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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 6140

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

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

Ref	Draft type/title	Description/background information	Comment deadline
ED0135	Draft determination: Remedial matters relating to the depreciation of buildings	As a result of the Taxation (Budget Measures) Act 2010 and the issue of interpretation statement IS 10/02: Meaning of "building" in the depreciation provisions, the Commissioner proposes to amend a number of the general asset classes in the "Building and structures" asset category and the "Contractors, builders and quarrying" industry category.	30 September 2011
ED0136	Draft general depreciation determination: Residential rental property chattels	This draft general depreciation determination proposes to replace all asset classes in the "Residential Rental Property Chattels" industry category with a new list.	5 October 2011

Correction – to TIB Vol 23, No 1 (February 2011)

Under "Remedial items" in the commentary for "Consequential R&D amendments", the first bullet point in Example 2 on page 85 should read: "It may treat the payments as income. If this is the case, section CX 47 will apply and treat the amount as **exempt** income …" (emphasis added to show change).

IN SUMMARY

Revenue alert

Legislation and determinations

Legal decisions – case notes

REVENUE ALERT

Revenue alerts inform taxpayers and tax agents about significant and/or emerging tax planning issues or arrangements where Inland Revenue has concerns and is undertaking further risk assessment and investigative activities.

RA 11/01: DONATIONS TAX CREDIT – ARRANGEMENTS ENTERED INTO TO GET A TAX CREDIT WHERE THERE HAS NOT BEEN A TRUE GIFT OF MONEY

Explanation

A revenue alert is issued by the Commissioner of Inland Revenue and provides information about a significant and/or emerging tax planning issue of concern to Inland Revenue. At the time an alert is issued risk assessments will already be underway to determine the level of risk and to consider appropriate responses.

A revenue alert will identify:

- the issue (which may be a scheme, arrangement, or particular transaction) that the Commissioner believes may be contrary to the law or is inconsistent with policy
- the common features of the issue
- our current view
- our current approach.

An alert should not be interpreted as being Inland Revenue's final position. Rather, an alert outlines the Commissioner's current view on how the law should be applied. For any alert we issue it is likely that some investigatory work has already been carried out.

If people have entered into an arrangement similar to the one described or are thinking about it, they should talk to their tax advisor and/or to Inland Revenue for advice about tax implications

Issue

Many people make charitable donations each year and receive tax credits accordingly. However, increasingly Inland Revenue is seeing situations where people are claiming tax credits for "donations" in situations where they have not made a true gift of their own money.

Any payment of over $5 to a charity (or some similar public entities) can potentially qualify for a donations tax credit if it is a gift. To be a gift it must:

- be made voluntarily
- provide a material benefit to the recipient without imposing a countervailing detriment
- be for no consideration
- provide no material benefit or advantage to the giver in return.

Features

Inland Revenue has been investigating arrangements where tax credits for donations have been claimed in circumstances where a true gift of money has not been made. These arrangements involve recharacterising (as a gift of money) actions which would have not ordinarily been a donation, in order to receive the donations tax credit from Inland Revenue.

A common feature of these arrangements is that the payment of money is made on the understanding that the donor will receive something in return for the payment of money, eg, the purchase of property.

In many such cases the money is paid back to the donor or an associate within a short period of time (often a matter of days). We consider that a payment in those circumstances is not a gift.

We are also seeing cases where donations tax credits are being claimed where the money being donated does not even belong to the donor.

Current view

Payments made under these arrangements are not a charitable or other public benefit gift, and do not qualify for a tax credit. These payments of money are made in circumstances where the person (or an associate) expects to receive a material benefit or advantage in return.

Examples

The following are some of the arrangements we have identified so far. There will be similar arrangements where the payment would not be a gift of money.

Example 1

A person has a loan outstanding to a charitable organisation which that organisation is unable to repay. Instead of forgiving the loan the person pays the organisation an amount of money equal to the debt in the form of a "donation", on the understanding that the money will, in turn, be used to repay the debt. The organisation repays the debt and the person claims a donations tax credit for the amount given to the charitable organisation.

A variation of this example involves the person first purchasing a debt owed by a charitable organisation so that this kind of arrangement can be put in place.

The payment to the charitable organisation is not considered to be a valid gift as the money was only paid to the charitable organisation on the understanding that it would be used to repay the debt.

Example 2

Another example we have seen involves situations where a person intended to make a gift of property (eg, a motor vehicle) to a charitable organisation. Instead of gifting the property to that organisation (which would not qualify for the tax credit) the person makes a gift of money to the organisation which the charitable organisation then uses to purchase the property from them. The person claims a donations tax credit for the amount of money given to the charitable organisation. In some cases the arrangement also enables the charitable organisation to claim a second hand goods input tax credit for GST purposes on the purchase of the property.

It is not considered that this example involves a valid gift as the person only paid the money to the charitable organisation on the understanding that the property would be purchased from them. That is, the money is returned so that under this arrangement there is no gift of money.

It is also considered that the claiming of a second-hand goods input tax credit by the charitable organisation could be tax avoidance.

Example 3

We are also seeing examples where charitable entities are avoiding their GST liability as well as helping to generate donation tax credits for individuals in circumstances where the money being donated really comes from a fundraising event and may not even belong to the donor. Under this arrangement fundraising is done on behalf of the charitable organisation. The money raised is then passed to an individual (generally closely associated with the charitable organisation) under the understanding that the person will then "donate" that money to the charitable organisation. The charitable organisation will not have to account for any GST on the fundraising event, and the donor will claim a donations tax credit in respect of that money and typically this will also be given by the person to the charitable organisation.

In this example it is considered that taking into account the whole arrangement, there is not a valid gift for the purposes of claiming the donations tax credit as the money paid to the charitable organisation was not the donor's.

Current status

Where Inland Revenue considers that donations tax credits have been claimed in situations where a true gift of money has not been made we will recover the excess tax credit from the person making the claim and will also consider the imposition of monetary penalties.

It is our view that some of these arrangements may in extreme cases amount to fraud and we will consider prosecution where appropriate.

If you consider that our concerns may apply to your situation, we recommend you discuss the matter with your tax advisor or with us, and consider making a voluntary disclosure

Guidelines for making a voluntary disclosure are given in our guide *Putting your tax returns right (IR 280)* and Standard Practice Statement SPS 09/02: *Voluntary disclosures* (May 2009).

Sections LD 1 and LD 3 of the Income Tax 2007

This revenue alert is issued on 2 August 2011.

Graham Tubb

Group Tax Counsel, Legal & Technical Services

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 CFC 2011/03: NON-ATTRIBUTING ACTIVE INSURANCE CFC STATUS (CIGNA APAC HOLDINGS LIMITED)

Reference

This determination is made under section 91AAQ of the Tax Administration Act 1994.

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

Explanation (which does not form part of the determination)

Under sections CQ 2(1)(h) and DN 2(1)(h) of the Income Tax Act 2007, subject to sections CQ 2(2B) and DN 2(2), no attributed CFC income or loss arises from a CFC that is a non-attributing active CFC under section EX 21B of the Income Tax Act 2007.

Section EX 21B(3) of the Income Tax Act 2007 provides that a CFC that is an insurer meeting the requirements of a determination made by the Commissioner under section 91AAQ of the Tax Administration Act 1994 is a non-attributing active CFC. In the absence of such a determination, a CFC carrying on an insurance business is unlikely to be a non-attributing active CFC, because insurance income is otherwise treated as passive income and an attributable CFC amount by section EX 20B(3) of the Income Tax Act 2007.

Section 91AAQ(1)(b) of the Tax Administration Act 1994 allows a person to apply to the Commissioner for such a determination in respect of the members of a group of CFCs, if the members satisfy subsection (3). Cigna APAC Holdings Limited has made application in respect of the members of the group of CFCs set out below.

It has been determined, having regard to the matters set out in subsections (4) and (5) of section 91AAQ of the Tax Administration Act 1994, that the members of the group of CFCs satisfy the requirements set out in section 91AAQ(3) of the Tax Administration Act 1994 and are accordingly non-attributing active CFCs for the purposes of section EX 21B of the Income Tax Act 2007.

Scope of determination

The CFCs to which this determination applies are:

Name	Jurisdiction
Cigna Hong Kong Holdings Company Limited	Hong Kong
Cigna Worldwide Life Insurance Company Limited	Hong Kong
Cigna Worldwide General Insurance Company Limited	Hong Kong

Interpretation

In this document, unless the context otherwise requires:

"Attributed CFC income or loss" means attributed CFC income under section CQ 2 or attributed CFC loss under section DN 2 of the Income Tax Act 2007.

"CFC" means a CFC as defined in section YA 1 of the Income Tax Act 2007.

"Non-attributing active CFC" means a non-attributing active CFC under section EX 21B of the Income Tax Act 2007.

Determination

Pursuant to section 91AAQ of the Tax Administration Act 1994 I hereby determine that the above CFCs are non-attributing active CFCs for the purposes of section EX 21B of the Income Tax Act 2007.

Application date

This determination applies for the 2010–11 and 2011–12 income years.

This determination is signed by me this 10th day of August 2011.

John Trezise

Investigations Manager

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.

COMMISSIONER GRANTED LEAVE TO APPEAL TRUSTEE COMPANY LIQUIDATION CASE

Case	Commissioner of Inland Revenue v Newmarket Trustees Ltd (application for leave to appeal)
Decision date	23 June 2011
Act(s)	Companies Act 1993, Tax Administration Act 1994
Keywords	Extension of time to appeal, liquidation, Newmarket Trustees Limited, Chester Trustee Services Limited

Summary

The Commissioner successfully applied to the Court of Appeal for an extension of time to appeal a decision by the High Court not to liquidate Newmarket Trustees Limited, a trustee company.

Impact of decision

The Commissioner can now proceed with his substantive appeal of *CIR v Newmarket Trustees Ltd*.

Facts

The present case stems from an application by the Commissioner to have Newmarket Trustees Limited ("Newmarket"), as trustee of the Southern Lights Trust, placed into liquidation following the expiry of a statutory demand for unpaid taxes.

Following the Newmarket liquidation hearing, the High Court declined to liquidate the company on the basis that, among other things:

a) no benefit would arise from liquidation because Newmarket had no assets

b) the Commissioner did not press for investigation as a ground for a liquidation order

c) liquidation would be costly for Newmarket, as it was a trustee for numerous other trusts

d) Newmarket should have the opportunity to seek adjustments of the Commissioner's assessments.

The Commissioner decided to appeal the High Court's decision (*CIR v Newmarket Trustees Ltd* HC Auckland CIV-2010-404-003913, 22 February 2011) not to liquidate Newmarket, and a notice of appeal was filed with the Court of Appeal within the required timeframe.

However, the notice of appeal was served on Newmarket approximately a day and a half late, although attempts were made to serve Newmarket at its registered office during that time. On the last day for filing, Newmarket's solicitor was advised that an appeal had been filed.

The Commissioner filed an application for an extension of time to appeal, which was subsequently opposed by Newmarket on the basis that the Commissioner's substantive appeal was hopeless.

Decision

The Court of Appeal considered that because:

a) the delay in service was minimal

b) the problem with service arose as a result of a genuine mistake, and

c) there was no suggestion that the delay in service caused Newmarket any prejudice

the only reason for not granting an extension of time would be if the Commissioner's substantive appeal was "hopeless".

Although the Court of Appeal noted that it was not in a position to examine the merits of the substantive appeal in any detail, based on the material before it, the Court of Appeal decided that "it is plain that this is not one of those cases where the appeal is so hopeless that an extension of time should be declined".

As a further reason for allowing an extension of time in this case, the Court of Appeal noted that it might also be useful for it to consider the *Chester Trustee Services Ltd v CIR* [2003] 1 NZLR 395 (CA) decision in applying a court's discretion to make an order for liquidation.

In respect of costs, the Court of Appeal followed the case of *My Noodle Ltd v Queenstown Lakes District Council* [2009] NZCA 224 (CA) and awarded costs to the Commissioner given that it should have been clear to Newmarket that in the circumstances an extension of time would be granted.

APPLICATION FOR RECALL OF TRA DECISION

Case	TRA 42/03, 105/04, 23/05, 54/05 and 38/07 [2011] NZTRA 6
Decision date	16 June 2011
Act(s)	Tax Administration Act 1994, Income Tax Act 1994
Keywords	Recall, appeal

Summary

The disputant was not successful in the recall application. Due to an appeal having being lodged by the disputant, the Taxation Review Authority ("TRA") is functus officio. Further, the decision relied upon by the disputant to justify the recall application was irrelevant.

Impact of decision

This decision confirms the limited grounds upon which a decision may be recalled and that it is not appropriate to recall a decision that is also under appeal.

Facts

On 25 February 2011 the disputant applied to the TRA to recall Judge Barber's decision dated 1 February 2011 reported as [2011] TRA 2 ("the Decision") and, on the same date, appealed the Decision to the High Court. The Decision struck out the disputant's challenges against assessments of income tax for the 1997 to 2005 income tax years. The proceedings related to the Trinity scheme.

The disputant applied to recall the Decision based on the following:

1. The case of *Telstra New Zealand Holdings Ltd v CIR* (2011) 25 NZTC 25,068 (HC) ("*Telstra*"); a purported new judicial decision of relevance, had not been drawn to Judge Barber's attention.
2. There was an alleged abuse of process and the TRA was bound by previous Trinity decisions to accept his right to recall. The disputant submitted that his right to recall was directly covered by the High Court and Court of Appeal in the substantive Trinity proceedings (who purportedly refused to accept the Commissioner's submissions that they had no jurisdiction to hear a recall application filed nine months after the substantive challenge appeal was lodged).
3. His Honour did not have jurisdiction to strike out challenges on the merits.

The Commissioner's position in respect of this application was that:

a) the disputant's decision to appeal had taken the matter out of the TRA's hands as it was functus officio and was unable to take further action in respect of this matter

b) the recall application was, in any event, unfounded and was a further demonstration of the disputant's refusal to accept any adverse judgment, and of his apparent determination to take any opportunity to indefinitely continue litigating Trinity issues.

Decision

Judge Barber dismissed the disputant's application with reference to the disputant's appeal. Specifically His Honour found that:

> As Venning J recognised in *Russell v Klinac* [HC Whangarei AP 18/01, 11 December 2001] at [27], it cannot be appropriate for a trial court to revisit an apparently final decision after that decision has been submitted to the "processes of superior courts". That would give rise to the "plainly … unacceptable" prospect of "the same matter being litigated twice in two Courts at the same time", refer *Redcliffe Forestry Ltd v Commissioner of Inland Revenue* [2011] 1 NZLR 336 (HC) at [12] ("*Redcliffe*") [8].
>
> In this case, the "same matter" is the sustainability of the disputant's challenges in light of the previous Trinity judgments. I have found that the challenges are unsustainable. The disputant must overcome that on appeal. It is "plainly unacceptable", in the words of the current President of the Court of Appeal, for that finding to be revisited before this Authority while the appeal is pending [9].
>
> Strictly, that view disposes of the disputant's application to recall which I therefore dismiss [10] …

His Honour addressed some of the other matters raised in the application. Judge Barber rejected the disputant's "right to recall" argument finding that:

> The disputant acknowledges, the very late recall application in the Trinity challenge proceeding was only possible because the appellants failed to comply with their obligation to seal the High Court judgment promptly after lodging an appeal. The Commissioner (rightly) objected to this conduct but, nevertheless, decided to oppose the application on its merits. The application was heard and dismissed by Venning J on that basis in *Accent Management Ltd v Commissioner of Inland Revenue* (2006) 22 NZTC 19,758 (HC) at [48], [52]–[53] and [88]. The Court of Appeal expressed doubt about

its own jurisdiction to hear an appeal from a refusal to recall, but was not asked to, and did not, express any view on the jurisdiction of the High Court [12].

Judge Barber reiterated that the grounds for recall are "strictly limited" and are "to be exercised only in the most limited of circumstances" referring to the recent decisions of *Erwood v Maxted* [2010] NZCA 93 and *Case Z26* (2010) 24 NZTC 14,380 respectively. For recall to be available on the basis of a new judicial decision, that new decision must either directly or indirectly overrule the decision subject to the recall application by making it "clear" that the decision was "wrong"; *Child Poverty Action Group Inc (CPAG) v Attorney-General* HC Wellington CIV-2009-404-273, (at [13] to [15]).

Amongst other findings, it was held that *Telstra* (which concerned an application by the Commissioner to have a notice of discontinuance set aside on the basis that there was an abuse of process):

1. was not a Trinity scheme judgment; was not about striking out challenge proceedings; was, so far as relevant, consistent with the authorities cited in the Decision and did not, even according to the disputant, compel a different (or any particular) decision on the merits of the case
2. did not indicate that the Decision was wrong or bring this case within the limited circumstances where recall was warranted
3. was no basis for criticising the decision-making process in the Decision, nor any basis for criticising the outcome of that process.

Judge Barber held that the disputant's complaints about the merits of the Decision went to the correctness of that decision and should be pursued by way of appeal.

COURT DECLINES TO USE THE "SLIP RULE"

Case	NTH Douglas and Others v Commissioner of Inland Revenue
Decision date	8 July 2011
Act(s)	High Court Rules
Keywords	Slip rule, Russell, tax avoidance

Summary

Justice Courtney considered the purpose of the "slip rule" was to correct errors but that it was not to be lightly invoked as it would weaken the finality of a judgment and was not used in this instance.

Impact of decision

Although this was a judgment (in the Commissioner's favour) in the ongoing Russell template litigation, it is a useful precedent on the application of the "slip rule" under the High Court Rules.

Facts

The taxpayers were involved in the Russell template avoidance scheme. They were considered by the Commissioner to be engaged in tax avoidance and assessed accordingly. The taxpayers challenged the assessments by tax objections and judicial review but the various reviews and appeals to and from the Taxation Review Authority ("TRA") did nothing to alter the conclusion of tax avoidance.

Due to the prolonged period of the litigation, when the appeal was dismissed by the High Court, the Judge ordered the Commissioner to file and serve affidavits annexing the original cases stated for the various individual taxpayers involved at the same time as he sought to seal the final judgments (see *Douglas v CIR* (2009) 24 NZTC 23,331).

The Commissioner filed the required affidavits when seeking to seal his judgments but, due to an error, did not serve the affidavits on the taxpayers' agent (Mr Russell) until the same time as he served the sealed judgments.

The taxpayers made an application that the judgments had been sealed in error and could not be relied upon by any person. The application was made relying upon the "slip rule" of the High Court Rule:

> **Correction of accidental slip or omission**
>
> (1) A judgment or order may be corrected by the court or the Registrar who made it, if it—
>
> (a) contains a clerical mistake or an error arising from an accidental slip or omission, whether or not made by an officer of the court; or

(b) is drawn up so that it does not express what was decided and intended.

(2) The correction may be made by the court or the Registrar, as the case may be,—

(a) on its or his or her own initiative; or

(b) on an interlocutory application.

Decision

Justice Courtney considered the purpose of the "slip rule" was to correct errors but that it was not to be lightly invoked as it would weaken the finality of a judgment. While acknowledging the Commissioner had acted in error, Her Honour was not satisfied the "slip rule" should be invoked. She concluded that while there was a requirement to serve the affidavits, it was not intended to give the taxpayers further rights of challenge.

Although unfortunate that the affidavits were not served prior to sealing of the judgments, it would make no difference to the taxpayers' position and the sealed orders were not contrary to the judgment reached. Thus the Court declined to invalidate the sealed orders.

COURT DECLINES LEAVE TO AMEND CLAIM AFTER JUDGMENT DELIVERED

Case	Dunphy & Ors v Commissioner of Inland Revenue
Decision date	11 July 2011
Act(s)	Income Tax Act 1976
Keywords	Judicial review, leave to amend statement of claim, settlement, costs

Summary

An applicant unsuccessfully applied for leave to amend his claim after the judgment granting judicial review had been delivered and after the applicant and the Commissioner had settled all matters in relation to the proceeding.

Impact of decision

Beyond the specific circumstances of the case, this judgment confirms the conclusive nature of a settlement entered into by parties that settles all matters in a proceeding.

Facts

On 28 April 2010, Chisholm J granted three taxpayers applications for judicial review, directing the Commissioner of Inland Revenue ("the Commissioner") to reconsider those taxpayers' claims for tax refunds on the strength of the Privy Council's decision in *Peterson v Commissioner of Inland Revenue* [2006] 3 NZLR 433. The claims for refunds related to those taxpayers investments in the film *Utu*.

It was anticipated that the claims for refunds by the other applicants in the proceedings would be resolved in accordance with that judgment. However, in his judgment, Chisholm J reserved leave to any party to apply further "should clarification of any of these orders be required".

In a memorandum dated 18 May 2011, counsel for the applicants advised that all the applicants' claims had been resolved save for the claim of the fourth applicant, Mr Robert Maxwell. In respect of Mr Maxwell, counsel sought an order amending the statement of claim and, if that amendment was permitted, an order directing the Commissioner to reconsider Mr Maxwell's claim in light of it.

Specifically, counsel for the applicants sought to amend Appendix 4 of the amended statement of claim, changing the amount Mr Maxwell had invested in *Utu* from $20,000 (as currently pleaded) to $40,000 (the purported actual amount). It was noted that the $40,000 amount had been included in the initial statement of claim filed.

In a memorandum dated 27 May 2011, counsel for the Commissioner strongly opposed the application on the basis that, amongst other things, a settlement deed had been entered into which settles all matters between Mr Maxwell and the Commissioner in relation to the proceeding. Counsel further queried whether the application came within the reserved leave to apply for clarification of any of the orders in Chisholm J's substantive judgment of 28 April 2011.

Decision

Chisholm J dismissed the application finding that:

> Assuming for the moment that there is jurisdiction to grant leave for the fourth applicant's [Mr Maxwell's] pleading to be amended at this late stage, I am not prepared to grant leave. The proposed amendment is not within the scope of the "clarification" leave reserved to the parties in the substantive judgment. More importantly, the parties appear to have settled all matters in relation to this proceeding.
>
> The application is dismissed. There will be an order for costs on the 2B scale against the fourth applicant in favour of the respondent [7].

His Honour assumed that the applicant did not intend to file any further documentation given the time that had passed since counsel for the Commissioner's memorandum had been filed.

A BUY-BACK OF PART OF A PROPERTY IS NOT "ACQUISITION" UNDER SECTION CD 1(2)(A)

Case	Junior Farms Ltd v Commissioner of Inland Revenue
Decision date	22 July 2011
Act(s)	Income Tax Act 1994
Keywords	Acquisition, disposed legal and equitable interests

Summary

The Court held that a sale arrangement of the property which included a buy-back of part of it for resale was not an "acquisition" for purposes of section CD 1(2)(a) of the Income Tax Act 1994.

Impact of decision

There are no precedential implications as the case turns largely on its facts. The Court took a "plain language" approach to statutory interpretation and construed contractual agreements together rather than separately.

Facts

On or about 21 July 1964, Junior Farms Ltd ("Junior Farms") purchased a property of approximately 92 acres of land on the northern side of Ormiston Road, East Tamaki ("the property").

In about 1988, Manukau City Council ("MCC") notified Junior Farms that a portion of the property was required for flood protection purposes.

In about November 1994, Junior Farms entered into two sale agreements ("the agreements") in respect of the property. Under the first sale agreement ("the first agreement"), Junior Farms sold the property for $2,681,000.00. In the second sale agreement ("the second agreement"), Hampton sold back part of the property (approximately 14 hectares) which was designated for flood protection purposes ("the floodplain area") to Junior Farms for $100.

Junior Farms claimed that the floodplain area was not disposed under the first agreement. It claimed that under the agreements its interest in the floodplain area was held under trust or as equitable ownership.

Decision

The main issue turns on the interpretation of the agreements as to whether they should be construed as one transaction (as contended by Junior Farms) or the two separate transactions (as contended by the Commissioner).

Justice Brewer held that the agreements together with a side letter executed at that time constituted one transaction and concluded that the agreement was a device to give effect to the sale of the industrial part of the property only, with Junior Farms retaining its interests in the floodplain area. There was therefore no disposal of the legal and beneficial interest to the floodplain area of the property by Junior Farms under the first agreement and hence, no acquisition of the same under the second agreement.

WIDE-RANGING DISCOVERY ORDERED

Case	Commissioner of Inland Revenue v Giovanni Holdings Ltd and Ors
Decision date	28 July 2011
Act(s)	Companies Act 1993, High Court Rules
Keywords	Discovery, public interest immunity, electronic database

Summary

The Commissioner was unsuccessful in opposing an application for discovery where he maintained that tax secrecy, public interest immunity or administrative difficulty would arise if the orders were granted. The Court held that these were matters for the Court, not the Commissioner, to decide.

Impact of decision

This decision may have implications for the discovery of information exchanged under the double tax agreements. From a practical perspective, the extent of possible discovery as a consequence of this decision is very broad.

Facts

On 6 September 2010, the Commissioner sought and obtained a freezing order without notice over a property owned by Giovanni Holdings Ltd ("Giovanni"). The freezing order was obtained on the basis that a Mr Petroulias and another were/are the beneficial owners of the property.

Proceedings

Giovanni filed an application in October 2010 seeking an order discharging or varying the freezing order. In the course of case management of that application, the Commissioner objected to representation of Giovanni by Ms Hancock (the director of Giovanni). The High Court (in a decision dated 22 December 2010) decided in favour of Giovanni and allowed Ms Hancock to represent the company.

Giovanni also filed an application seeking an order that general discovery be made by the Commissioner. The Commissioner opposed the application. This hearing was to consider the discovery issue.

Decision

Giovanni sought an order for general discovery of:

a) all transcripts of recorded phone calls held between Mr Petroulias and others and provided to the Commissioner by the Australian Tax Office ("ATO")

b) all electronic databases containing relevant information, including the "Z:drive" which was seized in the Commissioner's access operations in 2006

c) all probative communication between the Commissioner and the ATO

d) all other probative documents, correspondence and records of interviews with any party.

McKenzie J firstly granted the leave sought by Mr Petroulias to be heard in the discovery proceedings (the application had only been filed by Giovanni) as it was necessary in the interests of justice.

With regard to the general discovery sought, McKenzie J noted that the Commissioner's actions were being challenged (an application to strike out the proceedings had been filed on the basis of abuse of process) and acknowledged what while these were better addressed in the substantive proceedings, it was relevant in considering the extent of appropriate discovery.

McKenzie J agreed that, as a matter of general principle, the *Peruvian Guano* test was not appropriate in cases where, as a matter of policy, they should be dealt with swiftly (such as freezing orders). His Honour acknowledged that discovery was not usually appropriate in freezing order applications as they are usually dealt with on an urgent basis and confirmed that the onus is usually on the applicant for the freezing order to show it has a good arguable case and to disclose all material facts and possible defences. However, McKenzie J considered that this case was different as the application for discharge of the freezing order would require an inquiry wider than whether the Commissioner had an arguable case regarding beneficial ownership of the relevant property. Further, any delay in the proceedings (despite the urgency of a freezing order application) did not weigh against discovery, particularly when the Commissioner's position is protected by the freezing order.

The Commissioner had argued that all relevant material had been produced pursuant to section 81(1) of the Tax Administration Act 1994. McKenzie J rejected that submission stating that not all discoverable documents will usually be produced in evidence and should be verified by a discovery affidavit. McKenzie J confirmed the position in *Knight v CIR* and *BNZ Investments Ltd v CIR* that the conduct of litigation (and specifically discovery) is a purpose of carrying into effect the Inland Revenue Acts for the purposes of section 81.

However, his Honour recognised that production of discovered documents can be withheld where a claim of privilege is available. In that regard, McKenzie J referred to the Commissioners submission that the documents were subject to public interest immunity and confirmed the principle in *BNZ Investments* [2008] 2 NZLR 709 that section 81 addresses the reconciliation of the principles of taxpayer discovery and the interests of justice. While the respondents submitted that no public interest immunity issues arise as discussed in *CIR v ER Squibb* (1992) 14 NZTC 9146, McKenzie J stated it need not be addressed at this point in the proceedings (noting that the ultimate decision on a claim of public interest immunity is for the Court to decide, not the Commissioner and if necessary the Court will inspect the documents to determine the question).

With regard to the first category of documents, his Honour disagreed that the respondents had failed to establish relevance and held that the Commissioner's reliance on some of this material provided a sufficient basis for discovery of all transcripts.

As for the second category, McKenzie J noted that the "Z:drive" had been subject to previous litigation (Venning J had decided that the Commissioner was not required to make available a cloned copy of the hard drive). However, McKenzie J stated that the question before his Honour was different to that before Venning J and held that discovery should be required of relevant documents contained on that hard drive.

McKenzie J rejected the Commissioner's submission that discovery would be unduly burdensome due to the volume of information on the hard drive. His Honour stated that there are two ways to avoid such a burden: the Commissioner can either make a copy of the "Z:drive" available to the respondents or carry out keyword searching to locate relevant documents. McKenzie J considered it was inappropriate for the Court to fix a list of words and stated that it will be for the Commissioner to decide the relevant search terms (noting that the Commissioner will need to set out the basis for the relevance testing in an affidavit to ensure adequacy of the search can be examined should it be challenged).

His Honour rejected the Commissioner's submission that as the documents in the third category were the subject of incomplete investigations in both New Zealand and

Australia, the disclosure would prejudice the maintenance of the law. McKenzie J held that section 81 was also relevant to this category of evidence and again stated that any decision on public interest immunity was for the Court not the Commissioner.

As for the fourth category, being all other relevant documents, correspondence and records of interviews, McKenzie J also ordered that these should be discovered.

In summary, the Commissioner was ordered to produce a discovery affidavit listing all relevant information from all four categories (which are or have been in the Commissioner's control) within 20 working days.

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