

TAX INFORMATION

Bulletin

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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.

IN SUMMARY

Interpretation statements

IS 13/02: Income tax – whether certain rights conferred by the Companies Act 1993 could give rise to a “shareholder decision-making right”

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This interpretation statement concerns whether certain rights conferred by the Companies Act 1993 could give rise to a “shareholder decision-making right” as defined in section YA 1 of the Income Tax Act 2007. This statement addresses an issue that has been raised by taxpayers and their advisers in the course of a number of private binding ruling applications.

Binding rulings

Product ruling BR Prd 13/11: Meridian Energy Limited

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This product ruling applies to the sale of up to 49% of the ordinary shares in Meridian Energy Limited, through the use of instalment receipts, by the Crown to New Zealand resident retail and institutional investors, pursuant to the terms contained in the combined Investment Statement and Prospectus.

Legislation and determinations

Special Determination S24: Application of the financial arrangements rules to the sale of shares in Meridian by the Crown

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This determination relates to the sale of up to 49% of the ordinary shares in Meridian Energy Limited by the Crown to New Zealand resident retail and institutional investors, pursuant to the terms contained in the combined Investment Statement and Prospectus.

Foreign currency amounts – conversion to New Zealand dollars

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This article provides the exchange rates acceptable to Inland Revenue for converting foreign currency amounts to New Zealand dollars for the six months ending 30 September 2013.

New legislation

Order in Council

31

Information-sharing agreement between Inland Revenue and the Department of Internal Affairs – contact details as part of passport renewal or application process

This Order in Council approves a new information-sharing agreement between Inland Revenue and the Department of Internal Affairs. Under the agreement, Internal Affairs will provide Inland Revenue with all contact details that it has obtained as part of the adult passport application process.

Questions we’ve been asked

QB 13/04: Income tax – Retention money

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This question we’ve been asked does not represent a change in the Commissioner’s longstanding published view on the tax treatment of retention money. This item replaces and updates an item published in March 1980 in *Public Information Bulletin* No 103.

Items of interest

Update on Public Information Bulletin review

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Inland Revenue has now completed the formal process of reviewing all items containing tax technical information in the 183 *Public Information Bulletin* volumes and identifying those which are of no current relevance and will not be republished. The remainder have either been updated and republished in a current *Tax Information Bulletin* or, in the case of a small number, are to be given further consideration.

Legal decisions – case notes

Trinity avoidance scheme

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The Judgment upheld the application by the Commissioner of Inland Revenue to dismiss or strike out the claim of judicial bias against Venning J in regard to his 2004 Judgment where he held the Trinity scheme was tax avoidance.

Outstanding proceedings not a “substantial dispute” for the purpose of setting aside a statutory demand where there are finalised tax challenges

39

The Judgment dismissed an application by Trinity investors to set aside statutory demands based on assessments confirmed by the Supreme Court. The application relied on another proceeding seeking to dispute the validity of the Court’s previous decisions in relation to the Trinity scheme. The Judge declined to make an order for immediate liquidation but required full payment in 10 working days, failing which liquidation can be applied for.

INTERPRETATION STATEMENTS

This section of the *TIB* contains interpretation statements issued by the Commissioner of Inland Revenue.

These statements set out the Commissioner's view on how the law applies to a particular set of circumstances when it is either not possible or not appropriate to issue a binding public ruling.

In most cases Inland Revenue will assess taxpayers in line with the following interpretation statements. However, our statutory duty is to make correct assessments, so we may not necessarily assess taxpayers on the basis of earlier advice if at the time of the assessment we consider that the earlier advice is not consistent with the law.

IS 13/02: INCOME TAX – WHETHER CERTAIN RIGHTS CONFERRED BY THE COMPANIES ACT 1993 COULD GIVE RISE TO A “SHAREHOLDER DECISION-MAKING RIGHT”

Legislative references are to the Income Tax Act 2007 (ITA 2007) and the Companies Act 1993 (CA 1993). Relevant legislative provisions are reproduced in the Appendix to this Interpretation Statement.

Summary

1. This Interpretation Statement considers whether certain protective rights conferred by the CA 1993 could give rise to a “shareholder decision-making right” under s YA 1 of the ITA 2007.
 2. Under s YC 2 of the ITA 2007, a person’s “voting interest” in a company equals the percentage of shareholder decision-making rights carried by shares or options over shares held by the person. A “shareholder decision-making right” is a right carried by a share issued by a company (or an option over a share issued by a company) to vote or participate in any decision-making concerning:
 - dividends or distributions to be paid;
 - the constitution;
 - variations in capital; and
 - the appointment of directors.
 3. The Commissioner considers that s 36(1) of the CA 1993 is the only provision in that Act that gives rise to any shareholder decision-making rights. Section 36(1) of the CA 1993 sets out the rights attached to shares. These are the rights to:
 - a vote in any resolution;
 - an equal share in dividends; and
 - an equal share in the surplus assets of the company.
 4. Section 36(2) provides that these rights may be negated, altered or added to by the constitution or the terms of issue of the shares. The CA 1993 anticipates that some classes of shares may carry no voting rights.
- This Interpretation Statement is of particular relevance to those non-voting classes of shares. This is because provisions in the CA 1993 confer certain protective rights to all shareholders, irrespective of their voting rights or the company’s constitution. The question is whether those types of rights could be a shareholder decision-making right.
5. Two provisions in the CA 1993 were identified as potentially giving rise to a shareholder decision-making right for tax purposes. Section 107 allows a company to undertake various actions without adhering to procedural requirements of the CA 1993 if all shareholders agree. Section 117 provides shareholders with the right to vote on an action taken by a company that affects the rights attached to their shares.
 6. The Commissioner considers that ss 107 and 117 of the CA 1993 do not give rise to a shareholder decision-making right under s YA 1 of the ITA 2007. Any rights conferred by those sections are not included in the calculation of a person’s “voting interest” in a company under s YC 2 of the ITA 2007.
 7. This Interpretation Statement focuses on rights conferred by the CA 1993. However, protective rights of a similar nature to those in s 117 may also be provided in a company constitution, the terms of issue of a share, options over shares or in the NZX listing rules. The conclusions reached in this Interpretation Statement would apply equally to those similar rights.
- Why is this issue relevant?*
8. Several private binding ruling applications identified this issue as being potentially relevant for shareholder continuity purposes. This Interpretation Statement is issued to provide certainty for all taxpayers.

9. The calculation of a person's voting interest in a company is relevant for applying the continuity provisions in the ITA 2007 (unless a market value circumstance exists). The continuity provisions generally require that a group of persons' combined voting interests in a company or companies exceeds certain minimum levels over a period. The continuity provisions govern a company's ability to carry forward losses, memorandum account credits or excess tax credits and to offset losses with other companies. If rights arising under ss 107 and 117 of the CA 1993 were voting interests, this might impact on a company's ability to satisfy shareholder continuity requirements. Problems could similarly arise for the rules concerning consolidation, controlled foreign companies and associated persons.

Summary of reasoning

10. The definition of a "shareholder decision-making right" requires that the right is carried by a share or an option over a share issued by a company. The Commissioner considers that rights arising under ss 107 and 117 of the CA 1993 are carried by all shares issued by a company.
11. The definition further requires that the right is to "vote or participate in any decision-making" concerning four types of decisions. It is certainly arguable that rights arising under ss 107 and 117 of the CA 1993 could provide a shareholder with an ability to "participate" in any decision-making. However, the rights conferred by ss 107 and 117 are not substantive voting rights. They are rights of a contingent nature, and arise temporarily on certain actions being proposed by a company. The issue is whether the definition is to be interpreted in a broad way that includes these contingent "protective" rights or whether the definition should be limited to substantive rights.
12. The definitions of "voting interest" and "shareholder decision-making right" were enacted as a means of measuring a shareholder's level of control over the company's decisions and resources. A definition of "market value interest" applies in some situations where voting interests may not accurately reflect a person's interests in a company.
13. The Commissioner considers that protective rights of a contingent and temporary nature were not intended to be included in the calculation of a person's voting interest in a company. A broad interpretation including these types of rights in calculating a person's voting interest in a company could lead to absurdity by making the calculations unworkable.

14. Therefore, the Commissioner considers that the preferred interpretation is that ss 107 and 117 of the CA 1993 do not give rise to a shareholder decision-making right. This conclusion equally applies to protective rights of a similar nature to those in s 117 that are in a company constitution, the terms of issue of shares, options over shares or the NZX listing rules.

Analysis

15. This Interpretation Statement considers whether certain protective rights could affect the percentage of voting interests held by a shareholder of a company for the purposes of the ITA 2007. The issue is particularly relevant for a shareholder who holds non-voting shares or options over shares issued by a company. It might seem counter-intuitive that a shareholder holding non-voting shares or options could somehow be said to have a voting interest in the company. However, the question arises due to the broad definitions of "voting interest" and "shareholder decision-making right" in the ITA 2007. The issue is important because it could affect rules relating to shareholder continuity, associated persons, controlled foreign companies and consolidated groups.
16. This Interpretation Statement first sets out the definitions of "voting interest" and "shareholder decision-making right" in the ITA 2007. It then explains why rights arising under ss 107 and 117 of the CA 1993 could fall within those definitions for tax purposes. The statement then considers the purpose of the definitions and whether an interpretation can be reached that is consistent with this purpose.

What are "voting interests" and "shareholder decision-making rights"?

17. A person's voting interest in a company is referred to in various provisions in the ITA 2007. These provisions include rules relating to associated persons, shareholder continuity, controlled foreign companies and consolidation.
18. Section YA 1 of the ITA 2007 defines a voting interest as follows:

voting interest—

 - (a) means, for a person and a company and a time, the percentage voting interest that the person is treated as holding in the company at the time under sections YC 2 to YC 20 (which relate to the measurement of company ownership):
19. Section YC 2 of the ITA 2007 provides:

YC 2 Voting interests

Percentage of shareholder decision-making rights

 - (1) A person's voting interest in a company equals the percentage of the total shareholder decision-

making rights for the company carried by shares or options held by the person.

When decision-making rights vary

- (2) Despite subsection (1), if the percentage of shareholder decision-making rights for a company carried by shares or options held by any person differs as between the types of decision-making listed in the definition of shareholder decision-making right, the person's voting interest in the company equals the average of those differing percentages.

20. A person's voting interest in a company equals the percentage of the total shareholder decision-making rights for the company that are carried by the shares or options the person holds. The scope of this Interpretation Statement is limited to considering the types of rights that might be a shareholder decision-making right.

21. Section YA 1 of the ITA 2007 defines a shareholder decision-making right as follows:

shareholder decision-making right means a right, carried by a share issued by a company or an option over a share issued by a company, to vote or participate in any decision-making concerning—

- (a) a dividend or other distribution to be paid or made by the company, whether on a liquidation of the company or otherwise, excluding decision-making undertaken by directors acting only in their capacity as directors; or
- (b) the constitution of the company; or
- (c) a variation in the capital of the company; or
- (d) the appointment of a director of the company

22. The definition contains three requirements. The relevant right must:

- be "carried by" a share or an option over a share;
- be a right to "vote or participate in any decision-making"; and
- relate to one of the four listed types of decision-making (ie, a dividend or distribution to be paid, the company's constitution, a variation in capital, or the appointment of a director).

What rights in the Companies Act 1993 could be a shareholder decision-making right?

Section 36(1) – rights and powers attaching to shares

23. Section 36 of the CA 1993 provides:

36 Rights and powers attaching to shares

- (1) Subject to subsection (2), a share in a company confers on the holder—

- (a) the right to 1 vote on a poll at a meeting of the company on any resolution, including any resolution to—
 - (i) appoint or remove a director or auditor;
 - (ii) adopt a constitution;
 - (iii) alter the company's constitution, if it has one;
 - (iv) approve a major transaction;
 - (v) approve an amalgamation of the company under section 221;
 - (vi) put the company into liquidation;
- (b) the right to an equal share in dividends authorised by the board;
- (c) the right to an equal share in the distribution of the surplus assets of the company.

- (2) Subject to section 53, the rights specified in subsection (1) may be negated, altered, or added to by the constitution of the company or in accordance with the terms on which the share is issued under section 41(b) or section 42 or section 44 or section 107(2), as the case may be.

24. Section 36(1) provides that the rights conferred by a share are the right to one vote at a meeting on any resolution, the right to an equal share in dividends and the right to an equal share in the distribution of surplus assets. Some of these rights would give rise to a shareholder decision-making right to the extent they fall within the four listed types of decision contained in the definition.

25. Section 36(2) provides that the rights specified in s 36(1) may be negated, altered or added to by the company's constitution or the terms of issue of a share. Consistent with this, s 37 anticipates that a company may issue shares that confer no voting rights. Certain classes of shares (eg, preference shares) may offer the holder a preferential claim to a dividend but confer no, or limited, voting rights. Therefore, it would seem that such shares would not confer any shareholder decision-making rights on the holder. However, some provisions in the CA 1993 confer a right to participate in certain matters on all classes of shares, regardless of voting rights. The company constitution or the terms of issue of the share cannot negate these rights.

26. These identified rights include the right to:

- participate as an "entitled person" under any s 107 agreement;
- comment on the management of the company at an annual shareholders' meeting under s 109(1);
- vote as part of an interest group under s 117 on any issue affecting the rights attached to that shareholder's shares;

- exercise buy-out rights under s 118, where that shareholder has voted against an action approved by that shareholder’s interest group under s 117; and
 - receive notice of and attend an annual shareholders’ meeting under s 120(1).
27. The above rights are present in all classes of shares, irrespective of voting rights or the company constitution.
28. Although the holder of a class of share that confers no voting rights may have a right to attend (s 120(1)) and comment (s 109(1)) at a shareholders’ meeting, those provisions do not give the holder of such a share any ability to vote or otherwise participate in any decisions made at that meeting. Therefore, these sections would not give rise to a shareholder decision-making right. The constitution cannot negate several other provisions in the CA 1993. These provisions include the requirement for a special resolution of shareholders for particular actions to be undertaken regarding alterations to the constitution, major transactions, amalgamations or liquidation. However, while there must always be a special resolution on such actions, the constitution or the terms of issue of a share can limit the classes of shareholder entitled to vote on those resolutions, as provided in s 36(2).
29. Taking this all into account, only two provisions were identified that could potentially give rise to shareholder decision-making rights—ss 107 and 117 of the CA 1993. Both of these provisions permit shareholders, including holders of non-voting shares, to participate in particular company decisions.

Section 107 – unanimous assent to certain types of action

30. Section 107 of the CA 1993 provides that, if all entitled persons have agreed or concur, certain actions can take place otherwise than in accordance with the CA 1993. The section relevantly states:

107 Unanimous assent to certain types of action

- (1) Notwithstanding section 52 but subject to section 108, if all entitled persons have agreed or concur,—
- (a) a dividend may be authorised otherwise than in accordance with section 53:
 - (b) a discount scheme may be approved otherwise than in accordance with section 55:
 - (c) shares in a company may be acquired otherwise than in accordance with sections 59 to 65:
 - (d) shares in a company may be redeemed otherwise than in accordance with sections 69 to 72:

- (e) financial assistance may be given for the purpose of, or in connection with, the purchase of shares otherwise than in accordance with sections 76 to 80:
 - (f) any of the matters referred to in section 161(1) may be authorised otherwise than in accordance with that section.
- (2) If all entitled persons have agreed or concur, shares may be issued otherwise than in accordance with section 42 or section 44 or section 45.
- (3) If all entitled persons have agreed to or concur in a company entering into a transaction in which a director is interested, nothing in sections 140 and 141 shall apply in relation to that transaction.

...

31. Section 2 of the CA 1993 defines an “entitled person” as: **entitled person**, in relation to a company, means—
- (a) a shareholder; and
 - (b) a person upon whom the constitution confers any of the rights and powers of a shareholder:
32. Section 107 allows some of the formal requirements of the CA 1993 to be bypassed for the listed actions if all entitled persons agree or concur. The definition of entitled person does not distinguish between shareholders who are entitled to vote on a particular action, and those who are not. Therefore, the use of the term “entitled person” shows that all shareholders of the company (not just voting shareholders) **must** agree or concur to the action being taken. The agreement or concurrence must be in writing.
33. Section 107 was enacted following submissions about the costs and formalities small companies would face in complying with the draft Companies Act 1990. In *Company Law Reform: Transition and Revision* (NZLC R16, Law Commission, Wellington, 1990), the Law Commission stated at [45]:

Unanimous assent to company action

Section 78A [now s 107] is a very important new provision. The Law Commission accepts the submissions made by a number of bodies and individuals that the 1990 [draft Companies] Act imposed excessive formalities on the day-to-day operation of small (and, in particular, one-shareholder) companies. **This section permits the formalities which were considered to be a problem to be disregarded completely, if all entitled persons agree, or if they concur in the informal action taken.** In a normal company, in which all the section 6 [Essential rights and powers] rights and powers are attached to shares, a company will be able to issue shares, or repurchase shares, for example, without any formalities at all, where the shareholders agree to or concur in the issue or repurchase.

[Emphasis added]

34. Andrew Beck and others in *Morison's Company and Securities Law* (looseleaf ed, LexisNexis) state at [16.10]:

The Act provides for suspension of some of the formalities and procedures required by the Act where all those affected agree to the relevant action, or concur in it being taken. All entitled persons must agree to or concur in the action, and the agreement or concurrence must be in writing. The entitled persons will normally be all the shareholders, but will also include any person other than a shareholder upon whom the constitution of the company confers rights which would otherwise be enjoyed by shareholders. The agreement may either be a separate "one off" agreement to a particular exercise of a power, or a standing agreement to the exercise of the power generally or from time to time. An entitled person can at any time by notice in writing to the company withdraw from a general or standing unanimous shareholder agreement, and in the absence of continuing unanimity s 107 will no longer apply. ...

[Emphasis added]

35. Section 107 enables companies to suspend some of the formalities and procedures in the CA 1993, if all entitled persons have agreed to the action in writing. If unanimous assent is not obtained, the company must adhere to all the formalities and procedures in the CA 1993.

Section 117 – alteration of shareholder rights

36. Section 117 of the CA 1993 provides:

117 Alteration of shareholder rights

- (1) A company must not take action that affects the rights attached to shares unless that action has been approved by a special resolution of each interest group.
- (2) For the purposes of subsection (1), the rights attached to a share include—
 - (a) the rights, privileges, limitations, and conditions attached to the share by this Act or the constitution, including voting rights and rights to distributions;
 - (b) pre-emptive rights arising under section 45;
 - (c) the right to have the procedure set out in this section, and any further procedure required by the constitution for the amendment or alteration of rights, observed by the company;
 - (d) the right that a procedure required by the constitution for the amendment or alteration of rights not be amended or altered.
- (3) For the purposes of subsection (1), the issue of further shares ranking equally with, or in priority to, existing shares, whether as to voting rights or distributions, is deemed to be action affecting the rights attached to the existing shares, unless—

- (a) the constitution of the company expressly permits the issue of further shares ranking equally with, or in priority to, those shares; or
 - (b) the issue is made in accordance with the pre-emptive rights of shareholders under section 45 or under the constitution of the company.
37. A company must not take action that affects the rights attached to shares, unless that action has been approved by a special resolution of each interest group. An "interest group" is defined in the CA 1993 as a group of shareholders with identical rights who will be affected by the company's action or proposal.
38. Section 117 provides the members of an interest group (whether or not their shares confer voting rights) with the ability to approve or not approve a particular action that would affect the rights attached to their shares. The rights "attached to a share" are defined non-exhaustively to include the rights, privileges, limitations and conditions attached to the share by the CA 1993 or the constitution. This specifically includes voting rights, the right to distributions and pre-emptive rights. The section also clarifies that the issue of further shares that rank in priority to, or equal with, the class of share is an action affecting that class of share.
39. Section 117 requires that the approval is made by special resolution (requiring the assent of 75 percent of affected shareholders in that interest group). If a special resolution is passed and a particular shareholder voted against approving the action or did not sign the resolution, s 118 provides that the shareholder may require the company to purchase their shares under s 111.
40. Section 119 provides that when a company takes action that affects the rights attached to shares, that action is not invalidated by reason only that the action was not approved in accordance with s 117. However, in such circumstances, the affected interest group could take action against the company for unfair prejudicial conduct under s 174 of the CA 1993.
41. The rights conferred on shareholders under s 117 are of a protective nature, and are contingent on the company's actions. They arise when the company calls for a special resolution of the affected interest group (or otherwise decides to undertake the action). Once this happens, s 117 allows an affected shareholder to vote in a special resolution to approve or not approve the action.

Could ss 107 and 117 give rise to a “shareholder decision-making right”?

42. Two questions arise about the relationship between ss 107 and 117 of the CA 1993 and the definition of a shareholder decision-making right:
 - Is the existence of ss 107 and 117 in the CA 1993 a shareholder decision-making right at all times?
 - Could ss 107 and 117 give rise to a shareholder decision-making right when triggered (ie, when unanimous assent is sought or a special resolution of an affected interest group is called by a company)?
43. The Commissioner considers that the mere existence of ss 107 and 117 cannot give rise to shareholder decision-making rights. The existence of those provisions does not ordinarily provide shareholders with any rights to vote or participate in any decision-making regarding the four listed types of decision. The company must first trigger the rights by:
 - requesting the unanimous written assent of all shareholders so an action can be undertaken otherwise than in accordance with certain procedures (s 107); or
 - calling for a resolution to approve a proposed action that will affect the rights attached to a particular class of share (s 117).
44. Also, the definition of a shareholder decision-making right is limited to the four listed types of decision. These are any decision concerning dividends or distributions to be paid, the constitution, the appointment of a director, and a variation of capital. Sections 107 and 117 concern a broader variety of actions. The actions could concern the four listed types of decision, but they could also concern other things that are not relevant to the definition of a shareholder decision-making right. It is also possible that a company might never propose to obtain unanimous assent to an action under s 107 or take an action that affects rights attached to shares under s 117.
45. Further, the company constitution cannot negate the protective right under s 117 and the ability to use the s 107 procedure. If an interpretation were taken that the existence of these rights in the CA 1993 could be a shareholder decision-making right for tax purposes, every share a company issued would confer voting interests. The Commissioner considers that the mere existence of those provisions in the CA 1993 does not confer a shareholder decision-making right on all shareholders.
46. The more relevant question is whether ss 107 and 117 could give rise to a shareholder decision-making right

when invoked. The provisions require shareholders to provide their assent or to vote in a special resolution. The question is whether the right to assent or vote on that particular decision could at that time be a right carried by a share (or an option over a share) to vote or participate in any decision-making concerning the four listed types of decision.

47. As noted at [22] above, the definition of a shareholder decision-making right requires that the rights are carried by a share or an option over a share. The rights must also be a right to vote or participate in any decision-making concerning the four listed types of decision. These criteria will now be discussed in the context of ss 107 and 117 of the CA 1993.

Are rights arising under ss 107 and 117 “carried by” a share?

48. The first question is whether the rights arising under ss 107 and 117 could be said to be “carried by” a share issued by a company. Although the company constitution or share issue terms may include similar rights, the constitution or share issue terms cannot negate or alter rights arising under ss 107 and 117 of the CA 1993.
49. The *Concise Oxford English Dictionary* (12th ed, Oxford University Press, New York, 2011) relevantly defines the word “carry” as “have as a feature or consequence”.
50. Case law discussing the nature of shares assists in determining what rights might be “carried by” a share. For instance, in *IRC v Crossman* [1937] AC 26 (HL) at 66, Lord Russell described a share as:

A share in a limited company is a property the nature of which has been accurately expounded by Farwell J. in *Borland’s Trustee v Steel*. It is the interest of a person in the Company, that interest being composed of rights and obligations which are defined by the Companies Act and by the memorandum and articles of association of the company.
51. A share consists of a “bundle of rights and obligations” (see *Borland’s Trustee v Steel Brothers & Co Ltd* [1901] 1 Ch 279). The CA 1993 and the company constitution define these rights and obligations.
52. It is considered that rights in the company constitution or the terms of issue of a share will be carried by the shares. Similarly, any rights contained in an option will be carried by that option.
53. In terms of rights and obligations defined by the CA 1993, s 36 of that Act sets out the rights that can make up a share. Although rights arising under s 117 are conferred by statute, similar rights are also sometimes referred to in the company constitution.

However, unlike other rights arising under s 36(1) of the CA 1993, the constitution or the terms of issue of shares cannot negate s 117. Therefore, even if the constitution or terms of issue of a share do not explicitly refer to s 117, those rights would be an attribute or a feature of all shares a company issues.

54. Also, s 117(2)(c) specifically provides that the procedure set out in that section is a right “attached to a share”. The reference to rights “attached to” shares is similar to the reference to rights that are “carried by” shares. The UK case *Cumbrian Newspapers Group Ltd v Cumberland and Westmorland Herald Newspaper and Printing Co Ltd* [1987] Ch 1 used the words “carried by” interchangeably with “attached to”. That case concerned a UK provision similar in nature to s 117. The court stated at 15:

I turn to the critical question: are the plaintiff’s rights under articles 5, 7, 9 and 12, rights attached to a class of shares?

... If articles provide that particular shares carry particular rights not enjoyed by the holders of other shares, it is easy to conclude that the rights are attached to a class of shares, for the purpose both of section 125 of the Act of 1985 and of article 4 of Table A. It is common ground that rights falling into this category are rights attached to a class of shares for those purposes.

55. Therefore, a right that is “attached to” a share could also be regarded as being “carried by” that share.
56. The Commissioner considers that s 117 rights are a feature or consequence of every share a company issues, and so all shares carry such rights.
57. Section 107 permits a company to obtain the unanimous assent of all entitled persons before undertaking certain actions. This group may include persons who are not shareholders. For such persons, the ability to assent to an action cannot be carried by shares (in terms of the definition of a shareholder decision-making right). However, for shareholders, it is certainly arguable that the ability to assent to an action under s 107 is carried by a share.
58. Therefore, the ability to assent to an action under s 107 and the rights arising under s 117 of the CA 1993 would be “carried by” shares held by a person. Similar rights in the company constitution or terms of issue of a share would also be carried by that share. Similarly, any rights in an option over a share would be carried by that option.

Do ss 107 and 117 confer a right to vote or participate in any decision-making?

59. The next question is whether ss 107 and 117 give rise to rights to participate or vote in any decision-making.

The ordinary meanings of “participate” and “vote” (*Concise Oxford English Dictionary* (12th ed, Oxford University Press, New York, 2011)) are:

participate v. 1 (often participate in) be involved; take part. 2 (participate of) archaic partake of (a quality).

vote n. a formal indication of a choice between two or more candidates or courses of action, expressed typically through a ballot or a show of hands . an act of voting . (the vote) the right to indicate a choice in an election ...

60. A shareholder decision-making right is a right (carried by a share or an option over a share) for a shareholder to choose between two or more courses of action or to be involved or take part in any of the listed types of decisions. This type of right seems broad. It is arguable from this ordinary meaning that the rights in ss 107 and 107 could give rise to an ability to “vote or participate in any decision-making”.

Section 107

61. Some of the actions in s 107 relate to the types of decision referred to in the definition of a shareholder decision-making right. Section 107 lists actions such as authorising dividends and acquiring the company’s own shares.
62. For example, an argument could be made that s 107(1)(a) provides an opportunity for shareholders to participate in a decision concerning dividends to be paid. Section 107(1)(a) provides that, if unanimous assent were obtained, a dividend may be authorised otherwise than in accordance with s 53 of the CA 1993. Decisions concerning the payment of dividends are not conferred on shareholders under any other provisions of the CA 1993.
63. However, s 107(1)(a) refers only to the authorising of a dividend otherwise than in accordance with s 53 of the CA 1993. Section 53 requires the directors of a company to pay equal dividends to all of the shareholders in a particular class. Therefore, s 107(1)(a) allows the company’s directors to authorise the payment of unequal dividends if all entitled persons have agreed. The decision about the dividend to be paid remains with the directors. Section 107 does not provide shareholders with a right to participate in that decision. It simply allows the company to bypass the procedural requirements in the CA 1993.
64. Also, if unanimous assent is not achieved, the company would be required to follow the procedural requirements of the CA 1993. Any non-voting shareholders would not be involved in that decision (unless their rights were also affected under s 117).

As noted above, s 107 operates to allow companies to bypass certain procedural requirements in the CA 1993 if all shareholders agree. The section does not confer any rights on the shareholders, but allows the company to undertake certain actions in a way that might otherwise not be allowed under the CA 1993.

65. Therefore, the Commissioner considers that s 107 does not give rise to a shareholder decision-making right. The section simply allows a company to undertake certain actions or procedures otherwise than in accordance with particular provisions in the CA 1993, if the company's shareholders agree.
66. Despite this conclusion, the possible inclusion of s 107 as a shareholder decision-making right will be discussed later with s 117 to determine whether including it would be consistent with the purpose of the definition.

Section 117

67. In respect of s 117, once the relevant resolution is called for by a company proposing to take action affecting the rights attached to shares, the affected shareholders can vote in a special resolution on that particular action. This could be seen to be a right to "vote or participate" in that action (if it relates to the relevant decision-making).
68. However, it could be argued that the affected shareholders are not involved or taking part in the decision-making. The phrase "vote or participate" could be read in a limited way, as relating to substantive voting or participation rights, rather than to contingent rights that only arise temporarily when a company proposes to take a certain action.
69. The Commissioner considers that the definition of a "shareholder decision-making right" is capable of being given a broad or a narrow meaning. The broader interpretation which would include any rights (ie, including protective rights) is arguably the more natural meaning. However, a narrower meaning which restricts the definition to substantive rights is also available. The question is which of these interpretations best accords with Parliament's purpose.

How should the definition of "shareholder decision-making right" be interpreted?

70. Section 5 of the Interpretation Act 1999 provides that the meaning of an enactment must be determined from its text and in the light of its purpose. The Supreme Court supported a purposive approach to statutory interpretation in *Commerce Commission v Fonterra Co-operative Group Ltd* [2007] NZSC 36, [2007] 3 NZLR 767 at [22] to [24]. Tipping J noted at

[22] that even if the meaning of text appears plain, it should always be cross-checked against purpose. This includes cross-checking against the immediate and general legislative context and any social, commercial or other objective of the Act. See also *CIR v Alcan NZ Ltd* [1994] 3 NZLR 439 (CA) at 444 and *CIR v Auckland Harbour Board* (2001) 20 NZTC 17,008 (PC) at [14] and [15].

71. However, any purposive interpretation must be available on the words used in the provision. This is supported by comments made by Blanchard J in *Stiassny v CIR* [2012] NZSC 106, [2013] 1 NZLR 453. Blanchard J noted at [23] that the purpose of a provision may be a guide to its meaning and intended application. But, in most cases, the only evidence of that purpose is in the detailed wording of the provision. His Honour considered that the safest method is to read the words in their "most natural sense".
72. The courts will seek to interpret legislation in a way that avoids absurdity or unworkability where possible (see *Alcan* at 446; *Frucor Beverages Ltd v Rio Beverages Ltd* [2001] 2 NZLR 604 (CA) and *Skycity Auckland Ltd v Gambling Commission* [2007] NZCA 407, [2008] 2 NZLR 182). And in *Contract Pacific Ltd v CIR* [2010] NZSC 136, [2011] 1 NZLR 302 the Supreme Court undertook a "commonsense and practical approach" to the interpretation of legislation at [24] to [29]. J F Burrows and R I Carter, *Statute Law in New Zealand* (4th ed, LexisNexis, Wellington, 2009) state at 329:

Moreover, if the most natural grammatical interpretation of the text leads to a result that is thoroughly impractical, the court may strive to find an interpretation, even if not the most natural, which is practical and sensible. Words may thus be strained to this end ...
73. Burrows and Carter state further at 332:

... there is only so far words will stretch. If the words of the Act are plain and can have only one meaning, the accepted doctrine is that a court must simply apply them even if the result is inconvenient or unjust. However, the more undesirable the result, the more the interpreter will question whether that "plain" meaning is the only possible one, and whether an acceptable alternative construction may be found. It is all a question of degree: there may indeed be extreme cases where the natural meaning of the text leads to a result so absurd that a court is prepared to do actual violence to the words to avoid it.
74. In *Frucor Beverages* Thomas J held at [29] that a literal interpretation of the legislation in that case would have led to "anomalous, illogical and futile" results and "unworkable or inconvenient consequences". He stated at [29] that, where the legislative purpose of the statute is clear, the provision should not be reduced

to a nullity by a literal adherence to the language, unless the language is “intractable”. The subsequent Supreme Court decisions referred to above support this approach.

75. The concept of “absurdity” has a wide meaning. The concept includes results which are “unworkable or impracticable, inconvenient, anomalous or illogical, futile or pointless, artificial, or productive of a disproportionate counter-mischief” (per Thomas J in *Frucon*). However, there are other requirements before the courts will strive to interpret legislation to avoid absurdity. The legislative purpose must be clear. The court must be satisfied that the absurdity would frustrate that purpose. And, before the court could seek to avoid absurdity, it must be satisfied that the statutory language is not “intractable”. The legislative words used must be capable of including the preferred meaning.
76. It was earlier concluded that both a broader and narrower meaning is available on the words used in the definition of a shareholder decision-making right. Given the above approach to statutory interpretation taken by the courts, the following analysis considers:
- the legislative purpose of the definition of a shareholder decision-making right;
 - whether an absurdity arises if the rights under ss 107 and 117 of the CA 1993 are included in the definition; and
 - which interpretation best accords with Parliament’s purpose.

What is the purpose of the definition of a shareholder decision-making right?

77. Section YA 1 of the ITA 2007 provides that a person’s “voting interest” in a company is determined under ss YC 2 to YC 20. Section YC 2 defines “voting interests” as follows:

YC 2 Voting interests

Percentage of shareholder decision-making rights

- (1) A person’s voting interest in a company equals the percentage of the total shareholder decision-making rights for the company carried by shares or options held by the person.

When decision-making rights vary

- (2) Despite subsection (1), if the percentage of shareholder decision-making rights for a company carried by shares or options held by any person differs as between the types of decision-making listed in the definition of shareholder decision-making right, the person’s voting interest in the company equals the average of those differing percentages.

78. Section YC 3 defines “market value interests” as follows:

YC 3 Market value interests

Percentage of market value

- (1) A person’s market value interest in a company equals the percentage of the total market value of shares and options over shares in the company that the market value of shares and options over shares in the company held by the person represents.

Adjustments for options

- (2) For the purposes of subsection (1), the market value of any share in a company that is subject to an option is calculated having regard to the terms of the option.

79. At first glance it seems that the calculation of a person’s voting interest in a company relates to their substantive voting rights in the company. A different calculation, concerning the percentage of the total market value of shares and options over shares in the company that the person holds, is made under the “market value interest” definition.
80. The calculation of market value interests generally arises where a person’s interest in a company is not accurately reflected by measuring voting interests. For present purposes, it is sufficient to note that this alternate test, which applies in certain situations, focuses on the percentage of the market value of the shares and options in the company that the person holds. The difference between these two tests is that one relates to what is essentially voting power and the other relates to the proportion of the total market value of the company’s shares and options a person holds.
81. The meaning of a “shareholder decision-making right” is important for determining how a person’s “voting interest” in a company (rather than their market value interest) is determined.
82. There is no pre-legislative or other commentary on the definition of a “shareholder decision-making right”, either from when the definition was first enacted or when any subsequent minor wording alterations were made. However, the purpose of the definition can be determined by considering the Act in a wider sense, in terms of the relevant provisions in the ITA 2007 that refer to shareholder decision-making rights.
83. The origin of the definition of “shareholder decision-making right” was the direct control interest test in the controlled foreign company (CFC) rules (originally s 245C of the Income Tax Act 1976). The definition of “shareholder decision-making rights” was then contained in s 8B of that Act. Sections 8A to 8F were inserted by s 7 of the Income Tax Amendment Act

- (No 2) 1992, which was before the enactment of the CA 1993.
84. Under s 245C(1), a foreign company was a CFC if (relevantly) a group of five or fewer persons resident in New Zealand had:
- a control interest in the company that was greater than 50%; or
 - the power to control the exercise of the company's shareholder decision-making rights "and thereby to ensure that the affairs of the company are conducted in accordance with the wishes of that group".
85. Determining a person's direct control interest was initially provided for in s 245C(4). A person's direct control interest in a foreign company was the highest percentage held in terms of several factors (including shares held and rights to vote or participate in decision-making).
86. As noted above, s 245C(1) of the Income Tax Act 1976 referred to persons who had the power to control the exercise of the company's shareholder decision-making rights "and thereby to ensure that the affairs of the company are conducted in accordance with the wishes of that group". Similarly, in the 2004 and 2007 Income Tax Acts the equivalent wording was amended in s EX 1(1) (c) to refer to those who can control the exercise of the shareholder decision-making rights for the company and, as a result, "control the company's affairs".
87. *International Tax Reform Full Imputation Part 2* (Report of the Consultative Committee on Full Imputation and International Tax Reform, July 1988) states:
- 3.2.1 The attributes of a company which are critical for the purposes of calculating control and income interests are the **rights or powers which give the holders the ability to receive or control the disposition of the company's income or capital**. In general, these rights or powers attach to shares and are held by the shareholders of the company. **Different classes of shares may, however, have a wide variety of rights attached to them so that it is not sufficient to focus on the percentage of the shares held by a person.** ...
- [Emphasis added]
88. The references to "shareholder decision-making rights" and other control interests reflected the desire for a control test to refer to the rights and powers conferred on shareholders to receive or control the disposition of the company's income or capital. As set out above, the relevant provisions referred to shareholders who had the power to control the exercise of the company's shareholder decision-making rights "and thereby to ensure that the affairs of the company are conducted in accordance with the wishes of that group".
89. These references to controlling the company's income and capital and ensuring that the company's affairs are conducted in accordance with the wishes of that group indicate that shareholder decision-making rights were intended to be substantive rights to vote. This would not include protective rights that are contingent on particular events and only temporarily give rise to rights when a company proposes a particular action.
90. In *Taxation Policy – Business Tax Policy* (A statement on Government Tax Policy, Policy Advice Division of Inland Revenue and The Treasury, July 1991) the (then) proposed changes to the rules for measuring an interest in a company are explained. That paper stated:
- Measuring an interest in a company under the new rules**
- To the extent practicable, a common measure of a shareholder's economic interest in a company would apply for the purposes of:
- the loss carry-forward rules in section 188 of the Act
 - the credit continuity rules under the imputation and associated regimes. These rules govern eligibility to carry-forward imputation, brand equivalent tax and dividend withholding payment credits and are discussed in Chapter 9
 - rules that govern eligibility for two or more companies to be treated as one taxpayer under the consolidation option outlined in Chapter 5
 - the loss-offset rules in section 191 of the Act (this and the rules in relation to consolidation are hereafter referred to jointly in this Chapter as "commonality" rules).
- In the light of the problems associated with existing rules to measure a shareholder's interest in a company, from the 1992/93 income year a shareholder's interest in a company's tax losses or credits will be measured primarily **by reference to the percentage of voting power held by that person in relation to decision making by the company. Apart from measuring an interest by reference to market value, voting power is seen as the best proxy for a measure of a shareholder's beneficial interest in the losses or credits of a company and it will often be relatively simple to apply. By exercising voting power, a shareholder can protect its position relative to other shareholders and can ensure appropriate access to the earnings of the company when they are distributed.**
- [Emphasis added]
91. The paper referred to situations where both voting interests and market value interests might be taken into account:
- Where voting rights in relation to a shareholder's interest differ as between the different types of decision-making described in the previous paragraph,

the interest would be determined as the percentage it represents of the market value of all interests in the company, as well as percentage of voting power. Because the percentage of voting power differs between different types of decisions, each measure of voting power would be applied independently and the continuity threshold would have to be satisfied in relation to each measure. Resort is made to a measure based on market value because the differing voting rights may result in voting power giving an unreliable indication of a shareholder's economic interest in a company's losses or credits.

There will be other circumstances where voting power is unlikely to give an accurate measure of shareholders' interests. In these circumstances a shareholder's interest in a company would be computed by reference to both the market value of that interest and its voting power for the purposes of applying the loss and credit carry-forward provisions and the commonality rules. If the minimum continuity or commonality of ownership threshold under either measure is not satisfied, eligibility for loss carry-forward and/or offset would be forfeited.

Broadly, a shareholder's interest would be measured by reference to its market value and its voting power where:

- a shareholder has an entitlement to a certain proportion of company profits which it can be ascertained is different from its voting power and can veto any alteration in that entitlement
- the company or its shareholders, have issued options, other than certain options over listed company shares, options to acquire shares at their market value, or options issued by shareholders without the company's knowledge
- the company has issued shares (other than fixed rate dividend shares) the returns on which are guaranteed by a third party
- the shares have been subject to an arrangement with the purpose or effect of defeating the intent and application of the credit and loss carry-forward rules or the loss offset and consolidation provisions.

Where any of the above tests is triggered, the interests described (such as options) would be taken into account in determining the percentage of the market value of a company held by any share or option holder.

92. The above comments all indicate that determining a shareholder's interest in a company was intended to focus on the voting power held by that shareholder. If a market value circumstance arose, reference was then made to the percentage of the market value of shares in the company that are held by the person—regardless of voting power.

93. Further support for a conclusion that protective contingent rights are not included in the measurement of a person's "voting interest" is found in comments in a government discussion document relating to the introduction of the financial arrangements rules. Although that document does not concern the meaning of "voting interests", it provides some helpful comments on measuring a person's ownership of a company in terms of the debt/equity boundary. The *Consultative Document on Accrual Treatment of Income and Expenditure* (Consultative Committee on Accrual Tax Treatment of Income and Expenditure, October 1986) states at [4.2]:

An equity instrument carries with it elements of ownership whereas a debt instrument is more limited in the sense that it constitutes evidence of a loan, advance or credit facility. The debt/equity distinction thus rests on the presence or absence of ownership of the underlying assets. **Ownership has two key features:**

- a **management control – owners exercise power over the way resources of a business are employed; and**
- b **share in the risk of the enterprise – the claim of owners to the return from the resources of a business is limited to the residual return after all payments to creditors have been met. This risk manifests itself in two ways:**
 - i the return to owners varies with the profits derived from employing resources; and
 - ii if the resources are sold and the business or investment is wound up, owners receive the residual after all payments to creditors have been met.

These criteria can be used to draw a distinction between debt and equity. Thus, in general, holders of equity instruments have some control over the affairs of the business concerned; a return which varies with the business's profitability; and a residual claim on the assets of the business after the claims of all other creditors have been met. **Holders of debt instruments, on the other hand, generally have no formal rights to participate in the business's decision-making; a return which does not vary with the business's profitability; and a prior claim over equity holders on its assets.**

While these distinguishing characteristics serve as a general guide, in practice, debt and equity instruments can be virtually interchangeable. Each can have some of the characteristics of the other. **Some debt instruments have an element of management control (eg secured debentures with an associated trust deed) and the return on debt instruments can vary. Similarly, some equity instruments carry negligible management control and/or provide a constant return (eg preference shares).**

[Emphasis added]

94. Some equity instruments (for example, preference shares) may exhibit characteristics that are more in the nature of debt than equity. Such shares are likely to have a preferential fixed return but have no interest in the losses or profits of a company. The holders of such shares do not obtain returns that vary with the profits of the company or exercise any power over the way in which resources are employed. Section 117 of the CA 1993 would still apply to these types of shares. Section 117 provides those shareholders with protection against certain actions that a company may take. However, this does not give those shareholders any control over the company, in terms of substantive voting rights.
95. Consistent with this view, s YC 6 specifically excludes an “excluded fixed rate security” and an “excluded option” from the voting interest calculations in s YC 2 (other than in circumstances involving the calculation of market value interests for the purposes of the credit continuity provisions). Essentially, these are instruments that confer no substantive voting rights. An excluded fixed rate security is a security that provides a fixed rate return and confers no shareholder decision-making rights on the holder, other than protective rights. An excluded option includes an option issued on arm’s length terms that carries no shareholder decision-making rights, other than protective rights.
98. Any rights to vote or participate under s 107 and s 117 of the CA 1993 are contingent on the company taking particular actions (or proposing to take such actions), and only temporarily arise for the duration of the vote on that particular proposed action.
99. In such uncertain circumstances, difficulties arise in calculating the percentage of voting interests held by the shareholders of that company at a point in time.
100. Questions could arise if contingent and temporary protective rights were a “shareholder decision-making right” when invoked, including:
- When the relevant resolution or unanimous assent is requested, do the affected shareholders have 100 percent of the rights to vote on or participate in that particular decision? If so, this could temporarily give those shareholders all the voting interests on that decision.
 - At that time, would the affected shareholders’ temporary rights then be included in calculating the percentage of the total rights held by all voting shareholders? If so, this could alter the calculation of voting interests in the company for all shareholders.
101. The questions raised could mean that non-voting shareholders may, at times, hold between them decision-making rights in the company that are included in calculating the percentage of voting interests held by all shareholders. Taken to an extreme, it might affect the following parts of the ITA 2007:

Summary

96. The Commissioner considers that the definitions of “shareholder decision-making right” and “voting interest” were intended to relate to substantive voting rights held by the owners of a company. Shareholders who hold substantive voting rights for the relevant types of decision-making can share in the control over the company’s decisions regarding its capital and resources. Non-voting shares may be included in a calculation of ownership and control in circumstances where market value interests are calculated, rather than voting interests (which are specifically provided for in the ITA 2007).

Does the inclusion of rights under ss 107 and 117 lead to absurdity?

97. If an interpretation were taken that s 107 or s 117 rights could be a “shareholder decision-making right”, this would occur at particular points in time. Under s 107, this would be the request for shareholder approval for a company to take an action otherwise than in accordance with the CA 1993. Under s 117, this would be the calling of the resolution to vote on the company’s proposed action.
102. The rights in ss 107 and 117 are provided to all shareholders of a company and cannot be negated by a company constitution. Similar rights to s 117 might also be included in an option, the company constitution or share issue terms. The Commissioner considers that including these types of protective rights in the definition of a shareholder decision-making right could lead to unworkable consequences.

That is, every share issued by a company could carry a voting interest at some point in time, potentially affecting the calculations in the above regimes in the ITA 2007.

Which interpretation best accords with the legislative intent?

103. The definition of a “shareholder decision-making right” does not use words such as “substantive” when referring to shareholders’ rights to vote or participate in certain decisions. The issue was whether a limitation can be read into the definition.
104. As concluded at [96] above, the Commissioner considers that the definitions of “voting interest” and “shareholder decision-making right” were intended to reflect shareholders’ substantive voting rights in a company, in terms of the level of control they have over the company’s decisions and resources. A person’s voting interest in a company was not intended to include protective rights that are contingent and temporary in nature, and which might never arise. The Commissioner considers that the unworkability and absurdity that arises if these types of rights are included as a shareholder decision-making right means that the narrower interpretation should be preferred. The Commissioner considers that this interpretation is available on the words used in the definition.
105. Therefore, the Commissioner considers that the definition of a “shareholder decision-making right” does not include contingent rights of a protective nature, such as those arising when a company proposes to undertake a certain action under ss 107 or 117 of the CA 1993. The Commissioner considers that a shareholder decision-making right is a substantive voting or participation right. The same conclusion also applies to rights of a similar nature to s 117 that are contained in a company constitution, the terms of issue of a share, option over a share or the NZX rules.

Conclusion

106. The Commissioner considers that ss 107 and 117 of the CA 1993 do not give rise to a shareholder decision-making right.
107. Although rights arising under those provisions could be interpreted as being a right to vote or participate in some decisions, such an interpretation does not accord with Parliament’s purpose in enacting the definition. An interpretation including these contingent and temporary rights could lead to unworkable outcomes when calculating a person’s voting interests in some situations. The conclusion that the relevant rights to vote or participate should be substantive voting

rights is considered to be consistent with Parliament’s purpose that the persons holding the voting interests in a company are those that have a degree of control over the company’s decisions, and not those who may obtain protective rights temporarily.

References

Subject references
Income Tax; Shareholder decision-making right; Voting interest
Legislative references
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Income Tax Act 1976 – s 245C
Companies Act 1993 – ss 36, 107, 117
Case references
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<i>CIR v Auckland Harbour Board</i> (2001) 20 NZTC 17,008 (PC)
<i>Commerce Commission v Fonterra Co-operative Group Ltd</i> [2007] NZSC 36, [2007] 3 NZLR 767
<i>Contract Pacific Ltd v CIR</i> [2010] NZSC 136, [2011] 1 NZLR 302
<i>Cumbrian Newspapers Group Ltd v Cumberland and Westmorland Herald Newspaper and Printing Co Ltd</i> [1987] Ch 1
<i>Frucor Beverages Ltd v Rio Beverages Ltd</i> [2001] 2 NZLR 604 (CA)
<i>IRC v Crossman</i> [1937] AC 26 (HL)
<i>Skycity Auckland Ltd v The Gambling Commission</i> [2007] NZCA 407, [2008] 2 NZLR 182
<i>Stiassny v CIR</i> [2012] NZSC 106, [2013] 1 NZLR 453
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J F Burrows and R I Carter <i>Statute Law in New Zealand</i> (4th ed, LexisNexis, Wellington, 2009)
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APPENDIX – LEGISLATION

Income Tax Act 2007

1. “Voting interest” is defined in s YA 1 as follows:

voting interest—

 - (a) means, for a person and a company and a time, the percentage voting interest that the person is treated as holding in the company at the time under sections YC 2 to YC 20 (which relate to the measurement of company ownership):
2. Section YC 2 provides:

YC 2 Voting interests

Percentage of shareholder decision-making rights

 - (1) A person’s voting interest in a company equals the percentage of the total shareholder decision-making rights for the company carried by shares or options held by the person.

When decision-making rights vary

 - (2) Despite subsection (1), if the percentage of shareholder decision-making rights for a company carried by shares or options held by any person differs as between the types of decision-making listed in the definition of shareholder decision-making right, the person’s voting interest in the company equals the average of those differing percentages.
3. Section YC 3 provides:

YC 3 Market value interests

Percentage of market value

 - (1) A person’s market value interest in a company equals the percentage of the total market value of shares and options over shares in the company that the market value of shares and options over shares in the company held by the person represents.

Adjustments for options

 - (2) For the purposes of subsection (1), the market value of any share in a company that is subject to an option is calculated having regard to the terms of the option.
4. A “shareholder decision-making right” is defined in s YA 1 as follows:

shareholder decision-making right – means a right, carried by a share issued by a company or an option over a share issued by a company, to vote or participate in any decision-making concerning—

 - (a) a dividend or other distribution to be paid or made by the company, whether on a liquidation of the company or otherwise, excluding decision-making undertaken by directors acting only in their capacity as directors; or
 - (b) the constitution of the company; or
 - (c) a variation in the capital of the company; or
 - (d) the appointment of a director of the company

Companies Act 1993

5. Section 2 sets out the definition of “entitled persons” as follows:

entitled person, in relation to a company, means—

 - (a) a shareholder; and
 - (b) a person upon whom the constitution confers any of the rights and powers of a shareholder:
6. Section 36 provides:

36 Rights and powers attaching to shares

 - (1) Subject to subsection (2), a share in a company confers on the holder—
 - (a) the right to 1 vote on a poll at a meeting of the company on any resolution, including any resolution to—
 - (i) appoint or remove a director or auditor:
 - (ii) adopt a constitution:
 - (iii) alter the company’s constitution, if it has one:
 - (iv) approve a major transaction:
 - (v) approve an amalgamation of the company under section 221:
 - (vi) put the company into liquidation:
 - (b) the right to an equal share in dividends authorised by the board:
 - (c) the right to an equal share in the distribution of the surplus assets of the company.
 - (2) Subject to section 53, the rights specified in subsection (1) may be negated, altered, or added to by the constitution of the company or in accordance with the terms on which the share is issued under section 41(b) or section 42 or section 44 or section 107(2), as the case may be.
7. Section 107 provides:

107 Unanimous assent to certain types of action

 - (1) Notwithstanding section 52 but subject to section 108, if all entitled persons have agreed or concur,—
 - (a) a dividend may be authorised otherwise than in accordance with section 53:
 - (b) a discount scheme may be approved otherwise than in accordance with section 55:
 - (c) shares in a company may be acquired otherwise than in accordance with sections 59 to 65:
 - (d) shares in a company may be redeemed otherwise than in accordance with sections 69 to 72:
 - (e) financial assistance may be given for the purpose of, or in connection with, the purchase of shares otherwise than in accordance with sections 76 to 80:

- (f) any of the matters referred to in section 161(1) may be authorised otherwise than in accordance with that section.
- (2) If all entitled persons have agreed or concur, shares may be issued otherwise than in accordance with section 42 or section 44 or section 45.
- (3) If all entitled persons have agreed to or concur in a company entering into a transaction in which a director is interested, nothing in sections 140 and 141 shall apply in relation to that transaction.
- (4) For the purposes of this section, no agreement or concurrence of the entitled persons is valid or enforceable unless the agreement or concurrence is in writing.
- (5) An agreement or concurrence may be—
 - (a) a separate agreement to, or concurrence in, the particular exercise of the power referred to; or
 - (b) an agreement to, or concurrence in, the exercise of the power generally or from time to time.
- (6) An entitled person may at any time, by notice in writing to the company, withdraw from any agreement or concurrence referred to in subsection (5)(b) and any such notice shall have effect accordingly.
- (7) Where a power is exercised pursuant to an agreement or concurrence referred to in subsection (5)(b), the board of the company must, within 10 working days of the exercise of the power, send to every entitled person a notice in writing containing details of the exercise of the power.
- (8) If the board of a company fails to comply with subsection (7), every director of the company commits an offence and is liable on conviction to the penalty set out in section 374(1).

8. Section 117 provides:

117 Alteration of shareholder rights

- (1) A company must not take action that affects the rights attached to shares unless that action has been approved by a special resolution of each interest group.
- (2) For the purposes of subsection (1), the rights attached to a share include—
 - (a) the rights, privileges, limitations, and conditions attached to the share by this Act or the constitution, including voting rights and rights to distributions;
 - (b) pre-emptive rights arising under section 45;
 - (c) the right to have the procedure set out in this section, and any further procedure required by the constitution for the amendment or alteration of rights, observed by the company:

- (d) the right that a procedure required by the constitution for the amendment or alteration of rights not be amended or altered.
- (3) For the purposes of subsection (1), the issue of further shares ranking equally with, or in priority to, existing shares, whether as to voting rights or distributions, is deemed to be action affecting the rights attached to the existing shares, unless—
 - (a) the constitution of the company expressly permits the issue of further shares ranking equally with, or in priority to, those shares; or
 - (b) the issue is made in accordance with the pre-emptive rights of shareholders under section 45 or under the constitution of the company.

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 *Binding rulings: How to get certainty on the tax position of your transaction (IR 715)*. You can download this publication free from our website at www.ird.govt.nz

PRODUCT RULING BR PRD 13/11: MERIDIAN ENERGY LIMITED

This is a product ruling made under s 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling has been applied for by the Minister of State Owned Enterprises and the Minister of Finance, in their capacity as holders of all of the issued shares in Meridian Energy Limited (Meridian) on behalf of Her Majesty the Queen in Right of New Zealand (the Crown).

Taxation Laws

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

This Ruling applies in respect of ss CA 1(2), CB 1, CB 3, CB 4, CB 5, CD 1, CV 13, DB 23, DB 49, ED 1, EW 3, EW 5(13), EW 6(2), EW 31, EW 32(3), EW 35, FC 1, FC 2, HC 6, HC 17, the definition of “agreement for the sale and purchase of property or services” in s YA 1, and s YB 21.

The Arrangement to which this Ruling applies

The Arrangement is the sale of up to 49% of the ordinary shares (the Shares) in Meridian Energy Limited (Meridian), through the use of instalment receipts, by the Ministers of State Owned Enterprises and Finance (the Ministers) on behalf of Her Majesty the Queen in Right of New Zealand (the Crown) as vendor to purchasers (IR Holders), pursuant to the terms of the Retail Offer and the Institutional Offer contained in a combined Investment Statement and Prospectus (the Offer Document). For the avoidance of doubt, this Ruling does not apply to the Participating Iwi Offer contained in the Offer Document. This Ruling also does not apply to holders of Instalment Receipts to the extent to which the Shares to which those Instalment Receipts relate are held by an Australian trustee entity.

The purchase price will be paid in two instalments (the First Instalment and the Final Instalment). All Shares sold under the Offer Document (other than Shares sold to applicants whose address as recorded in the Instalment Receipt register (Registered Address) is in Australia) will be held in trust by a New Zealand trustee entity (the New Zealand

IR Trustee) until payment of the Final Instalment. Upon payment of the First Instalment, an IR Holder will receive an instalment receipt for each Share acquired under the Offer Document (the Instalment Receipt), which will be evidence of the IR Holder’s beneficial interest in that Share.

Further details of the Arrangement are set out in the paragraphs below.

1. The Ministers currently hold all of the Shares in Meridian on behalf of the Crown. The Crown is intending to sell up to 49% of the ordinary shares in Meridian under an initial public offering (the Offer). The purchase price payable per Share under the Offer (the Final Price) will be determined under an institutional book-build process prior to the allotment date of shares under the Offer (the Allotment Date).
2. The Final Price will be paid by investors in two instalments. The First Instalment is payable on application and the Final Instalment is payable approximately 18 months after the Allotment Date (the Final Instalment Payment Date). The Final Instalment will be the Final Price less the First Instalment. The Final Price offered to New Zealand Applicants pursuant to the Retail Offer will be capped (as described at para 7 below). No IR Holder has the ability to prepay any part of the Final Price.
3. On the Allotment Date, Shares sold by the Crown to each successful applicant (other than any applicant whose Registered Address is in Australia) (IR Holder) under the Offer will be transferred to the New Zealand IR Trustee and will be held by that New Zealand IR Trustee on behalf of and for the benefit of that IR Holder until payment of the Final Instalment. Pending payment of the Final Instalment, each IR Holder will be issued with Instalment Receipts by the New Zealand IR Trustee representing the beneficial interest of the IR Holder in the underlying Share.
4. Shares sold to each successful applicant whose Registered Address is in Australia will be transferred to an Australian trustee entity to be held subject to

a separate trust deed. This Ruling does not apply to holders of Instalment Receipts to the extent to which the Shares to which those Instalment Receipts relate are held by an Australian trustee entity. References in this Ruling to “IR Holders” exclude references to any such holder of Instalment Receipts.

5. The New Zealand IR Trustee will allot Instalment Receipts as directed by the Crown. The New Zealand IR Trustee will not be an “issuer” or a “promoter” under the Securities Act 1978.
6. The underlying Share will be held on trust subject to a security interest in favour of the Crown securing the obligation to pay the Final Instalment and, if applicable, default interest, enforcement costs and certain other payments. Upon payment of the Final Instalment, IR Holders will receive legal title to the underlying Shares and the Instalment Receipts will be cancelled.
7. The Final Price payable by New Zealand Applicants who are allocated Instalment Receipts and corresponding Shares in the Retail Offer will be capped at a certain amount. This means that such New Zealand Applicants who continue to hold their Instalment Receipts in the same registered name until the Final Instalment Payment Date may pay a lesser aggregate Final Price than participants in the Institutional Offer.
8. The price cap offered to such New Zealand Applicants encourages them to participate in the offer and hold their Instalment Receipts until the Final Instalment Payment Date. The capped price will not apply to other IR Holders (such as institutional investors who participate in the Offer or any investors who acquire Instalment Receipts after the Allotment Date).
9. “New Zealand Applicant” is defined in the Offer Document as an applicant who provides, in conjunction with their application to acquire Shares, a New Zealand IRD number, a New Zealand bank account number, a New Zealand address and a declaration that the applicant is:
 - a) in the case of an individual, a New Zealand citizen or permanent resident; or
 - b) in the case of a company, incorporated in New Zealand and the majority of its ultimate beneficial owners consists of persons who are New Zealand citizens or permanent residents; or
 - c) in the case of a trust, established in New Zealand and the majority of its ultimate beneficiaries consists of persons who are New Zealand citizens or permanent residents; or
 - d) in the case of any other legal entity, incorporated or established in New Zealand and the majority of its ultimate beneficial owners, beneficiaries or members consists of persons who are New Zealand citizens or permanent residents.
10. The Offer Document will contain “lowest price” wording. This wording will form part of the agreement between the Crown as vendor and each IR Holder as purchaser. The lowest price wording will provide that the lowest price that the parties (the Crown and each IR Holder) would have agreed on the date the agreement between them was entered into for the supply of each underlying Share on the Allotment Date is the (applicable) Final Price. The Offer, therefore, will give rise to two types of contract for sale and purchase of Shares:
 - a) one for New Zealand Applicants entitled to benefit from the price cap described above, which provides that those New Zealand Applicants who are allocated Instalment Receipts and corresponding Shares in the Retail Offer and who hold those Instalment Receipts to the Final Instalment Payment Date are entitled to pay the capped Final Price in respect of those Instalment Receipts; and
 - b) one for all other IR Holders, which provides for payment of the (potentially higher) Final Price in respect of Instalment Receipts held by those IR Holders, including New Zealand Applicants who acquired their Instalment Receipts other than pursuant to the Offer on the Allotment Date.
11. Meridian will apply for the Shares and the Instalment Receipts to be listed on the New Zealand and Australian stock exchanges (the NZX and ASX respectively). However, only the Instalment Receipts will be quoted on the exchanges until the Final Instalment Payment Date, after which the Shares will be quoted (and the Instalment Receipts will cease to be quoted).

Role of New Zealand IR Trustee

12. Legal title to the underlying Shares to which Instalment Receipts relate will be held by the New Zealand IR Trustee as trustee pursuant to a trust deed (the IR Trust Deed) between the Crown, Meridian and the New Zealand IR Trustee. The New Zealand IR Trustee will hold legal title to the underlying Shares on trust for IR Holders (who will hold the beneficial interest in the Shares) subject to a security interest in favour of the Crown. In this regard, cl 3.1 of the draft IR Trust Deed states:

Subject to clause 3.4, as soon as possible after the closing of the Offer (or at such later time as is contemplated in the Offer Document), the Crown will, provided any conditions to which the contract with the relevant Successful Applicant may be subject have been satisfied, and in consideration for receipt of the First Instalment and the obligation of the Holders of Instalment Receipts at the Final Instalment Record Date to pay the Final Instalment in accordance with the terms of the Offer and this Deed, transfer to the Trustee the Shares in respect of which there are Successful Applications by Successful Applicants to be held subject to the terms of the trusts set out in this Deed and will deliver to the Trustee certificate(s), if any, relating to those Shares. With effect from the time of that transfer:

- (a) the Security Interest shall be deemed to take effect; and
- (b) the Beneficial Interest shall vest in the person entitled to the Beneficial Interest in terms of the definition of that term in clause 1.1 and the appointment of the Trustee as the nominee of each such person pursuant to clause 4 shall take effect.

13. Each Instalment Receipt corresponds to a specific Share and each will be held by the New Zealand IR Trustee on a separate trust for the holder of the corresponding Instalment Receipt. Clause 4.1(a), 4.2 and 4.3 of the draft IR Trust Deed state:

4.1 Establishment

- (a) As from the date of registration of the transfer of a Share to the Trustee under clause 3.1, a Separate Trust in respect of each such Share shall be constituted by and subject to the terms and conditions of this Deed in favour of the Trustee as nominee for the relevant Successful Applicant and in favour of the relevant Successful Applicant as beneficiary, and the Trustee shall hold that Share which is the subject of that Separate Trust as nominee for the relevant Successful Applicant on the terms and conditions of this Deed.

...

4.2 Retention of Share

- (a) The Share the subject of a Separate Trust shall, during the Term of that Separate Trust, be held by the Trustee as nominee for the Holder of the Instalment Receipt which corresponds to the Share, but subject always to the Security Interest and this Deed. The provisions of this Deed which limit the rights of an Instalment Receipt Holder as holder of the Beneficial Interest are included for the purpose of giving effect to, and protecting, the Security Interest, and for no other purpose (other than where necessary to give effect to the requirements of Part 5A of the Public Finance Act 1989 or to the Crown's rights where a Holder misrepresents its status as a New Zealand Applicant (as defined in the Offer Document))

and do not impact upon or alter the status of the Trustee as the nominee for each Instalment Receipt Holder.

- (b) The holding of a Share on the trusts described in clause 4.2(a) is subject to the following qualifications:
 - (i) a Share may be retained by a Custodian or Sub-Custodian as nominee for the Trustee; and
 - (ii) the Trustee may have any certificates in relation to any Shares held in custody by any person on behalf of the Trustee.

4.3 Instalment Receipt Holders' rights and limits thereon

- (a) An Instalment Receipt Holder shall be entitled to the Beneficial Interest in each of the Shares corresponding to the Instalment Receipts registered in the name of such Holder.
- (b) Notwithstanding clause 4.3(a), the Beneficial Interest held by an Instalment Receipt Holder in any Share shall not:
 - (i) confer upon the Instalment Receipt Holder, other than as provided in this Deed, any right or power to require the transfer to it or any other person of the Share prior to it having paid the Final Instalment and any other amounts payable under this Deed by Cleared Payment in respect of that Share; or
 - (ii) entitle the Instalment Receipt Holder to any further assurance of that Beneficial Interest beyond that resulting from the Acceptance of the relevant Application (in the case of a Successful Applicant) or registration of the Instalment Receipt Holder in the Instalment Receipt Register (in the case of the Successful Applicant or any other Instalment Receipt Holder), and from the terms of this Deed.

14. The New Zealand IR Trustee will have various duties under the IR Trust Deed, including as described below in relation to dividends paid by Meridian on underlying Shares (Dividends), voting of those Shares and the transfer of the underlying Shares to IR Holders on payment of the Final Instalment.

15. Other key duties imposed on the New Zealand IR Trustee include:

- a) holding the Shares on trust for IR Holders;
- b) selling the underlying Shares to recover the Final Instalment owed to the Crown if an IR Holder defaults in payment of the Final Instalment and cancelling the relevant Instalment Receipts; and
- c) arranging the registration of transfers of title to Instalment Receipts (or arranging the refusal of such transfer in accordance with applicable laws or stock exchange listing requirements).

Dividends paid on Shares

16. Under the Trust Deed, each IR Holder will be entitled to receive Dividends paid on the underlying Shares to which that IR Holder's Instalment Receipts relate, together with any imputation credits attached to those Dividends. In the IR Trust Deed, the New Zealand IR Trustee, as registered holder of the Shares and acting in the interests of the IR Holder, agrees to ensure that payment of all Dividends will be made directly by Meridian to IR Holders, as if those IR Holders were the registered holders of the underlying Shares at the relevant time. Meridian undertakes to pay the Dividends directly to the relevant IR Holder. The New Zealand IR Trustee also agrees to take reasonable steps to confer on IR Holders the benefit of imputation credits attached to any Dividends or any other tax benefit permitted by the Act.

17. Clauses 16.1 and 16.4 of the draft IR Trust Deed state:

16.1 Entitlements to Dividends

Subject to clauses 16.7(a) and 18.4, if the Company pays a Dividend in respect of any Share at any time before the Final Instalment Payment Date, the Trustee shall hold the Dividend (and all its right, title and interest thereto) as a bare trustee for the relevant Eligible Instalment Receipt Holder on the terms set out in this Deed and shall (as registered holder of such Share and acting in the interests of the Eligible Instalment Receipt Holder):

- (a) in respect of a Dividend wholly or partly in cash, take all Reasonable Steps to cause the Company to pay such Dividend (or the cash portion) directly to the Eligible Instalment Receipt Holder; and
- (b) in respect of a Dividend wholly or partly other than in cash, take all Reasonable Steps to cause such Dividend (or the non-cash portion) to vest in the Eligible Instalment Receipt Holder,

and the Crown will procure the Company to provide the Trustee with all reasonable assistance to comply with this clause 16.1 and, in particular, prior to the Final Instalment Payment Date, to pay (or vest) Dividends directly to, or with, the relevant Eligible Instalment Receipt Holder.

16.4 Method of payment of Dividends

- (a) Subject to clauses 16.7(a) and 18.4, payment of any Dividend pursuant to clause 16.1(a) to an Eligible Instalment Receipt Holder in respect of the Shares corresponding to its Instalment Receipts may be made to the Eligible Instalment Receipt Holder as if that Holder was the registered holder of the Shares at such time and otherwise in the same manner and by the same means as applies to Shareholders (other than the Trustee), or by one of the methods described in clause 29.1.

- (b) The Trustee shall not retain for its own account any Dividends in respect of the Shares.
- (c) Payment of any Dividend in accordance with clause 16.4(a) may be effected through the Trustee, the Company, the Instalment Receipt Registrar, or, if this can be conveniently arranged, directly through the Share Registrar.
- (d) The payment of any Dividend to an Eligible Instalment Receipt Holder is at that Eligible Instalment Receipt Holder's risk.
- (e) Money earned by the Company or the Trustee on the amount of a Dividend pending clearance of a cheque or other collection by an Eligible Instalment Receipt Holder shall be for the benefit of the Company or the Crown, as the case may be.
- (f) If, for any reason, the Trustee is prevented from making a payment as provided in this clause 16.4 or in the case of a non-cash Dividend, if there are no Reasonable Steps which can be taken under clause 16.1(b), the Trustee shall continue to hold the Dividend in question as a bare trustee for the Eligible Instalment Receipt Holder and shall take or continue to take (subject to clause 16.8) all Reasonable Steps to transfer or make available the Dividend to that Eligible Instalment Receipt Holder.
- (g) The Trustee is not responsible to any person for any neglect or default on the part of the Company in relation to any matter dealt with in this clause 16.4.
- (h) The Crown will procure that the payment of any Dividend to an Eligible Instalment Receipt Holder pursuant to this clause 16 is made at the same time as payment by the Company or the Share Registrar of the equivalent Dividend is made to holders of Shares.
- (i) The Trustee or other person making payment of any Dividend under clause 16.4(c) may make, and account to the relevant tax authorities for, any withholding payments required by law.

18. If the New Zealand IR Trustee does receive a Dividend (i.e. the Dividend is not paid directly by Meridian to the IR Holder) and the New Zealand IR Trustee is prevented for some reason from paying the Dividend on to the IR Holder, the New Zealand IR Trustee will hold the amount of the Dividend as bare trustee for the relevant IR Holder and must continue to take all reasonable steps to transfer or make available the Dividend to the IR Holder.

19. If the New Zealand IR Trustee receives payment of a Dividend after the Final Instalment Payment Date then:

- a) if the payment is attributable to a Share for which the Final Instalment has been paid by a cleared payment, the New Zealand IR Trustee will hold the Dividend as bare trustee for the relevant IR Holder

and must take all reasonable steps to transfer the Dividend to that IR Holder; or

- b) if the payment is attributable to a Share for which there has been a default in the payment of the Final Instalment, the Dividend is to be applied in or towards payment of the amounts due to the Crown.
20. IR Holders will not be able to elect for Dividends to be retained by Meridian or the New Zealand IR Trustee and applied towards payment of Final Instalment.

Voting rights in respect of Shares

21. Each IR Holder will be invited to attend shareholder meetings of Meridian. However, until an IR Holder pays the Final Instalment and becomes registered as the holder of the underlying Shares, the IR Holder will not be entitled to vote the underlying Shares, directly, at such meetings (IR Holders will not be registered shareholders of Meridian in terms of the Companies Act 1993 or Meridian's constitution).
22. For each meeting of Meridian's shareholders prior to the Final Instalment Payment Date, the New Zealand IR Trustee will arrange for IR Holders to be sent a form inviting them to instruct the New Zealand IR Trustee as to the manner in which the votes attached to the underlying Shares are to be exercised by the New Zealand IR Trustee at that meeting.
23. The New Zealand IR Trustee has the power, and is required, to call for a poll on each resolution put to each meeting. If valid voting instructions are received within the specified time the New Zealand IR Trustee will vote the relevant Shares in accordance with the IR Holder's instructions. The New Zealand IR Trustee will request a meeting of shareholders if requested to do so by persons holding such number of Instalment Receipts as would entitle them to request a meeting if they were shareholders.
24. The New Zealand IR Trustee will not have the right to exercise votes for any Shares for which it does not receive voting instructions, nor will it have the right to vote those Shares at its own discretion.
25. The right of an IR Holder to give voting instructions to the New Zealand IR Trustee, and the obligation of the New Zealand IR Trustee to act in accordance with those instructions, will be able to be suspended in certain circumstances, reflecting the ownership requirements under the Public Finance Act 1989 (more particularly described in section 4.3 of the current draft of the Offer Document).

Payment of Final Instalment

26. Payment of the Final Instalment is due by IR Holders at 5pm on the Final Instalment Payment Date (expected to be approximately 18 months after the Allotment Date). Once payment of the Final Instalment is made, the New Zealand IR Trustee will transfer the underlying Share to the IR Holder within four business days of cleared payment being received by the Crown. On the transfer of the Share, the underlying security interest of the Crown will be extinguished and the relevant Instalment Receipt will be cancelled. IR Holders will then be entered onto Meridian's shareholder register. The Shares will then be traded on the ASX and NZX in place of the Instalment Receipts.

Default in payment of Final Instalment

27. If the Final Instalment is not paid when due, the New Zealand IR Trustee will be required to sell the underlying Share pursuant to the Crown's security interest and apply the proceeds in paying the Final Instalment on behalf of the IR Holder. Interest is payable by the IR Holder on the unpaid amount (being the Final Instalment, costs, expenses, taxes and other charges then owed) from the Final Instalment Payment Date. Any fees, costs, taxes, interest and similar charges are deducted from the sale proceeds with any surplus payable to the IR Holder. If the net proceeds are insufficient to pay the Final Instalment, then the New Zealand IR Trustee can recover the shortfall from the IR Holder on behalf of the Crown.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

- a) The Arrangement is an "agreement for the sale and purchase of property or services" (as defined in s YA 1), and a "financial arrangement" as defined in s EW 3.
- b) The Shares are each an excepted financial arrangement under s EW 5(13) and are part of that financial arrangement.
- c) Under s EW 6(2), any amounts that are solely attributable to the Shares will not be taken into account under the financial arrangements rules (as set out in Determination S24).
- d) For an IR Holder that is issued Instalment Receipts on the Allotment Date under the Offer and holds them until the Final Instalment Payment Date (Original IR Holder), the lowest price for s EW 32(3) is the applicable Final Price and no income or expenditure will arise under the financial arrangements rules in subpart EW.

- e) Any Dividend paid prior to the Final Instalment Payment Date will be taxable under s CD 1 as dividend income of the relevant IR Holder, provided that it is solely attributable to an “excepted financial arrangement” (as set out in Determination S24), and will not be taxable to the relevant IR Holder under ss CV 13 or HC 17.
- f) The transfer of legal title to the underlying Share to an IR Holder upon payment of the Final Instalment on the Final Instalment Payment Date will not give rise to income under any of ss CA 1(2), CB 1, CB 3, CB 4, or CB 5.
- g) For each IR Holder for whom a Share is revenue account property or “trading stock” (as that term is defined in s YA 1), the cost of that Share, upon its acquisition by the IR Holder on payment of the Final Instalment, for s DB 23 and s DB 49 respectively, is:
 - i) in the case of an Original IR Holder, the aggregate of the First Instalment and the (applicable) Final Instalment paid by that Original IR Holder; and
 - ii) in the case of any other IR Holder, the aggregate of the amount paid by that IR Holder to acquire the Instalment Receipt to which that underlying Share relates from another IR Holder, and the Final Instalment paid by the IR Holder.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 19 September 2013 and ending on 19 September 2016.

This Ruling is signed by me on the 19th day of September 2013.

Howard Davis
Director (Taxpayer Rulings)

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.

SPECIAL DETERMINATION S24: APPLICATION OF THE FINANCIAL ARRANGEMENTS RULES TO THE SALE OF SHARES IN MERIDIAN BY THE CROWN

This determination may be cited as Special Determination S24: “Application of the financial arrangements rules to the sale of shares in Meridian by the Crown”.

1. Explanation (which does not form part of the determination)

1. This determination relates to an arrangement involving the sale of up to 49% of the ordinary shares (the Shares) in Meridian Energy Limited (Meridian) by the Minister of State Owned Enterprises and the Minister of Finance on behalf of Her Majesty the Queen in Right of New Zealand (the Crown) as vendor to purchasers (IR Holders), pursuant to the terms of the Retail Offer and the Institutional Offer contained in a combined Investment Statement and Prospectus (the Offer Document).
2. For the avoidance of doubt, this Determination does not apply to the Participating Iwi Offer contained in the Offer Document. This determination also does not apply to holders of Instalment Receipts to the extent to which the Shares to which those Instalment Receipts relate are held by an Australian trustee entity.
3. The purchase price will be paid in two instalments (the First Instalment and the Final Instalment). All Shares sold under the Offer Document (other than Shares sold to applicants whose address as recorded in the Instalment Receipt register (Registered Address) is in Australia) will be held in trust by a New Zealand trustee entity until payment of the Final Instalment. Upon payment of the First Instalment, an IR Holder will receive an instalment receipt for each Share acquired under the Offer Document (the Instalment Receipt), which will be evidence of the IR Holder’s beneficial interest in that Share.
4. Instalment Receipts will be tradable and are expected to be listed on the New Zealand and Australian stock exchanges. The Final Instalment will be payable by the holder of the Instalment Receipt on the Final Instalment Payment Date (which will be approximately 18 months after the Instalment Receipts are issued).
5. IR Holders will be entitled to receive dividends paid by Meridian on the underlying Shares. If the Final Instalment is not paid on time, penalty interest may be charged.
6. The arrangement is the subject of product ruling BR Prd 13/11 issued on 19 September 2013, and is fully described in that ruling.
7. The arrangement for the sale of the Meridian Shares is a financial arrangement and an “agreement for the sale and purchase of property or services” (as defined in s YA 1 of the Income Tax Act 2007). The Meridian Shares are excepted financial arrangements, as defined in s EW 5(13), and form part of that financial arrangement.
8. An amount that is solely attributable to an excepted financial arrangement described in any of ss EW 5(2) to (16) is not an amount taken into account under the financial arrangements rules. This determination prescribes the method to be used for determining the amount that is solely attributable to the Shares.

2. Reference

This determination is made under s 90AC(1)(h) of the Tax Administration Act 1994.

3. Scope of determination

This determination applies to the sale of Meridian Shares by the Crown, the sale or purchase of Instalment Receipts by IR Holders on the relevant stock exchange and the acquisition of the Shares by the IR Holders on payment of the Final Instalment.

4. Principle

1. The sale of the Meridian Shares is a financial arrangement and an “agreement for the sale and purchase of property or services” (as defined in s YA 1 of the Income Tax Act 2007). The Meridian Shares are excepted financial arrangements, as defined in s EW 5(13), and form part of that financial arrangement.

2. Any amount that is solely attributable to an excepted financial arrangement described in ss EW 5(2) to (16) is not an amount that is taken into account under the financial arrangements rules (s EW 6(2)).
3. This determination specifies that the amounts that are solely attributable to the Meridian Shares, which are not taken into account under the financial arrangements rules, are:
 - a) any dividends paid by Meridian in relation to the underlying Shares; and
 - b) any gain or loss made by an IR Holder who buys or sells an Instalment Receipt on the stock exchange or who receives the Shares on payment of the Final Instalment.
4. Any penalty interest charged for late payment of the Final Instalment will not be solely attributable to the Meridian Shares.
5. Due to the amounts set out in (3) being solely attributable to an excepted financial arrangement (the Meridian Shares), no income or expenditure will arise for any IR Holder under the financial arrangements rules (other than an IR Holder who is required to pay penalty interest for the late payment of the Final Instalment). This is because the consideration paid or payable to the IR Holder will equal the consideration paid or payable by the IR Holder.
6. Any gain or loss made by an IR Holder may be subject to other provisions of the Income Tax Act 2007 (outside of the financial arrangements rules). Any IR Holder is required to fulfil their obligations under those other provisions of the Act.

5. Interpretation

This determination has no specialised terms that need to be defined further.

6. Method

1. The amounts that are solely attributable to the Meridian Shares are:
 - a) any dividends paid by Meridian in relation to the underlying Shares; and
 - b) any gain or loss made by an IR Holder who buys or sells an Instalment Receipt on the stock exchange or who acquires the Shares on payment of the Final Instalment.
2. All other amounts paid or payable under the arrangement, including any penalty interest charged for late payment of the Final Instalment, will not be solely attributable to the Meridian Shares.

7. Examples

These examples illustrate the application of the method set out in this determination. The figures and values used in these examples are indicative only and cannot be relied on as an indication of the expected value of Instalment Receipts or Meridian Shares.

Example A

An IR Holder acquires an Instalment Receipt under the Offer Document for \$2.00. The IR Holder sells the Instalment Receipt on the stock market to a third party for \$3.20. The IR Holder makes a realised gain from the sale of \$1.20. The IR Holder does not receive any dividends in the period that they are holding the Instalment Receipt.

The gain of \$1.20 is solely attributable to an excepted financial arrangement (the Meridian Shares) and is not taken into account under the financial arrangements rules.

Example B

A purchaser buys an Instalment Receipt on the stock market for \$3.20. The purchaser holds that receipt until the Final Instalment Payment Date, and pays the Final Instalment of \$1.80. The purchaser receives the Meridian Shares from the trust, which are valued at \$6.00 on the date of receipt. The purchaser therefore has an unrealised gain of \$1.00.

The purchaser also receives dividends from Meridian during the period that they hold the Instalment Receipt. The gain of \$1.00 and the dividends received from Meridian are solely attributable to an excepted financial arrangement (the Meridian Shares) and are not taken into account under the financial arrangements rules.

Example C

A purchaser buys an Instalment Receipt on the stock market for \$3.00. Three months later, the purchaser sells the Instalment Receipt on the stock market for \$2.60. The purchaser has a realised loss of \$0.40. The purchaser receives a dividend from Meridian during the period that they hold the Instalment Receipt.

The loss of \$0.40 and the dividend received from Meridian are solely attributable to an excepted financial arrangement (the Meridian Shares) and are not taken into account under the financial arrangements rules.

This Determination is signed by me on the 19th day of September 2013.

Howard Davis
Director (Taxpayer Rulings)

FOREIGN CURRENCY AMOUNTS – CONVERSION TO NEW ZEALAND DOLLARS

This article provides the exchange rates acceptable to Inland Revenue for converting foreign currency amounts to New Zealand dollars for the six months ending 30 September 2013.

The Income Tax Act 2007 (“2007 Act”) requires foreign currency amounts to be converted into New Zealand dollars applying one of the following methods:

- actual rate for the day for each transaction (including close of trading spot exchange rate on the day), or
- rolling 12-month average rate for a 12-month accounting period or income year (see the table **Currency rates 6 months ending 30 September 2013 – rolling 12-month average**), or
- mid-month actual rate as the basis of the rolling average for accounting periods or income years greater or lesser than 12 months (see the table **Currency rates 6 months ending 30 September 2013 – mid-month actual**).

Legislation enacted in September 2010 with effect from 1 April 2008 permits the Commissioner to set currency rates and approve methods of calculating exchange rates. The Commissioner can set rates for general use by taxpayers or for specific taxpayers. The Commissioner’s ability to set rates and approve methods applies in circumstances where the 2007 Act does not contain a specific currency conversion rule (sections YF 1(5) and (6)), or in circumstances where the 2007 Act provides a rate or method for currency conversion (section YF 2).

Inland Revenue uses wholesale rates from Bloomberg for rolling 12-month average, mid-month actual and end of month. These rates are provided in three tables.

To convert foreign currency amounts to New Zealand dollars for any country listed, divide the foreign currency amount by the exchange rate shown. Round the exchange rate calculations to four decimal places wherever possible.

If you need an exchange rate for a country or a day not listed in the tables, please contact one of New Zealand’s major trading banks.

Note: All section references relate to the 2007 Act.

Actual rate for the day for each transaction

The actual rate for the day for each transaction can be used in the following circumstances:

- where the 2007 Act does not provide a specific currency conversion rule, then foreign currency amounts can be

converted by applying the close of trading spot exchange rate on the date that the transaction which is required to be measured or calculated occurs (section YF 1(2))

- where a person chooses to use the actual rate for the day of the transaction when calculating their FIF income or loss when applying the comparative value method, fair dividend rate method, deemed rate of return method or the cost method (section EX 57(2)(a))
- where a person chooses to use the close of trading spot exchange rate to convert foreign income tax paid by a CFC (section LK 3(a)) or by a FIF where the attributable FIF income method is used (sections EX 50(8)–(9) and LK 3(a)).

Unless the actual rate is the rate for the 15th or the last day of the month, these rates are not supplied by Inland Revenue.

The table **Currency rates 6 months ending 30 September 2013 – month end** provides exchange rates for the last day of the month. These are provided for convenience to assist taxpayers who may need exchange rates on those days.

Currency rates 6 months ending 30 September 2013 – rolling 12-month average table

This table is the average of the mid-month exchange rate for that month and the previous 11 months, ie, the 12-month average. This table should be used where the accounting period or income year encompasses 12 complete months.

This table can be used to convert foreign currency amounts to New Zealand dollars for:

- FIF income or loss calculated under the comparative value method, the fair dividend rate method, the deemed rate of return method or cost method (section EX 57(2)(b)) for accounting periods of 12 months
- FIF income or loss calculated under the attributable FIF income method (section EX 50(3)(a)) for accounting periods of 12 months
- attributed CFC income or loss calculated under the CFC rules (section EX 21(4)(b)) for accounting periods of 12 months
- calculating the New Zealand dollar amount of foreign income tax under the CFC rules (section LK 3(b)) or under the FIF rules where the attributable FIF income method is used (sections EX 50(8)–(9) and LK 3(b)) for accounting periods of 12 months.

Currency rates 6 months ending 30 September 2013 – mid-month actual table

This table sets out the exchange rate on the 15th day of the month, or if no exchange rates were quoted on that day, on the preceding working day on which they were quoted. This table can be used as the basis of the rolling average where the accounting period or income year is less than or greater than 12 months (see Example 4). You can also use the rates from this table as the actual rate for any transactions arising on the 15th of the month.

This table can be used as the basis of the rolling average for calculating:

- FIF income or loss under the comparative value method, the fair dividend rate method, the deemed rate of return method or cost method (section EX 57(2)(b)) for accounting periods or income years of less than or greater than 12 months
- FIF income or loss calculated under the attributable FIF income method (section EX 50(3)(a)) for accounting periods of less than or greater than 12 months
- attributed CFC income or loss calculated under the CFC rules (section EX 21(4)(b)) for accounting periods of less than or greater than 12 months
- the New Zealand dollar amount of foreign income tax under the CFC rules (section LK 3(b)) or under the FIF rules where the attributable FIF income method is used (sections EX 50(8)–(9) and LK 3(b)) for accounting periods of less than or greater than 12 months.

Example 1

A taxpayer with a 30 September balance date purchases shares in a Philippine company (which is a FIF but does produce a guaranteed yield) on 6 September 2013. Its opening market value on 1 October 2013 or its closing market value on 30 September 2013 is PHP 350,000. Using the comparative value method and applying the actual rate for the day (section EX 57(2)(a)), the opening market value is converted as follows:

$$\text{PHP } 350,000 \div 35.9919 = \$9,724.41$$

(In this example, the rate selected is the month-end rate for September 2013 for PHP. Refer to the table “Currency rates 6 months ending 30 September 2013 – month end”.)

Example 2

A CFC resident in Hong Kong has an accounting period ending on 30 June 2013. Attributed CFC income for the period 1 July 2012 to 30 June 2013 is 200,000 Hong Kong dollars (HKD), which converts to:

$$\text{HKD } 200,000 \div 6.3913 = \$31,292.54$$

(In this example, the rate selected is the rolling 12-month average rate for June 2013 for HKD. Refer to the table “Currency rates 6 months ending September 2013 – rolling 12-month average”.)

Example 3

A resident individual with a 30 September 2013 accounting period acquires a FIF interest in a Japanese company on 1 October 2012 for 10,500,000 yen. The interest is sold in September 2013 for 10,000,000 yen. Using the comparative value method and applying section EX 57(2)(b), these amounts are converted as:

$$\text{JPY } 10,500,000 \div 75.9964 = \$138,164.43$$

$$\text{JPY } 10,000,000 \div 75.9964 = \$131,585.18$$

(In this example, the rolling 12-month rate for September 2013 has been applied to both calculations.)

Example 4

A CFC resident in Singapore was formed on 19 April 2013 and has a balance date of 30 September 2013. During the period 1 May 2013 to 30 September 2013, attributed CFC income of 500,000 Singaporean dollars was derived. For the conversion to New Zealand dollars the taxpayer chooses the method set out in section EX 21(4)(b).

1. Calculating the average monthly exchange rate for the complete months May–September 2013:

$$1.0264 + 1.0074 + 0.9854 + 1.0243 + 1.0322 = 5.0757$$

$$5.0757 \div 5 = 1.01514$$
2. Round exchange rate to four decimal places: 1.0151
3. Conversion to New Zealand currency:

$$\text{SGD } 500,000 \div 1.0151 = \$492,562.31$$

(In this example, the rates are from the table “Currency rates 6 months ending September 2013 – mid-month actual”, from May to September 2012 inclusive for SGD.)

Currency rates 6 months ending 30 September 2013 – rolling 12-month average

Currency	Code	15/04/2013	15/05/2013	15/06/2013	15/07/2013	15/08/2013	15/09/2013
Australia Dollar	AUD	0.7913	0.7962	0.8011	0.8078	0.8173	0.8251
Bahrain Dinar	BHD	0.3086	0.3103	0.3108	0.3104	0.3104	0.3099
Britain Pound	GBH	0.5189	0.5238	0.5248	0.5253	0.5254	0.5255
Canada Dollar	CAD	0.8184	0.8236	0.8247	0.8253	0.8281	0.8311
China Yuan	CNY	5.1375	5.1542	5.1475	5.1225	5.1058	5.0838
Denmark Kroner	DKK	4.7283	4.7511	4.7398	4.7084	4.6770	4.6649
Euporean Community Euro	EUR	0.6346	0.6375	0.6359	0.6315	0.6272	0.6255
Fiji Dollar	FJD	1.4656	1.4728	1.4727	1.4748	1.4815	1.4857
French Polynesia Franc	XPF	75.7392	76.0940	75.8996	75.3717	74.8487	74.6431
Hong Kong Dollar	HKD	6.3453	6.3803	6.3913	6.3813	6.3813	6.3712
India Rupee	INR	44.6153	44.8849	45.1276	45.3611	45.7596	46.2898
Indonesia Rupiah	IDR	7,851.5058	7,919.6108	7,964.7283	7,995.7692	8,060.0333	8,158.4967
Japan Yen	JPY	69.1612	71.0423	72.1944	73.4402	74.6783	75.9964
Korea Won	KOR	910.4685	913.0595	912.1790	908.9694	908.0382	904.4832
Kuwait Dinar	KWD	0.2306	0.2323	0.2329	0.2328	0.2329	0.2328
Malaysia Ringit	MYR	2.5277	2.5334	2.5352	2.5322	2.5435	2.5545
Norway Krone	NOK	4.7280	4.7449	4.7374	4.7271	4.7246	4.7337
Pakistan Rupee	PKR	78.3749	79.3225	79.7634	80.0082	80.5339	81.1460
Phillipines Peso	PHP	33.9327	33.9860	34.0916	34.1455	34.2675	34.3570
PNG Kina	PGK	1.7001	1.7155	1.7263	1.7311	1.7438	1.7576
Singapore Dollar	SGD	1.0142	1.0189	1.0194	1.0175	1.0189	1.0206
Solomon Islands Dollar*	SBD	3.3943	2.9501	2.4990	2.0387	2.0387	1.5592
South Africa Rand	ZAR	7.0792	7.1823	7.3010	7.3950	7.5130	7.6195
Sri Lanka Rupee	LKR	105.6995	106.0398	105.9503	105.5884	105.5884	105.3915
Sweden Krona	SEK	5.4604	5.4587	5.4303	5.3982	5.3868	5.3784
Swiss Franc	CHF	0.7695	0.7753	0.7748	0.7714	0.7680	0.7670
Taiwan Dollar	TAI	24.1508	24.3122	24.3533	24.3069	24.3048	24.2903
Thailand Baht	THB	25.0249	25.0592	25.0421	24.9721	24.9549	24.9868
Tonga Pa'anga*	TOP	1.3979	1.4060	1.4098	1.4132	1.4198	1.4242
United States Dollar	USD	0.8180	0.8226	0.8240	0.8227	0.8228	0.8214
Vanuatu Vatu	VUV	76.3726	76.8003	76.8003	76.7061	77.0489	77.3013
West Samoan Tala*	WST	1.8391	1.8472	1.8530	1.8536	1.8649	1.8750

Notes to table:

All currencies are expressed in NZD terms, ie, 1NZD per unit(s) of foreign currency.

The currencies marked with an asterisk * are not published on Bloomberg in NZD terms. However, these currencies are expressed in USD terms and therefore the equivalent NZD terms have been generated as a function of the foreign currency USD cross-rate converted to NZD terms at the NZDUSD rate provided.

The rates provided represent the Bloomberg generic rate (BGN) based on the last price (mid rate) at which the currency was traded at the close of the New York trading day. Where the date specified was not a trading day, then the rate reflects the last price on the preceding business day.

Source: Bloomberg CMPN BGN

Currency rates 6 months ending 30 September 2013 – mid-month actual

Currency	Code	15/04/2013	15/05/2013	15/06/2013	15/07/2013	15/08/2013	15/09/2013
Australia Dollar	AUD	0.8151	0.8326	0.8409	0.8581	0.8831	0.8795
Bahrain Dinar	BHD	0.3169	0.3107	0.3034	0.2944	0.3044	0.3065
Britain Pound	GBH	0.5499	0.5409	0.5126	0.5171	0.5162	0.5121
Canada Dollar	CAD	0.8621	0.8371	0.8183	0.8142	0.8320	0.8417
China Yuan	CNY	5.2000	5.0600	4.9300	4.7900	4.9400	4.9755
Denmark Kroner	DKK	4.8086	4.7653	4.4942	4.4578	4.5113	4.5604
Euporean Community Euro	EUR	0.6449	0.6396	0.6032	0.5978	0.6049	0.6116
Fiji Dollar	FJD	1.4950	1.5011	1.4706	1.4865	1.5232	1.5124
French Polynesia Franc	XPF	76.9556	76.3608	71.9575	71.2913	72.1401	72.9392
Hong Kong Dollar	HKD	6.5254	6.3959	6.2474	6.0582	6.2603	6.3052
India Rupee	INR	46.3020	44.9585	46.5563	46.4526	49.5886	51.6626
Indonesia Rupiah	IDR	8236.6600	7985.4500	7955.3300	7862.4200	8429.5200	9125.5400
Japan Yen	JPY	81.3500	84.2590	75.8370	77.9710	78.6120	80.7970
Korea Won	KOR	944.5067	920.2527	907.9036	875.7247	902.2449	883.0024
Kuwait Dinar	KWD	0.2396	0.2358	0.2279	0.2230	0.2295	0.2313
Malaysia Ringit	MYR	2.5770	2.4595	2.5094	2.4901	2.6533	2.6727
Norway Krone	NOK	4.8405	4.8187	4.6019	4.7331	4.7697	4.8222
Pakistan Rupee	PKR	82.6446	81.3008	79.3651	78.1250	82.6446	85.4701
Phillipines Peso	PHP	34.9873	33.7754	34.4911	33.9112	35.4663	35.6330
PNG Kina	PGK	1.8158	1.7590	1.7374	1.6856	1.8150	1.8731
Singapore Dollar	SGD	1.0417	1.0264	1.0074	0.9854	1.0243	1.0322
Solomon Islands Dollar*	SBD	0.1157	0.1148	0.1108	0.1103	0.1131	0.1127
South Africa Rand	ZAR	7.7376	7.6283	8.0063	7.7087	8.0667	8.0817
Sri Lanka Rupee	LKR	105.2632	103.0928	103.0928	102.0408	106.3830	107.5269
Sweden Krona	SEK	5.4009	5.4988	5.1737	5.2132	5.2538	5.3337
Swiss Franc	CHF	0.7829	0.7950	0.7415	0.7405	0.7477	0.7556
Taiwan Dollar	TAI	25.1457	24.6983	24.0378	23.2917	24.1860	24.1534
Thailand Baht	THB	24.4921	24.5251	24.6155	24.2996	25.2444	25.8980
Tonga Pa'anga*	TOP	1.4327	1.4280	1.4162	1.4140	1.4590	1.4585
United States Dollar	USD	0.8407	0.8241	0.8050	0.7808	0.8073	0.8131
Vanuatu Vatu	VUV	78.1250	78.1250	75.7576	74.6269	78.7402	79.3651
West Samoan Tala*	WST	1.8497	1.8611	1.8752	1.8188	1.9504	1.9644

Notes to table:

All currencies are expressed in NZD terms, ie, 1NZD per unit(s) of foreign currency.

The currencies marked with an asterisk * are not published on Bloomberg in NZD terms. However, these currencies are expressed in USD terms and therefore the equivalent NZD terms have been generated as a function of the foreign currency USD cross-rate converted to NZD terms at the NZDUSD rate provided.

The rates provided represent the Bloomberg generic rate (BGN) based on the last price (mid rate) at which the currency was traded at the close of the New York trading day. Where the date specified was not a trading day, then the rate reflects the last price on the preceding business day.

Source: Bloomberg CMPN BGN

Currency rates 6 months ending 30 September 2013 – month end

Currency	Code	30/04/2013	31/05/2013	30/06/2013	31/07/2013	31/08/2013	30/09/2013
Australia Dollar	AUD	0.8256	0.8297	0.8472	0.8889	0.8683	0.8896
Bahrain Dinar	BHD	0.3225	0.2995	0.2919	0.3010	0.2913	0.3129
Britain Pound	GBH	0.5512	0.5226	0.5088	0.5251	0.4984	0.5126
Canada Dollar	CAD	0.8620	0.8238	0.8141	0.8206	0.8144	0.8554
China Yuan	CNY	5.2700	4.8700	4.7500	4.8900	4.7300	5.0762
Denmark Kroner	DKK	4.8443	4.5579	4.4411	4.4751	4.3600	4.5759
Euporean Community Euro	EUR	0.6502	0.6112	0.5947	0.6002	0.5844	0.6135
Fiji Dollar	FJD	1.5214	1.4575	1.4529	1.5175	1.4738	1.5437
French Polynesia Franc	XPF	77.5813	72.9179	70.9765	71.6071	69.7621	73.2856
Hong Kong Dollar	HKD	6.6449	6.1695	6.0024	6.1924	5.9926	6.4374
India Rupee	INR	46.0586	45.2293	46.2461	48.2750	51.0792	51.8103
Indonesia Rupiah	IDR	8322.2800	7974.2100	7810.1700	8191.2800	8692.2100	9442.9600
Japan Yen	JPY	83.3310	79.8490	76.7260	78.1530	75.8700	81.5120
Korea Won	KOR	941.8600	898.6228	884.2300	896.2057	857.6573	892.8974
Kuwait Dinar	KWD	0.2434	0.2271	0.2209	0.2271	0.2205	0.2350
Malaysia Ringit	MYR	2.6009	2.4790	2.4673	2.5908	2.5529	2.6982
Norway Krone	NOK	4.9384	4.6627	4.6979	4.7050	4.7260	4.9918
Pakistan Rupee	PKR	84.0336	78.1250	76.9231	81.3008	80.6452	87.7193
Phillipines Peso	PHP	35.2162	33.8519	33.6730	34.7008	34.6471	35.9919
PNG Kina	PGK	1.8709	1.7145	1.6713	1.7773	1.7369	2.0007
Singapore Dollar	SGD	1.0538	1.0048	0.9810	1.0148	0.9851	1.0422
Solomon Islands Dollar*	SBD	6.1958	5.7798	5.6285	5.7819	5.4954	5.9960
South Africa Rand	ZAR	7.6793	8.0163	7.6461	7.8728	7.9438	8.3229
Sri Lanka Rupee	LKR	108.6957	100.0000	101.0101	105.2632	103.0928	109.8901
Sweden Krona	SEK	5.5502	5.2594	5.1842	5.2015	5.1158	5.3357
Swiss Franc	CHF	0.7949	0.7584	0.7312	0.7396	0.7188	0.7510
Taiwan Dollar	TAI	25.2221	23.7955	23.2500	23.9730	23.1222	24.5342
Thailand Baht	THB	25.0578	24.0980	24.0300	24.9610	24.8446	25.9287
Tonga Pa'anga*	TOP	1.4613	1.4154	1.3952	1.4367	1.4137	1.4779
United States Dollar	USD	0.8563	0.7946	0.7738	0.7985	0.7727	0.8300
Vanuatu Vatu	VUV	79.3651	76.9231	72.4638	77.5194	75.7576	80.0000
West Samoan Tala*	WST	1.8887	1.8096	1.7070	1.7615	1.8668	1.8601

Notes to table:

All currencies are expressed in NZD terms, ie, 1NZD per unit(s) of foreign currency.

The currencies marked with an asterisk * are not published on Bloomberg in NZD terms. However, these currencies are expressed in USD terms and therefore the equivalent NZD terms have been generated as a function of the foreign currency USD cross-rate converted to NZD terms at the NZDUSD rate provided.

The rates provided represent the Bloomberg generic rate (BGN) based on the last price (mid rate) at which the currency was traded at the close of the New York trading day. Where the date specified was not a trading day, then the rate reflects the last price on the preceding business day.

Source: Bloomberg CMPN BGN

NEW LEGISLATION

This section of the *TIB* covers new legislation, changes to legislation including general and remedial amendments, and Orders in Council.

ORDERS IN COUNCIL

INFORMATION-SHARING AGREEMENT BETWEEN INLAND REVENUE AND THE DEPARTMENT OF INTERNAL AFFAIRS – CONTACT DETAILS AS PART OF PASSPORT RENEWAL OR APPLICATION PROCESS

The Privacy (Information-Sharing Agreement Between Inland Revenue and Internal Affairs) Order 2013 approves a new information-sharing agreement between Inland Revenue and the Department of Internal Affairs. Under the agreement, Internal Affairs will provide Inland Revenue with all contact details that it has obtained as part of the adult passport application process. The agreement will enable Inland Revenue to match these contact details against those it holds for people in three specific groups:

- overseas-based student loan borrowers who are in default of their student loan repayments;
- liable parents living overseas who are in default of their child support payment obligations; and
- liable parents living overseas who are not in default of their child support payment obligations but whose contact details appear to be out of date.

Any information received by Inland Revenue relating to individuals outside of these three groups will be deleted within 30 days of receipt.

The objective of the information-sharing agreement is to obtain reliable and timely contact information to assist Inland Revenue's efforts to prevent and collect student loan defaults and child support debt from overseas-based borrowers and liable parents living overseas.

The Privacy Act 1993 provides a mechanism for the approval by Order in Council of information-sharing agreements between agencies. This is the first information-sharing agreement approved in accordance with Part 9A of that Act.

What information will be shared?

Only contact details supplied in applications for new or renewed adult passports will be shared under the agreement. This includes information necessary to identify and contact the person, and facilitate communication

between Inland Revenue and Internal Affairs. This information is shown in the table below.

Use	Data
Identifying the person	First name(s) Surname Date of birth
Contacting the person	Home address Passport delivery address Personal home telephone number Work telephone number Mobile phone number E-mail address
Communicating with Internal Affairs	Passport number

From time to time Inland Revenue may need to clarify the data received from Internal Affairs in order to verify the contact details of an individual. In these instances, Inland Revenue will use the passport number, supplied by Internal Affairs under the agreement, to clearly identify the individual.

How will the information be used?

Inland Revenue may use the personal information collected under the agreement to compare it with Inland Revenue's records to identify and then contact an individual overseas who is in default of their student loan or child support obligations. The information may also be used to contact a liable parent living overseas whose contact details appear to be out of date.

What actions may result from the receipt of the information shared under the agreement?

Once contact is made with an overseas-based borrower in default or a liable parent overseas in default and the individual's identity is confirmed, Inland Revenue can be expected to take steps to recover the overdue payments. This may include:

- requiring payment of overdue child support liability in full or student loan balance in full;
- requiring payment of the overdue student loan debt in full;

- requiring payment of part of the overdue student loan debt or overdue child support liability, with the remainder being paid under an instalment arrangement;
- requiring payment by instalment arrangement; or
- taking legal action.

The regulations came into effect on 3 October 2013. The approved information-sharing agreement can be found at www.ird.govt.nz/aboutir/agreements

Privacy (Information Sharing Agreement Between Inland Revenue and Internal Affairs) Order 2013 (SR 2013/374)

QUESTIONS WE'VE BEEN ASKED

This section of the *TIB* sets out the answers to some day-to-day questions people have asked. They are published here as they may be of general interest to readers.

QB 13/04: INCOME TAX – RETENTION MONEY

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

This question we've been asked is about ss BD 3, BD 4, CA 1, CB 1 and DA 1.

This item updates and replaces the item "Retention Moneys, Construction Contracts" published in *Public Information Bulletin* No 103, p 1 (March 1980). That item sets out when retention money due on construction projects should be returned as income and the timing of deductions for retention money payable to sub-contractors. The current relevance of this information was identified during a review of content published in *Public Information Bulletins* and *Tax Information Bulletins* before 1996. For more information about the review, please see "Review of Public Information Bulletins" in *Tax Information Bulletin* Vol 23, No 1 (February 2011).

This question we've been asked applies generally to business taxpayers for whom the payment, or the receipt, of retention money is on revenue account. This item applies to contracts generally and not only construction contracts.

Question

1. A contract to construct an asset provides that the customer will withhold a set percentage from any progress payment (say 10%) as security for the contractor delivering the work free of defects or omissions. The same term is in the sub-contract between the contractor and a sub-contractor engaged on the project.
2. When does the contractor:
 - derive as income the retention money the customer withholds; and
 - incur the expenditure of the retention money the contractor withholds from payments to the sub-contractor?

Answer

3. The contractor derives the retention money as income in the income year in which the works are complete and free of defects and omissions. That is the income year in which any repairs are completed and omissions rectified. That is when the income earning process

is completed and an enforceable debt is created. If payment is not to be made unless the work is certified by a third party, for example, by an engineer, the retention money is derived as income when that certificate is given. The same principle applies to derivation of income by the sub-contractor.

4. The contractor also incurs the expenditure of the retention money payment to the sub-contractor in the income year in which all repairs are completed and omissions rectified, because that is when the contractor becomes definitively committed to make the payment. It is this that determines when the expense is incurred and not the due date for the payment.
5. If the repairs and rectifications must be certified by a third party, for example, by an engineer, the contractor incurs the expenditure when that certificate is given as that is when the contractor becomes definitively committed to make the payment.

Explanation

6. "Retention money" can be described generally as "an amount withheld for an agreed period by a purchaser or a contractee as security against the failure to fulfil a contract" (*Shorter Oxford English Dictionary* (6th ed, Oxford University Press, New York, 2007)). In some cases, a contract may allow a customer to retain part of a contract payment until identified repairs are made or other breaches of the contract are remedied. It is common in the construction industry for contracts to provide for a retention amount, of a set percentage, to be withheld from each progress payment. These retentions give the customer some comfort that the works will be completed defect-free and to specification.
7. A contract may provide that money can be retained by a customer until a defect is remedied or other condition is satisfied – as is the case in the question and answer above. Some contracts require certification by a third party, such as an independent engineer, before retention money is payable. Alternatively, a contract may simply

provide that a set percentage of each progress payment will be retained by the payer until a future date. In that case the retention money is, in effect, a form of security for the payer against defects or inadequacies in the work becoming apparent during the retention period.

When is income recognised?

8. An amount of income must be allocated to an income year (s BD 3(1)), which will be the year in which it is “derived” unless that is altered by a specific timing provision in the Act (s BD 3(2)). In determining the time of derivation of income regard must be had to case law (s BD 3(3)). This is subject to an overriding rule that an amount is treated as being derived when credited to the account of a taxpayer or dealt with in some other way in their interest or on their behalf (s BD 3(4)).
9. An amount paid to a contractor, or sub-contractor, in the business of constructing assets or providing other contract services is income (ss CA 1 and CB 1). Case law has established that, with limited exceptions, business income is derived when a taxpayer has done all that is necessary to earn the income (see, for example *Arthur Murray (NSW) Pty Limited v FCT* (1965) 114 CLR 314 (HCA); *Bowcock v CIR* (1981) 5 NZTC 61,062 (HC); *CIR v Molloy* (1990) 12 NZTC 7,146 (HC); *Hawkes Bay Power Distribution Limited v CIR* (1999) 19 NZTC 15,226 (CA)) and a debt is created (see, for example *FCT v Australian Gaslight Company* (1983) 83 ATC 4800 (FFedC); *Gasparin v FCT* 94 ATC 4,280 (FFedC); *CIR v Farmer’s Trading Company Limited* (1982) 5 NZTC 61,200 (CA)).
10. In *HW Coyle Ltd v CIR* (1980) 4 NZTC 61,558 (HC), the High Court considered the derivation of payments under a construction contract. The Court held that the accounting treatment adopted by the taxpayer did not determine the result and said, at page 61,565, that the court’s task was:

... to apply the statutory provisions of the Land and Income Tax Act 1954, now the Income Tax Act 1976, to the Objector concerned and the particular contract.
11. The court held, at page 51,568, that the retention amounts under the contract had not:

... been derived or earned and should not be included in the assessable income of the taxpayer until they are payable.
12. Recognition of income under building contracts was also considered in *Horizon Homes Ltd v CIR* (1994) 16 NZTC 11,064 (HC), in which the High Court followed the approach taken in *Coyle* and, at page 11,079, said:

A taxpayer is not regarded as having derived income to which he is not yet contractually entitled.

13. The core provisions have been introduced into the Income Tax Act since the *Coyle* and *Horizon Homes* decisions. However, the cases are consistent with the core provisions in focusing on the statutory tests rather than accounting treatment.

When is expenditure deducted?

14. Deductions must be allocated to an income year (s BD 4(1)), which is the year the expenditure is “incurred” unless that is altered by a specific timing provision in the Act (s BD 4(2)). In determining the time of incurrence regard must be had to case law (s BD 4(3)). Case law has established that a taxpayer must have paid, agreed to pay or become definitively committed to a payment for an expense to be incurred (see, for example, *CIR v Mitsubishi Motors New Zealand Limited* (1995) 17 NZTC 12,351 (PC), *AM Bisley & Co Ltd and Ors v CIR* (1985) 7 NZTC 5,082 (HC), *HW Coyle Ltd v CIR*, *Case M123* (1990) 12 NZTC 2,788).
15. Section EA 3 contains a timing rule in relation to expenditure that is incurred before the services for which it is incurred are performed. This section will generally not apply to retention amounts because they represent expenditure on services already performed.

Terms of contract critical

16. The correct tax treatment in each case depends on the precise terms of the contract between the parties. If, for example, a contract provides that 10% of payment for work completed to date is to be retained by the payer, and the payer is not liable to pay that amount until an engineer’s certificate is provided, then the income earning process is completed if and when the engineer’s certificate is provided. The payer will incur, ie, become definitively committed to the payment, if and when the certificate is given.
17. If, instead, a contract simply provides for 10% of a payment for work to date to be retained by the payer until a later date (ie, there is no contractual requirement for repairs to be made or an engineer’s certificate to be issued), the income is derived when the work is completed and not at the later designated payment date. Similarly, the payer will be definitively committed to the payment once the work is complete even though actual payment is deferred until a later date.
18. It may be that the practical effect of retaining an amount until an engineer’s certificate is given will be the same as retaining it for a period during which the

payer can check for defects, inadequate work, etc. However, the tax position depends on the legal rights and obligations of the parties under the contract and not the practical effect of those terms.

19. It has been suggested that a customer (or head contractor) will incur the full cost of works, including all retentions, once the original works have been completed. That is, retentions are incurred even though payment of them is not required unless or until the contractor has repaired all defects and rectified all omissions. As the incurred and derived tests are different, it is argued that the customer can incur the retention payments on completion of the original works but the contractor will not derive that income until the repairs are completed and omissions rectified. The Commissioner agrees that the incurred and derived tests are different and, in some cases, this may mean that an expense is incurred before corresponding income is derived. However, if work remains to be done before retentions are legally payable under the contract, the payer has not incurred that amount as the payer has not yet become definitively committed to the payment.

Financial Arrangement Rules

20. Under the financial arrangement rules in subpart EW, part of a payment can be treated as interest for tax purposes. This can be the case where either goods or services are provided before payment or where payment occurs in advance of the provision of goods or services. However, as a general proposition, no interest will be implied under those rules where, essentially, the amount paid is the amount the parties would have agreed to pay if payment took place at the time services are performed, or property transferred. The rules also do not apply to certain short term agreements. The application of subpart EW to construction contracts, including retention payments, is outside the scope of this item.

Examples

Example 1 – Retention Pending Repair

21. Contractor contracts with Customer to construct and install a large item of industrial plant. The contract allows Customer to retain up to 5% of any progress payment until defects in work to date are rectified. Contractor's contract with Sub-Contractor provides for retentions on the same basis.
22. A sub-component of the plant, installed by Sub-Contractor, is defective and Customer retains an amount from the 30 January progress payment. Contractor retains the same amount from its progress payment to Sub-Contractor. Sub-Contractor completes the replacement of the sub-component by 29 March. Customer pays Contractor the retention on 5 April and Contractor pays Sub-Contractor the next day.
23. Contractor derives the income in the year ending 31 March, as Contractor becomes entitled to payment on 29 March when the repair is completed. Similarly, Sub-Contractor derives the income in the same year. Contractor also incurs the expenditure in the year ending 31 March as Contractor becomes definitively committed to pay Sub-Contractor when the repair is completed.

Example 2 – Requirement for Certification

24. Builder contracts with Customer to build a high-rise building. Builder must submit claims for progress payments to Engineer who then certifies the appropriate amount to be paid by Customer. Customer may retain up to 5% from any progress payment as security against any defects in the work. A retention amount is payable (as part of the next progress payment) once Engineer has certified that any defects have been remedied or (as part of the final payment) if Engineer has certified that the entire contract work has been completed.
25. Customer retains \$100,000 from the 30 November 2010 progress payment, in respect of identified defects, and Builder completes the repair of those defects on 28 February 2011.
 - If Engineer issues the certificate on 3 March 2011, Builder derives the retention amount as income in the income year ending 31 March 2011 and Customer incurs the expenditure in that year.
 - If instead, Engineer is unable to issue the certificate until 1 April 2011, Builder derives the retention amount as income in the income year ending 31 March 2012 and Customer does not incur the expenditure until that later year.

Example 3 – Relevance of Defect Liability Period

26. Contractor contracts with Customer to build a chemical plant. The contract provides for Customer to make progress payments. The contract also provides that Customer will retain 10% of each progress payment. Fifty percent of the retention money is to be paid to Contractor on practical completion of the plant. The balance of the retention money is to be paid at the end of a defects liability period that runs to a date after practical completion. Contractor's contract with Sub-Contractor provides for retentions on the same basis.
27. The 50% of the retention money payable on practical completion is derived as income by Contractor when practical completion occurs. That is the point at which everything that must be done to earn the money has been done. If, alternatively, the contract provides that practical completion must be certified by an engineer then the income will be derived on the date when the certificate is given.
28. The timing of derivation of the balance of the retention money will depend on the precise terms of the contract. If the contract provides that it will be paid at the end of a period that runs to a time after completion of the work (the defects liability period), then the income will be derived when the work is completed and not at the end of that period. This is because, by completing the work, Contractor has done all that is required to be done to earn the income. However, if the contract provides that the balance will be paid at the end of a defects liability period provided an engineer certifies that the works are free of defects, then the income will not be derived until that certificate is given. The giving of the certificate is something that must be done for the income to be earned.
29. The timing of incurrence by Contractor of the payment of retention money to Sub-contractor will be the same. Contractor will become definitively committed to pay the first 50% of the retention money on practical completion. However, if payment is conditional upon practical completion being certified, then the expense will be incurred if and when the certificate is given. The balance, payable at the end of the defect liability period will also be incurred on practical completion unless there is something more required (eg, certification that the works are free of defects) before payment is required. In that case, the balance will be incurred at the time the certificate is given.

Subject references
Derivation of income; Incurrence of expenditure; Retention money
Legislative references
Income Tax Act 2007, ss BD 3, BD 4, CA 1, CB 1 and DA 1
Case references
<i>AM Bisley & Co Ltd and Ors v Commissioner of Inland Revenue</i> (1985) 7 NZTC 5,082 (HC)
<i>Arthur Murray (NSW) Pty Limited v FCT</i> (1965) 114 CLR 314 (HCA)
<i>Bowcock v CIR</i> (1981) 5 NZTC 61,062 (HC)
<i>Case M123</i> (1990) 12 NZTC 2,788
<i>CIR v Farmer's Trading Company Limited</i> (1982) 5 NZTC 61,200 (CA)
<i>CIR v Mitsubishi Motors New Zealand Limited</i> (1995) 17 NZTC 12,351 (PC)
<i>CIR v Molloy</i> (1990) 12 NZTC 7146 (HC)
<i>FCT v Australian Gaslight Company</i> (1983) 83 ATC 4800 (FFedC)
<i>Gasparin v FCT</i> 94 ATC 4,280 (FFedC)
<i>Hawkes Bay Power Distribution Limited v CIR</i> (1999) 19 NZTC 15,226 (CA)
<i>Horizon Homes Ltd v CIR</i> (1994) 16 NZTC 11,064 (HC)
<i>HW Coyle Ltd v CIR</i> (1980) 4 NZTC 61,558 (HC)

ITEMS OF INTEREST

UPDATE ON PUBLIC INFORMATION BULLETIN REVIEW

In an item entitled “Review of Public Information Bulletins” published in *Tax Information Bulletin* Vol 23, No 1 (February 2011) Inland Revenue announced that a review of *Public Information Bulletins* (PIBs) had commenced. The review was carried out due to concern that items published in PIBs contained limited analysis or reasoning to support the views expressed and were often out of date. Many items referred to legislation that had been repealed or amended, or the Commissioner’s views or reasoning had developed or changed significantly since the time of publication.

Inland Revenue has now completed the formal process of reviewing all items containing tax technical information in the 183 PIB volumes and identifying those which are of no current relevance and will not be republished. The remainder have either been updated and republished in a current *Tax Information Bulletin* or, in the case of a small number, are to be given further consideration. The results of the review are published on Inland Revenue’s website at www.ird.govt.nz/technical-tax/pib-review/. The website contains tables of completed PIB reviews and links to archived historical legislative commentary contained in the PIBs.

The items still noted as being under consideration should continue to be referenced with some care, and not necessarily be taken as the Commissioner’s current view of the law or operational practice. Where there is doubt, professional advice should be sought.

All review decisions have been consulted on with the New Zealand Institute of Chartered Accountants and the New Zealand Law Society.

The review initially aimed to also consider early *Tax Information Bulletin* items, ie, ones issued before 1996. Due to issues of resourcing and competing priorities this has not been possible at this time. Care should also be taken with referencing these items given their age.

If you have any queries regarding this review, please contact Technical Services, Office of the Chief Tax Counsel, at public.consultation@ird.govt.nz

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.

TRINITY AVOIDANCE SCHEME

Case	Ben Nevis Forestry Ventures Limited and Bristol Forestry Venture Limited, Clive Richard Bradbury and Gregory Alan Peebles v Commissioner of Inland Revenue
Decision date	11 September 2013
Act(s)	High Court Rules
Keywords	Strike out, judicial bias, presumptive bias, nullity, functus officio, finality principle, jurisdiction

Summary

The Judgment upheld the application by the Commissioner of Inland Revenue (“the Commissioner”) to dismiss or strike out the claim of judicial bias against Venning J in regard to his 2004 Judgment where he held the Trinity scheme was tax avoidance.

Impact of decision

This decision confirms that where an appellate court has determined an appeal, the trial court does not have jurisdiction to set aside its original judgment on the grounds of bias—it is a matter that needs to be appealed.

Facts

The Judgment relates to an application by the Commissioner to dismiss/strike out the taxpayers’ (Ben Nevis Forestry Ventures Limited and others, “Ben Nevis”) claim of judicial bias against Venning J (“the Judge”) for his 2004 decision regarding the Trinity scheme (“the 2004 Judgment”). The bias being alleged is that (at [3]):

... when the Judge delivered the 2004 Judgment he was liable to the Commissioner in respect of certain duties arising out of his own investment in a forestry investment trust. Ben Nevis says that the Judge was, as a result, “beholden” to the Commissioner.

It was further submitted that the result of the alleged bias is that the 2004 Judgment is a nullity.

The Commissioner filed a protest under rule 5.49 of the High Court Rules on the basis that the High Court is now functus officio and therefore has no jurisdiction to set aside the 2004 Judgment. The Commissioner also applied to dismiss or strike out the proceedings on jurisdictional grounds, submitting any challenge to the 2004 Judgment can only be heard by an appellate court.

Decision

Nullity

The Court was required to determine whether the 2004 Judgment was a nullity that Ben Nevis would have been entitled (prior to any appeals) to have set aside in the exercise of its inherent jurisdiction.

Katz J stated that she had “real reservations as to whether allegations of bias (as opposed to breaches of the right to be heard) are appropriately dealt with as ‘nullities’, other than in the clearest of cases” at [30].

Katz J further stated that it must be at least arguable that the 2004 Judgment could have been challenged as a nullity prior to the decision being appealed.

The Court (at [49]) found the allegation that the 2004 Judgment was a nullity because the Judge was presumptively biased due to an alleged tax obligation that resulted in him being “beholden” to the Commissioner was:

... (an allegation which the Court of Appeal has previously suggested was “startling” and lacking in any evidential foundation). The rule against bias is an aspect of natural justice. However, the allegations of presumptive bias in this case are far removed from the facts of any previous case where a judgment or order has been found to be a “nullity”. The nullity exception is usually applied where a procedural breach is both obvious and egregious.

Jurisdiction

The Court was then required to decide whether it had jurisdiction to set aside the 2004 Judgment following its appeals.

It stated that to declare the 2004 Judgment a nullity it would have to declare the subsequent appeals of the 2007

Court of Appeal and 2008 Supreme Court decisions to be nullities. Further a re-hearing could not take place unless the High Court set aside the decisions of both the Court of Appeal and the Supreme Court.

Katz J stated (at [48]) that:

Once a final judgment has been delivered a court is *functus officio*, consistent with the principle that litigation must have a defined end point (the finality principle). In the interest of justice, however, courts have recognised some limited exceptions to the finality principle. These include where a judgment is a “nullity” because, for example, it was delivered without one party having been heard (a breach of natural justice). If a judgment is a nullity, the Court which delivered it can generally set it aside, without the need for an appeal.

The Court went on to state that had this case not been previously appealed, it would have been reluctant to dismiss the proceedings solely on jurisdictional grounds. The reasoning being (at [50]) that “[i]f there is room for reasonable doubt as to whether jurisdiction exists, it will rarely (if ever) be appropriate to dismiss proceedings on the basis of lack of jurisdiction”.

However, the Court noted (at [51]) that the case is different if a decision has already been appealed, stating:

... it is not, in my view, even remotely arguable that this Court now has jurisdiction to set aside the 2004 Judgment. To hear determine [the bias] proceedings would require the High Court to disregard the hierarchical nature of our court system and, in effect, declare the decisions of the superior courts to be nullities. The relief sought by Ben Nevis is indisputably beyond the jurisdiction of this Court.

The Court dismissed the proceedings.

OUTSTANDING PROCEEDINGS NOT A “SUBSTANTIAL DISPUTE” FOR THE PURPOSE OF SETTING ASIDE A STATUTORY DEMAND WHERE THERE ARE FINALISED TAX CHALLENGES

Case	Bristol Forestry Venture Limited and Ben Nevis Forestry Ventures Limited v Commissioner of Inland Revenue
Decision date	12 September 2013
Act(s)	Companies Act 1993
Keywords	Setting aside of statutory demand, substantial dispute, assessment, Trinity, immediate liquidation

Summary

The Judgment dismissed an application by Trinity investors to set aside statutory demands based on assessments confirmed by the Supreme Court. The application relied on another proceeding seeking to dispute the validity of the Court’s previous decisions in relation to the Trinity scheme.

The Judge declined to make an order for immediate liquidation but required full payment in 10 working days, failing which liquidation can be applied for.

Costs were awarded to the Commissioner of Inland Revenue.

Impact of decision

There is no substantial dispute for the purposes of section 291 of the Companies Act 1993 where an assessment, which has been challenged and confirmed, might be set aside in some future appeal.

Facts

The Judgment relates to applications made by Bristol Forestry Venture Limited (“Bristol”) and Ben Nevis Forestry Ventures Limited (“Ben Nevis”), (“the plaintiffs”) to set aside statutory demands.

The plaintiffs were involved in the Trinity tax avoidance arrangement and the statutory demands relate to their 1998 assessments, which were ultimately confirmed by the Supreme Court in *Ben Nevis Forestry Ventures Ltd & Ors v Commissioner of Inland Revenue* [2008] NZSC 115, [2009] 2 NZLR 289.

The plaintiffs’ application seeks to have the statutory demands set aside or (in the alternative) an order declaring that the documents are not statutory demands. The application relies primarily on another proceeding which seeks to dispute the validity of the Court’s previous decisions in relation to the Trinity scheme (*Ben Nevis Forestry Ventures*

Limited & Bristol Forestry Venture Limited & Bradbury & Peebles v Commissioner of Inland Revenue [2013] NZHC 2361; this decision was reserved at the date of hearing).

Decision

Associate Judge Faire dismissed the application to set aside the statutory demands. Having reached that conclusion, the Judge considered that the appropriate course in this case is not to order the immediate liquidation of the companies but, rather, to make an order in terms of section 291(1)(a) of the Companies Act 1993. Accordingly, the Judge ordered that both plaintiffs pay the sums due under the statutory demands within 10 working days, failing which the Commissioner may apply to put the plaintiffs into liquidation.

Substantial dispute

The Court was required to determine whether there was a substantial dispute as to whether or not the debt is owing or is due. It was for the plaintiffs to show a fairly arguable basis upon which they are not liable for the amounts claimed.

In considering whether the ongoing proceeding (which disputes the validity of previous decisions in relation to the Trinity scheme) is a substantial dispute as to whether or not the debt is owing or is due, the Court held (at [39]):

The challenge judgments, unless declared invalid, bring to an end any right to question liability to pay the shortfall penalties and interest by the operation of section 109 of the Tax Administration Act 1994. The result is that, as the position currently stands, the debt is not a contingent or prospective debt. It is a debt which is currently due.

The Judge also stated:

[41] Unless a judgment is stayed, there cannot be a substantial dispute over the debt it establishes. The possibility that a present existing and enforceable debt might be set aside in the future under a subsequent appeal does not give rise to a general dispute about the existence of the debt.

[42] Accordingly, I conclude that the first ground advanced by the plaintiffs in reliance on section 290(4)(a) of the Companies Act 1993 fails. The ancillary ground related to it, namely that the debt is not yet due, fails for the same reason. The challenge process has been completed. Section 109 of the Tax Administration Act 1994 applies. There is, therefore, a debt that satisfies the definition of a statutory demand as prescribed by section 289 of the Companies Act 1993.

Serving the statutory demands was an abuse of process and they could be set aside on other grounds

The Court considered whether or not the demands ought to be set aside on other grounds under section 290(4)(c) of the Companies Act 1993. Associate Judge Faire held (at [48]):

I cannot, in this case, find any specific factor – whether it is policy, a matter of principle or the justice of this case

– that would justify the application of section 290(4)(c) of the Companies Act 1993 in respect of the application. The defendant was entitled to issue a statutory demand in reliance on judgment which brought to an end the challenge process and which, as a consequence of section 109 of the Tax Administration Act 1994, prevents the position being disputed in a court, or in any proceedings “on any ground whatsoever”.

The statutory demands were not capable of being statutory demands

The Judge recorded that the plaintiffs relied on other matters and that this ground had been pleaded simply to emphasise the plaintiffs’ proposition that any debt owed to the Commissioner was not yet due, and therefore a demand for it did not satisfy the requirements of section 290(4)(a). The Judge considered that this submission was encompassed in the other grounds.

What is the appropriate order?

Having reached the conclusion that the statutory demands should not be set aside, the Court considered whether to make an order under section 291(1)(a) or 291(1)(b) of the Companies Act 1993. The Commissioner invited the Court to place the companies into immediate liquidation under section 291(1)(b).

The Court reviewed the authorities and considered that the general rule is that a winding-up order will not be made on a petition founded on a debt which was genuinely disputed. When the Court makes an immediate order for liquidation under section 291(1)(b), it bypasses the normal procedures of a liquidation application. There is no advertising and no opportunity is given to shareholders or other creditors to be heard about whether a liquidation order should be made or not. The scope for an inquiry to exercise discretion under section 241 is limited. Even though a presumption of inability to pay debts under section 287(a) may not be established, the company will be treated as unable to pay its debts. This means before taking the “short-cut route” under section 291(1)(b) there must be clear evidence the company is insolvent.

The Court further noted a number of factors for not placing the plaintiffs into immediate liquidation, namely:

- a) the indebtedness to the Commissioner could well be satisfied by the shareholders and no evidence was before the Court as to the shareholders’ ability to adopt this course;
- b) no advance warning of the immediate liquidation application was given to the companies and perhaps the opportunity for evidence of the shareholders’ ability to satisfy the debt was not available;
- c) the liquidation of the plaintiffs will not bring the matter to a conclusion as the shareholders can carry on with the proceedings that they have signalled;

- d) it was not readily apparent that there was a need for an early appointment of a liquidator; and
- e) wider considerations arise at the point that the Court must determine whether it will exercise its discretion to order a liquidation of a company than those that apply to an application to set aside a statutory demand.

The Court concluded the appropriate course of action was an order under section 291(1)(a) of the Companies Act 1993 (rather than section 291(b)(1)) ordering the plaintiffs to pay within 10 working days, failing which the Commissioner can apply to have the plaintiffs liquidated.

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Office of the Chief Tax Counsel

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

Legal and Technical Services

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

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