childcare providers

(Note: All calculations are rounded to the nearest dollar.)

Example 1

A childcare provider owns a domestic property. The purchase price of the domestic property is $200,000. The childcare provider receives an accommodation supplement of $10 per week based on the location of the domestic property and their individual circumstances. Therefore, the domestic accommodation fixed standard-cost that the childcare provider may elect to deduct per annum is:

[($200,000 × 5%) – ($10 × 52)] × 50% × 33.33% = $1,580.00

Example 2

A childcare provider rents a domestic property. The rent is $200 per week. The childcare provider receives an accommodation supplement of $20 per week based on the location of the domestic accommodation and their individual circumstances. Therefore, the domestic accommodation fixed standard-cost that the childcare provider may elect to deduct per annum is:

[($200 × 52) – ($20 × 52)] × 50% × 33.33% = $1,560.00

Example 3

A childcare provider owns a domestic property, which costs $200,000. The childcare provider receives an accommodation supplement of $10 per week based on the location of the domestic property and their individual circumstances.

The childcare provider provided care for several children in the income year for a total of 1,250 hours. The childcare provider charged an hourly rate of $4.00 and elected to use the standard-cost basis in accordance with Determination DET 09/02: *Standard-cost household service for childcare providers*.

The childcare provider's income tax liability is calculated as follows:

Income	1,250 hours × $4.00	$5,000.00
Less: Variable standard-cost	1,250 hours × $3.09	$3,863.00
		$1,137.00
Less: Fixed standard-cost Domestic accommodation as per Example 1 Administration and record keeping	$1,580.00 $301.00	$1,881.00
		($744.00)
Taxable income		nil

Example 4

A childcare provider rents a domestic property for $200 per week. The childcare provider receives an accommodation supplement of $20 per week based on the location of the domestic accommodation and their individual circumstances.

The childcare provider provided care for several children in the income year for a total of 1,250 hours. The childcare provider charged an hourly rate of $4.00 and elected to use the standard-cost basis in accordance with Determination DET 09/02: *Standard-cost household service for childcare providers*.

The childcare provider's income tax liability is calculated as follows:

Income	1,250 hours × $4.00	$5,000.00
Less: Variable standard-cost	1,250 hours × $3.09	$3,863.00
		$1,137.00
Less: Fixed standard-cost Domestic accommodation as per Example 2 Administration and record keeping	$1,560.00 $301.00	$1,861.00
		($724.00)
Taxable income		nil

Example 5

A childcare provider owns a domestic property, which costs $250,000 and receives no accommodation supplement.

The childcare provider provided care for several children in the income year for a total of 3,120 hours. The childcare provider charged an hourly rate of $4.00 and elected to use the standard-cost basis in accordance with Determination DET 09/02: *Standard-cost household service for childcare providers.*

The childcare provider's income tax liability is calculated as follows:

Income	3,120 hours × $4.00	$12,480.00
Less: Variable standard-cost	3,120 hours × $3.09	$9,641.00
		$2,839.00
Less: Fixed standard-cost Domestic accommodation [($250,000 × 5%) − $0] × 50% × 33.33%	$2,083.00	
Administration and record keeping	$301.00	$2,384.00
Taxable income		$455.00

Example 6

A childcare provider rents a domestic property for $210 per week and receives no accommodation supplement.

The childcare provider provided care for several children in the income year for a total of 3,120 hours. The childcare provider charged an hourly rate of $4.00 and elected to use the standard-cost basis in accordance with Determination DET 09/02: *Standard-cost household service for childcare providers*.

The childcare provider's income tax liability is calculated as follows:

Income	3,120 hours × $4.00	$12,480.00
Less: Variable standard-cost	3,120 hours × $3.09	$9,641.00
		$2,839.00
Less: Fixed standard-cost Domestic accommodation [($210 × 52) − 0] × 50% × 33.33%	$1,820.00	
Administration and record keeping	$301.00	$2,121.00
Taxable income		$718.00

DETERMINATION FDR 2009/1: A TYPE OF ATTRIBUTING INTEREST IN A FOREIGN INVESTMENT FUND FOR WHICH A PERSON MAY NOT USE THE FAIR DIVIDEND RATE METHOD (AMP FUTURE DIRECTIONS INTERNATIONAL BOND FUND)

Reference

This determination is made under section 91AAO(1)(b) of the Tax Administration Act 1994. This power has been delegated by the Commissioner of Inland Revenue to the position of Policy Manager, Policy Advice Division, under section 7 of the Tax Administration Act 1994.

Discussion (which does not form part of the determination)

Units in the non-resident issuer to which this determination applies (the AMP Future Directions International Bond Fund – "the Fund") are an attributing interest in a foreign investment fund ("FIF") for New Zealand resident investors. New Zealand resident investors are required to apply the FIF rules to determine their tax liability in respect of their units in the non-resident issuer each year.

The Fund invests predominantly in financial arrangements (at least 80% of the investment mix) comprising government, government-guaranteed and high-grade corporate bonds and securities in countries around the world. Up to 20% of the Fund may be invested in other asset classes (such as shares) with the objective of seeking opportunities to benefit from any above market performance generated by the underlying investment managers in such other asset classes. Consequently, the Fund will use derivatives to offset the exposure to such other asset classes, other than the exposure to the under or over performance of the underlying investment managers. The Fund is available either hedged to Australian dollars or unhedged.

The AMP Capital Hedged Global Fixed Interest Fund ("the AIF Q Fund"), which is resident in New Zealand, invests in the unhedged Fund and aims to be fully hedged to the New Zealand dollar by entering into appropriate currency hedge positions, which are financial arrangements separate from the units that the AIF Q Fund holds in the Fund.

Because the Fund does not have New Zealand dollar hedging arrangements and the AIF Q Fund enters into its own New Zealand dollar hedging arrangements, section EX 40(9)(d) of the Income Tax Act 2004 (taking into account the amendments made to that provision by the Taxation (Business Taxation and Remedial Matters) Act 2007) and section EX 46(10)(c) of the Income Tax Act 2007 do not exclude the AIF Q Fund from using the fair dividend rate ("FDR") method to determine its tax liability in respect of the units it holds in the Fund under the FIF rules.

However, the AIF Q Fund's hedging strategy ensures that its investment in the Fund is economically equivalent to a loan denominated in New Zealand dollars.

The policy intention is that the AIF Q Fund's investment in the Fund should not qualify for the FDR method as the AIF Q Fund's investment is akin to a New Zealand dollar denominated debt investment having regard to the nature of the Fund's investments and the AIF Q Fund's hedging position. However, in the absence of this determination, the AIF Q Fund could choose to use the FDR method for the 2007–2008 and subsequent income years. This result is inconsistent with the policy intention of the FIF rules.

I consider that it is appropriate for the AIF Q Fund to be excluded from using the FDR method in respect of its investment in the Fund for the 2007–08 and subsequent income years. The overall arrangement (as described to me by the applicant) consists predominantly of investments in debt securities and is sufficiently hedged so that it is akin to a New Zealand dollar denominated debt investment. Accordingly, it is appropriate that the FDR method not be used by the AIF Q Fund or other similarly hedged New Zealand resident investors in respect of investments in the Fund.

Scope of determination

The investments that this determination applies are units in the unhedged AMP Future Directions International Bond Fund, a unit trust established in Australia ("the Fund").

The Fund:

- is resident in Australia for tax purposes;
- invests predominantly (80% or more of total net assets) in fixed interest securities in countries around the world, including government and government-guaranteed securities, corporate securities, asset-backed securities and hybrid securities (such as convertible notes);
- can invest in other asset classes (such as shares) but the net exposure (including any derivatives used to offset the market exposure, that is, the exposure other than the under or over performance of the underlying investment managers) to such asset classes shall not exceed 5% of the value of the Fund;

- has a target tracking error measured against a performance benchmark of the Barclays Capital Global Aggregate Index.

Interpretation

In this determination:

"Financial arrangement" means financial arrangement under section EW 3 of the Act;

"Non-resident" means a person that is not resident in New Zealand for the purposes of the Act;

"The Act" means the Income Tax Act 2004 or the Income Tax Act 2007, as applicable;

"Target tracking error" means the Fund's target tracking error agreed with and disclosed, prior to this determination, to the Policy Manager, Inland Revenue who makes this determination.

Determination

An attributing interest in a FIF to which this determination applies is a type of attributing interest for which a person may not use the FDR method to calculate FIF income from the attributing interest, if the person fully hedges (on a pre-tax basis, plus or minus 10%) the interest back to the New Zealand dollar.

Application date

This determination applies for the 2007–2008 and subsequent income years. However, under section 91AAO(3B) of the Tax Administration Act 1994, this determination does not apply for an income year beginning before the date of this determination for an investor in the Fund unless that investor chooses for this determination to apply for that year.

Dated at Wellington this 8th day of May 2009.

David Carrigan
Policy Manager, Inland Revenue

DETERMINATION FDR 2009/2: A TYPE OF ATTRIBUTING INTEREST IN A FOREIGN INVESTMENT FUND FOR WHICH A PERSON MAY NOT USE THE FAIR DIVIDEND RATE METHOD (PIMCO WHOLESALE GLOBAL BOND FUND)

Reference

This determination is made under section 91AAO(1)(b) of the Tax Administration Act 1994.

This power has been delegated by the Commissioner of Inland Revenue to the position of Policy Manager, Policy Advice Division, under section 7 of the Tax Administration Act 1994.

Discussion (which does not form part of the determination)

Units in the EQT PIMCO Wholesale Global Bond Fund (PIMCO) to which this determination applies are an attributing interest in a foreign investment fund (FIF) for New Zealand resident investors.

New Zealand resident investors are required to apply the FIF rules to determine their tax liability in respect of their investment in units in PIMCO each year.

PIMCO invests in global fixed interest securities for which PIMCO has made foreign currency hedging arrangements to provide investors with an Australian dollar denominated return on these debt instruments. Section EX 46(10)(c) of the Income Tax Act 2007 ("the Act") would apply to prevent the use of the fair dividend rate (FDR) method if the foreign currency hedging arrangements were made to provide a New Zealand dollar denominated return on these financial arrangements.

Instead of PIMCO undertaking New Zealand dollar currency hedging arrangements New Zealand resident investors can enter into separate foreign currency hedging arrangements to provide a New Zealand dollar equivalent return when the two arrangements, being the investment in PIMCO and the currency hedge, are considered as a single arrangement.

The policy intention is that the FDR method of calculating FIF income should not be applied to investments that provide a New Zealand resident investor with a return similar to a New Zealand dollar denominated debt investment. It is appropriate for the Commissioner to take into account the whole of the arrangement, including any interposed entities or financial arrangements, in ascertaining whether an investment in a FIF provides the New Zealand resident investor with a return akin to New Zealand dollar denominated debt investment.

On this basis where the New Zealand resident investor undertakes New Zealand dollar currency hedging arrangements to at least 80% of the value of their interest in PIMCO, I consider that it is appropriate for the investment in PIMCO to be excluded from using the FDR method for the 2008–2009 and subsequent income years.

Scope of determination

This determination applies to an attributing interest in a FIF held by New Zealand resident investors in a non-resident issuer where:

1. The non-resident issuer:
    a) is an Australian unit trust established on 31 July 1998;
    b) is known as the EQT PIMCO Wholesale Global Bond Fund;
    c) issues units denominated in Australian dollars;
    d) invests predominately in investment grade global fixed interest securities;
    e) enters into foreign currency hedging arrangements to provide a return similar to Australian dollar denominated debt instruments;
2. In respect of the EQT PIMCO Wholesale Global Bond Fund:
    a) the volatility risk level of the non-resident issuer is represented to investors as low to medium;
    b) the average tracking error of the non-resident issuer as measured against the benchmark index is below the level agreed with and disclosed before this determination is made to the Policy Manager, Inland Revenue who makes this determination;
    c) the non-resident issuer does not adopt a target tracking error above the target percentage agreed with and disclosed before this determination is made to the Policy Manager, Inland Revenue who makes this determination; and
3. The New Zealand resident investor undertakes New Zealand dollar currency hedging arrangements to at least 80% of the value of their interest in the non-resident issuer.

Interpretation

In this determination unless the context otherwise requires:

"Benchmark Index" means the Lehman Brothers Global Aggregate Bond Index hedged to the Australian dollar, or a replacement index with substantially the same features;

"Financial arrangement" means financial arrangement under section EW 3 of the Act;

"Non-resident" means a person that is not resident in New Zealand for the purposes of the Act;

"The Act" means the Income Tax Act 2007.

Determination

An attributing interest in a FIF to which this determination applies is a type of attributing interest for which a person may not use the fair dividend rate method to calculate FIF income from the interest.

Application date

This determination applies for the 2008–2009 and subsequent income years. However, under section 91AAO(3B) of the Tax Administration Act 1994, this determination does not apply for an income year beginning before the date of this determination for an investor in PIMCO unless that investor chooses for this determination to apply for that year.

Dated at Wellington this 11th day of May 2009.

David Carrigan
Policy Manager, Inland Revenue

CPI ADJUSTMENT – CPI 09/01 FOR DETERMINATION DET 05/03: STANDARD-COST HOUSEHOLD SERVICE FOR BOARDING SERVICE PROVIDERS

In accordance with the provisions of Determination DET 05/03, as published in *Tax Information Bulletin* Vol 17, No 10 (December 2005), Inland Revenue advises that the weekly standard-cost component for the 2009 income year, is retrospectively adjusted as follows:

a) The weekly standard-cost for one to two boarders will increase from $220 each to $227 each.

b) The weekly standard-cost for third and subsequent number of boarders will increase from $179 each to $185 each.

The above amounts have been adjusted in accordance with the annual movement of the All Groups Consumers Price Index for the twelve months to March 2009, which showed an increase of 3.0%. For boarding service providers who have a standard 31 March balance date, the new amounts apply for the period from 1 April 2008 to 31 March 2009.

NATIONAL AVERAGE MARKET VALUES OF SPECIFIED LIVESTOCK DETERMINATION 2009

This determination may be cited as "The National Average Market Values of Specified Livestock Determination, 2009".

This determination is made in terms of section EC 15 of the Income Tax Act 2007 and shall apply to specified livestock on hand at the end of the 2008–2009 income year.

For the purposes of section EC 15 of the Income Tax Act 2007 the national average market values of specified livestock, for the 2008–2009 income year, are as set out in the following table.

Type of livestock	Classes of livestock	Average market value per head $
Sheep	Ewe hoggets	94.00
	Ram and wether hoggets	88.00
	Two-tooth ewes	116.00
	Mixed-age ewes (rising three-year and four-year old ewes)	99.00
	Rising five-year and older ewes	81.00
	Mixed-age wethers	56.00
	Breeding rams	218.00
Beef cattle	*Beef breeds and beef crosses*:	
	Rising one-year heifers	429.00
	Rising two-year heifers	663.00
	Mixed-age cows	770.00
	Rising one-year steers and bulls	534.00
	Rising two-year steers and bulls	748.00
	Rising three-year and older steers and bulls	908.00
	Breeding bulls	1743.00
Dairy cattle	*Friesian and related breeds:*	
	Rising one-year heifers	511.00
	Rising two-year heifers	1083.00
	Mixed-age cows	1312.00
	Rising one-year steers and bulls	381.00
	Rising two-year steers and bulls	576.00
	Rising three-year and older steers and bulls	724.00
	Breeding bulls	1220.00
	Jersey and other dairy cattle:	
	Rising one-year heifers	434.00
	Rising two-year heifers	953.00
	Mixed-age cows	1243.00
	Rising one-year steers and bulls	322.00
	Rising two-year and older steers and bulls	577.00
	Breeding bulls	998.00
Deer	*Red deer:*	
	Rising one-year hinds	272.00
	Rising two-year hinds	460.00
	Mixed-age hinds	514.00
	Rising one-year stags	318.00
	Rising two-year and older stags (non-breeding)	530.00
	Breeding stags	1393.00
	Wapiti, elk and related crossbreeds:	
	Rising one-year hinds	318.00
	Rising two-year hinds	484.00
	Mixed-age hinds	551.00
	Rising one-year stags	366.00
	Rising two-year and older stags (non-breeding)	574.00
	Breeding stags	1678.00
	Other breeds:	
	Rising one-year hinds	80.00
	Rising two-year hinds	122.00
	Mixed-age hinds	153.00
	Rising one-year stags	85.00
	Rising two-year and older stags (non-breeding)	152.00
	Breeding stags	340.00
Goats	*Angora and angora crosses (mohair producing):*	
	Rising one-year does	20.00
	Mixed-age does	25.00
	Rising one-year bucks (non-breeding)/wethers	10.00
	Bucks (non-breeding)/wethers over one year	12.00
	Breeding bucks	64.00
	Other fibre and meat producing goats (Cashmere or Cashgora producing):	
	Rising one-year does	28.00
	Mixed-age does	29.00
	Rising one-year bucks (non-breeding)/wethers	23.00
	Bucks (non-breeding)/wethers over one year	18.00
	Breeding bucks	168.00
	Milking (dairy) goats:	
	Rising one-year does	180.00
	Does over one year	260.00
	Breeding bucks	350.00
	Other dairy goats	50.00
Pigs	Breeding sows less than one year of age	154.00
	Breeding sows over one year	179.00
	Breeding boars	190.00
	Weaners less than 10 weeks of age (excluding sucklings)	52.00
	Growing pigs 10 to 17 weeks of age (porkers and baconers)	87.00
	Growing pigs over 17 weeks of age (baconers)	126.00

This determination is signed by me on the 15th day of May 2009.

Susan Price
Director, Public Rulings

LEGAL DECISIONS – CASE NOTES

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

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

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.

TRA ALLOWS DEDUCTION FOR GST INPUT TAX ON LEGAL SERVICES PROVIDED IN TRUSTS

Case	TRA Decision Number 06/2009; TRA 67/05 and 70/05
Decision date	27 February 2009
Act	Goods and Services Tax Act 1985 ("GST Act) and the Tax Administration Act 1994 (TAA)
Keywords	Section 3A principle purpose, legal services, taxable activity

Summary

The trustees claimed various invoice trust deductions for input tax on legal fees arising from litigation between the trustees and beneficiaries. The question was whether these services were acquired for the principle purpose of the trust's taxable activity.

Impact of decision

Trustees can claim a deduction for legal fees on a GST input return basis through the trust when the trust is carrying out a taxable activity even if the fees are paid for by a third party. In the absence of an exempt supply or criminal charges outside the scope of normal business activity, GST input tax on legal fees which are incurred in the course or furtherance of a GST registered person's taxable activity will be deductible in full.

Facts

This proceeding involved two disputant trusts who are acting in a type of representative capacity as part of a complex structure of family trusts all having similar claims. The cases of the other trusts have been stayed pending the outcome of this case.

The disputant trusts claimed deductions of GST input tax for legal fees associated with extensive trust litigation. The trust litigation came about due to a dispute between family members. The dispute involved the removal of trustees of various trusts ("breach of trust proceedings").

The Commissioner disallowed the disputant trusts' GST deductions on the basis that the legal services were not acquired for the principle purpose of making taxable supplies. Also the invoices were not issued to any particular trust nor were they valid "tax invoices" for GST purposes.

Decision

Whether legal services were acquired by the disputant trusts?

The disputant trusts engaged professional legal providers to assist them in defending the breach of trust proceedings. The family trusts (through their trustees) had a legal obligation to pay the legal service providers.

The fact that the legal fees may have been indirectly funded at times by a third party is of no relevance to the GST position in terms of an input tax claim, the GST-registered person has the contractual liability to pay for the relevant supply of legal and other services.

The fact that the majority of the invoices produced during the proceedings were addressed to "The trustees of the Trust" globally is of no relevance.

A GST-registered person will be in the GST tax base and eligible to claim all GST input tax on costs charged to it, unless the trust is making exempt supplies and those costs can be shown to be referable to those exempt supplies.

In the absence of a clear disqualifying feature like an exempt supply or criminal charges outside the scope of normal business activity, GST input tax on legal fees which are incurred in the course or furtherance of a GST registered person's taxable activity will be deductible in full; as they must be to avoid that person being a consumer.

Whether a taxable activity was carried on by the disputant trusts, and were legal costs acquired in the course of furtherance of that activity?

The disputant trusts were carrying on a "taxable activity" at the time the relevant legal services were acquired.

In the case of the first disputant trust, it carried on the activities of leasing its land to a winery for viticulture purposes and the balance of its land was used for cattle and sheep grazing, breeding and fattening. Financial statements for the trust record the rent being paid. The share of GST input tax incurred on the legal services was "an ordinary incident of administration of the trust" and proper and reasonable cost for the trust to incur (*Variety Leisure, Bayly* and *Case R38*).

In the case of the second disputant trust, it provided bailment services and performed other bailment activities. This trust owned a large amount of livestock and the bailment activity per se was an economic activity and not a hobby. While there was no formal bailment arrangement, the arrangements operated in practice for some time. The fact that a third party provided staff from time-to-time to assist with the running of the trust's farming/economic activities would not alter this conclusion as many farming arrangements, particularly on this scale, often involve shared and informal arrangements. Bailment rental was received by the trust in the relevant GST periods, bailment rental calculations are recorded, as well.

The fact that the trust also had a shareholding in a farming station company did not alter the fact that a taxable activity was being conducted by it. The farming is incidental to the principal taxable activity being carried on. The legal costs incurred were proper and reasonable ones and an incidence of ordinary trust management and administration.

Whether any legal services were acquired for the principal purpose of making taxable supplies?

The legal services acquired were no different conceptually from the costs or valuation and accounting and consulting services which each of the disputant trusts acquired in the same GST periods.

The key point in solving this issue is to determine what effect the legal services had on the making of taxable supplies by the disputant trusts. The Authority understood that unless the litigation was resolved, the respective taxable activities of the disputant trusts were likely to collapse or, at least, be affected adversely in terms of good trading relations.

The pro-rating system used by the trustees to allocate legal and other costs to each of the disputant trusts was a reasonable and fair thing to do as all the trusts were embroiled in the breach of trust proceedings.

The legal costs charged to the disputant trusts came essentially from one legal service provider. An analysis of the relevant invoices discloses a range of entirely orthodox and general legal costs associated with a breach of trust proceedings.

There is no question that the legal costs incurred in the relevant GST periods related to the defence of the breach of trust proceedings. That is to do with management of the trust and its activity.

Evidence confirmed that claims arising from the breach of trust proceedings against the disputant trusts were designed to protect the income-earning capacity of the disputant trusts, and to protect their capital. The trustees of the family trusts affected by the breach of trust proceedings had to defend allegations of a breach of trust against them. The trustees would have been in breach of trust in not defending the claims.

It is well-established that where a trustee's conduct in terms of a trust is challenged by beneficiaries alleging breach of trust and the trustee incurs legal cost in defending those allegations, the incurring of those costs is a normal incident of the administration of the trust.

If GST input tax is not allowed to each of the trusts as GST-registered persons, they will effectively be consumers for GST purposes, and would bear the actual GST cost charged to them by legal service providers. That seems contrary to the scheme and purpose of the Act. Even if either trust never made a taxable output again, the GST charged to it should be an input because, until the trust exits the GST tax-base, any inability to recover the GST charged to it will always leave it in a position of economic loss. That would not fairly reflect the value-added position of that trust in carrying on a taxable activity.

Are the tax invoices adequate?

The Authority has considered that on a sensible commercial practice basis, the invoices for legal services held by the trusts in the relevant GST periods satisfied all the necessary statutory requirements to support the deductions of GST input tax in terms of section 20(2) of the GST Act. The relevant invoices from the main legal service provider and other services providers constituted tax invoices for the purposes of section 24(3) of the GST Act. Consequently even in the absence of a valid tax invoice, it would be impractical in a dispute of this type to require anything more.

Conclusion

- The Authority understood the Commissioner acted incorrectly in disallowing the GST input tax claimed by the disputant trusts on the legal services charged to them in the particular GST periods;
- that the disputant trusts acquired legal services for the principal purpose of making taxable supplies;
- that the invoices held by the disputant trusts, in respect of the disallowed legal and other services provided to them, constitute valid tax invoices allowing a deduction of GST input tax under section 20(3)(a) of the GST Act.

INTERLOCUTORY APPLICATION FOR STAY OF LIQUIDATION PROCEEDINGS PENDING JUDICIAL REVIEW DISMISSAL

Case	Berrytime Land Limited and Berrytime Limited v Commissioner of Inland Revenue
Decision date	20 April 2009
Act	Judicature Amendment Act 1972, Tax Administration Act 1994
Keywords	"Exceptional circumstances" warranting judicial review

Summary

The High Court dismissed the application for a stay on the basis that the taxpayer's case for establishing "exceptional circumstances" required for judicial review was not strong.

Impact of decision

The High Court confirmed that judicial review proceedings cannot be used except in exceptional circumstances.

Facts

1. Berrytime and Berrytime Land filed GST self-assessments totalling $3,365,134.54 (for Berrytime) and $808,924.32 (for Berrytime Land). Apart from one payment of $246,914.63 on behalf of Berrytime Land, none of the assessed GST has been paid resulting in penalties and interest being added to the liability.

2. By a letter dated 16 June 2008, Berrytime claimed it had made errors in the GST returns. Berrytime proposed amendments be made to reduce their liability by $1,883,169.11. The letter requested new assessments be issued. The Commissioner treated this letter as a request for the exercise of the Commissioner's discretion under section 113 of the Tax Administration Act 1994 (TAA) as Berrytime was out of time to file a NOPA. However, the request was ultimately declined on 11 September 2008 due to a lack of documentary support.

3. The Commissioner filed proceedings to wind up both companies on 22 September 2008, on the grounds of persistent and/or serious failures to comply with the Companies Act, and that winding up was just and equitable. Amended statements of claim were filed on 10 October 2008. Liquidation was sought on the basis of the companies' inability to pay their debts, in addition to the grounds set out in the original statement of claim.

4. A second request for amendment of the GST assessments was made by the companies' in a letter dated 23 January 2009. Amendments were sought pursuant to section 113 for both Berrytime and for Berrytime Land. No supporting documentation was attached.

5. In a meeting held on 4 February 2009 between the Commissioner and the representatives for the companies, the Commissioner requested the companies provide information to support their position. In a follow-up letter dated 13 February 2009, the Commissioner requested this be provided by 27 February 2009 and advised that if significant progress could not be made over the following few weeks, the Commissioner would not seek an adjournment of the liquidation proceedings.

6. Nothing was received by 27 February 2009 and the Commissioner requested an update on 2 March 2009. On 3 March 2009, the companies advised that an update was forthcoming. On 10 March 2009, the Commissioner advised that if the information was not received by 13 March 2009, he would have no option but to decline the application.

7. On 13 March 2009, the Commissioner was provided with a number of documents. However, he considered that they did not support their position as set out in the letter dated 23 January 2009. Accordingly, the application was declined on 18 March 2009.

8. On 25 March 2009, the day before the liquidation hearing was due to proceed, the companies' filed an application for judicial review and an interlocutory application for interim orders staying the liquidation proceedings pending the outcome of the judicial review application.

9. The liquidation proceedings were heard the following day and the companies argued that the Commissioner should have amended the self-assessments. In his reserved judgment, issued on 3 April 2009, Doogue AJ concluded that both companies are insolvent. However, rather than make orders placing the companies in liquidation, he adjourned the proceedings until 7 April 2009, noting that if the companies had not made payment, then certificates of unpaid debt would be required. On 7 April 2009 the liquidation proceedings were further adjourned until 22 April 2009, pending the outcome of the interlocutory application.

10. In this interlocutory application, the companies argued that the decision of the Commissioner was communicated with insufficient notice and without providing opportunity to comment prior to the liquidation proceedings. The companies also argued that the Commissioner had made a mistake of fact in considering that the self-assessments were correct and had not taken relevant considerations into account. Further, it was made in breach of the Commissioner's duties and obligations under the TAA and SPS 07/03 and that the decision was unreasonable in light of the large amount of information requested and provided, that the information raised questions about the correctness of the self-assessments, and that the Commissioner was unreasonable in not taking account of evidence provided.

Decision

Are interim orders necessary to preserve the taxpayers' position?

11. The companies submitted that orders were necessary because if the companies were placed in liquidation, they would not have the opportunity to pursue the judicial review proceedings. The Commissioner disagreed on the basis that judicial review proceedings could be continued by a liquidator.

12. Andrews J accepted that it would be the companies' preference to pursue the judicial review proceedings themselves, rather than leave them in the hands of a liquidator and accepted there was some force in the argument that once in place, liquidation would be difficult to "unwind" should the outcome of judicial review lead to a reduction of the liability. Accordingly, her Honour concluded that interim orders may be necessary to preserve the companies' position.

Are interim orders justified taking into account all relevant factors?

13. It was accepted by the parties that the correctness of a tax assessment can only be challenged by way of the procedures set out in the TAA and that challenge by way of judicial review will be available only in "exceptional circumstances".

14. Andrews J held, after considering these factors, that the applications by the companies should be dismissed

15. In particular, her Honour held that the fact that the companies "were committed" to ensuring that the correct tax position was represented, and that "extraordinary efforts" had been taken to meet requests were not relevant in the light of a taxpayer's obligations under section 15B of the TAA as the companies were required to provide information and to cooperate.

16. The companies also submitted that there had been a "conscious mal-administration" in that the Commissioner had allowed himself only two hours to review the material provided on 13 March 2009 before determining that there was insufficient evidence to support the request for amendment.

17. However, evidence showed that the material was reviewed over three days. In any event, the history of contact between the parties, the failure of the companies to provide supporting documentation with their two requests for assessment, and the repeated requests by the Commissioner for information supporting the requests showed that considerable opportunity had been given to the companies to provide information. This evidenced that the Commissioner had acted lawfully and properly in dealing with the companies, and was not in breach of any of its obligations and duties under the TAA.

18. The companies also alleged that there had been an abuse of power by the Commissioner on the basis that the section 113 amendment request was rushed through so as to progress the liquidation proceedings, enabling the Commissioner to access a wealthy shareholder. Her Honour could find no grounds for establishing such a motive.

19. Andrews J concluded that the case for establishing exceptional circumstances required for establishing judicial review proceedings was not strong but rather could "only be described as weak".

20. With regard to the public interest, Andrews J accepted that in light of her finding above regarding the weakness of the case, the balance of requiring the public interest in the Commissioner being able to carry out his statutory duties against the likelihood of the companies' succeeding in their judicial review proceedings fell on the side of not preventing the Commissioner from carrying out his statutory duties and obligations or from continuing the liquidation proceedings.

21. As for the public and private repercussions of granting orders, while the Commissioner alleged that the court has no jurisdiction to stay itself, Andrews J accepted that section 8 of the Judicature Amendment Act 1972 gives clear statutory authority to stay any proceedings that are in connection with any matter to which the application for review relates. However, her Honour noted that this does not assist in considering whether an application for interim orders should be granted.

EXPENDITURE MUST BE SIGNIFICANTLY IN CONNECTION WITH DETERMINATION OF ASSESSABLE INCOME

Case	TRA Decision Number 08/2009, TRA Number 023/2007
Decision date	20 April 2009
Act	Income Tax Act 1994
Keywords	Deduction, income tax, expenditure

Summary

Taxpayer failed to establish that expenditure incurred was *significantly* in connection with her determined assessable income and therefore were non-deductible under section DJ(5)(a).

Impact of decision

This decision provides guidance on how section DJ(5)(a) should be interpreted.

Facts

1. This supplementary decision was issued pursuant to the "leave reserved" by Barber DCJ in his substantive decision issued on 14 January 2009.

2. The substantive decision dealt with the disputant's challenge of the defendant's assessment of her income tax liability in the 2004 income tax year over the aspect of conversion of her income from social welfare benefits to ACC earnings related compensation, and receipt of residual backdated ACC lump sums.

3. In his substantive decision, Barber DCJ, in relation to the deduction claimed for expenses incurred by the disputant in pursuing the issue, held the disputant had failed to establish that any expenditure was incurred by the disputant in the 2004 income tax year. Barber DCJ reserved leave for the disputant to provide further evidence in order to claim deductions.

4. As a consequence of Barber DCJ reserving leave, the disputant applied for reimbursement of expenses. In her application, the disputant outlined the various Review Hearings she had brought against ACC in July 2003, August 2003, and February 2004.

5. The disputant generally focussed on reasons for reimbursement of expenses totalling $3,706. The expenses claimed involved computer repairs in 2008 and 2009, postages over the years 2005 to 2009, photocopying over the years 2007 to 2009, obtaining copies of case law in 2005, inkjets over 2005 to 2008, and Court fees paid in 2005 and 2009.

Decision

6. Barber DCJ stated that the authority can only make a decision in respect of the deduction of expenditure for the 2004 income year. He found that no deduction was available to the disputant, because she had not discharged the onus on her to establish that any expenditure incurred in the 2004 income year was *principally*, if not *exclusively*, in connection with the determined assessable income. He suggested that it may be more appropriate to express the threshold as requiring expenditure to be *significantly* in connection with the determined assessable income but found that the taxpayer also failed to establish that.

7. Barber DCJ agreed with the Commissioner that the expenses and disbursements referred to by the disputant are not deductible in the 2004 income year because they were not incurred in that year, do not relate to that year, and do not satisfy the test of deductibility provided for in section DJ5(1)(a) of the Income Tax Act 1994.

8. Barber DCJ went on to say that the claimed expenditure did not have the necessary nexus with the determination of the disputant's assessable income. The expenditure is related to the disputant's successful efforts to be covered by ACC and receive ACC entitlements; not to determining her assessable income. She unsuccessfully sought costs from ACC Reviewers.

9. Barber DCJ noted that there could have been expenditure incurred by the disputant which may be deductible and reserved leave for the disputant to adduce clear evidence of that expenditure and its character and purpose.

SCOPE OF JUDICIAL REVIEW LIMITED IN TAX CASES

Case	Westpac v Commissioner of Inland Revenue
Decision date	08 April 2009
Act	Judicature Amendment Act 1972
Keywords	Judicial review, assessments, inconsistency

Summary

The Supreme Court declined the taxpayer's application for appeal to appeal the Court of Appeal's judgment limiting the scope of judicial review against the Commissioner.

Impact of Decision

The strict judgment by the Court of Appeal is the most recent statement of law on judicial review and the Commissioner. The approach taken by the Court of Appeal was considered not to be reasonably arguable to be wrong by the Supreme Court. This endorses the view taken at the Court of Appeal.

Facts

This was a part of the structured finance litigation.

The taxpayer had challenged the Commissioner's assessments based upon tax avoidance

One of the causes of action in the taxpayer's case was that the assessments were invalid because these were inconsistent with an earlier binding ruling (but not for the transactions upon which the assessments were based) and for other reasons. This cause of action was subject to a strike out application by the Commissioner on the basis it could never succeed.

The Commissioner was successful at the High Court (reported (2008) 23 NZTC 21,694) and the Court of Appeal (reported [2009] NZCA 24).

The taxpayer sought leave to appeal to the Supreme Court.

Decision

In a very short judgment the Supreme Court declined to grant leave to the taxpayer.

The Court considered "that it is not reasonably arguable that the Court of Appeal's approach to the law, including its view of the effect of the policy of the legislation, was wrong" (at par [4]).

The Supreme Court summarised the Court of Appeal's approach as:

> "In its judgment, the Court of Appeal took the view that established principles in relation to applications for judicial review in tax cases should not be widened. Review was available for assessments that were not truly assessments at all and, in exceptional cases, which might have involved maladministration, the Court reached this decision notwithstanding provisions in tax administration legislation concerning functions and duties of the Commissioner, including protection of the integrity of the tax system on which the applicant relied." (at par [2])

The Supreme Court noted the fact there were different views within Inland Revenue in respect of the assessments made was not, in the circumstances, a basis for a reasonable prospect of success in judicial review (at par [5]).

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