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TAX INFORMATION Bulletin

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Inland Revenue
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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

Legal decisions – case notes

Items of interest

FATCA intergovernmental agreement update

New Zealand has received notification from the United States Government of more favourable terms being granted to another jurisdiction. These terms are to form part of the Foreign Account Tax Compliance Act intergovernmental agreement signed between New Zealand and the United States in July 2014.

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**

PUBLIC RULING BR PUB 15/03: GST – LEGAL SERVICES PROVIDED TO NON-RESIDENTS RELATING TO TRANSACTIONS INVOLVING LAND IN NEW ZEALAND

This is a reissue of BR Pub 10/09. For more information about earlier publications of this Public Ruling see the Commentary to this Ruling.

This is a Public Ruling made under s 91D of the Tax Administration Act 1994.

Taxation Laws

All legislative references are to the Goods and Services Tax Act 1985 unless otherwise stated.

This Ruling applies in respect of s 11A(1)(k).

The Arrangement to which this Ruling applies

The Arrangement is the supply by a registered person of legal services to a non-resident (who is outside New Zealand at the time the services are performed) relating to:

- transactions involving the sale or purchase of land in New Zealand or the lease, licence, or mortgage of land in New Zealand, or
- easements, management agreements, construction agreements, trust deeds, guarantees and other agreements concerning land in New Zealand, or
- disputes arising in relation to land in New Zealand.

How the Taxation Law applies to the Arrangement

The Taxation Law applies to the Arrangement as follows.

Under s 11A(1)(k), the supply of the following types of legal services to a non-resident who is not in New Zealand at the time the legal services are performed is zero-rated:

- legal services relating to transactions involving the sale and purchase of land in New Zealand (including the drafting of agreements for the sale and purchase of land, the provision of legal advice in relation to the sale and purchase transaction and ancillary and related services leading up to the completion of the sale and purchase transaction);
- legal services relating to transactions involving the lease, licence or mortgage of land in New Zealand;
- legal services relating to easements, management agreements, construction agreements, trust deeds, guarantees and other agreements relating to land in New Zealand; and
- legal services relating to disputes arising in relation to land in New Zealand (including drafting court documents, court appearances, representation in negotiations and settlements and general advice in relation to such disputes).

The period for which this Ruling applies

This Ruling will apply for an indefinite period beginning on 24 May 2015.

This Ruling is signed by me on 4 March 2015.

Susan Price

Director, Public Rulings

COMMENTARY ON PUBLIC RULING BR PUB 15/03

This commentary is not a legally binding statement. The commentary is intended to help readers understand and apply the conclusions reached in Public Ruling BR Pub 15/03 (the Ruling).

Legislative references are to the Goods and Services Tax Act 1985 unless otherwise stated. Relevant legislative provisions are reproduced in the Appendix to this commentary.

Summary

1. Services supplied to a person who is a non-resident, and who is outside New Zealand at the time the services are performed, will be zero-rated under s 11A(1)(k) provided that the services are not directly in connection with land situated in New Zealand or any improvement to the land.
2. The following principles on the interpretation of the phrase "directly in connection with" can be drawn from case law:
   - Whether there is sufficient relationship between two things, so as to be "in connection with" each other, is a matter of fact and degree and impression and the evaluation of whether there is a sufficient relationship between these two things requires a common sense assessment of the factual situation. Each case depends on its own facts and the particular statute under consideration.
   - The inclusion of the word "directly" in section 11A(1)(k)(i) indicates that a close connection would be required between a service and land for the service to be regarded as a service that is supplied "directly in connection with" the land.
   - Although there must be a direct relationship between the service and the property, for the service to be directly in connection with that property, the non-resident to whom the service is provided need not own or be entitled to the use or possession of the particular property.
   - Services that are "directly in connection with" land clearly include services that have a physical effect on the land, such as gardening or repairs to improvements to land.
   - Services that merely bring about or facilitate a transaction that has direct effect on land and which are one step removed from a transaction that has a direct effect on the land are not supplied "directly in connection with" the land. This though is a matter of fact and degree as discussed above.
   - If the service could not have been performed but for the existence of the land, this may suggest that the service is supplied "directly in connection with" the land, but this factor is not conclusive.
3. Sections 11A(2), 11A(3) and 11A(3B) are relevant when considering whether a person is outside New Zealand or whether the services are received in New Zealand.
4. Legal services of the type outlined in the Arrangement are not directly in connection with the land or improvements to the land. Rather they are either one step removed from the transaction that has a direct effect on the land, or ancillary to that transaction.

Background

5. BR Pub 15/03 is a reissue of BR Pub 10/09, which expires on 23 May 2015. This Ruling is essentially the same as BR Pub 10/09 and the original ruling, BR Pub 07/03. However, minor amendments have been made to reflect the introduction of s 11A(3B).
6. Under s 11A(1)(k), goods and services tax (GST) is chargeable at the rate of 0% on services supplied to a non-resident who is outside New Zealand at the time the services are performed. However, s 11A(1)(k) does not apply to services that are supplied "directly in connection with" land situated in New Zealand: s 11A(1)(k)(i)(A).
7. New Zealand legal firms may provide legal services to clients who are non-residents and who are outside New Zealand at the time the services are performed. Such legal services could include:
   - legal services relating to transactions involving the sale and purchase of land in New Zealand (including the drafting of agreements for sale and purchase of land, the provision of general legal advice in relation to the sale and purchase transaction and ancillary or related services leading up to the completion of the sale and purchase transaction);
   - legal services relating to transactions involving the lease, licence or mortgage of land in New Zealand;
   - legal services relating to easements, management agreements, construction agreements, trust deeds, guarantees and other agreements in relation to land in New Zealand (including the drafting of documents and the provision of legal advice in relation to such transactions); and
   - legal services relating to disputes arising in relation to land in New Zealand (including drafting court documents, court appearances, representation in negotiations and settlements and the provision of general legal advice in relation to such disputes).

8. This ruling concerns the meaning of the phrase "directly in connection with" in s 11A(1)(k)(i) and the degree of connection necessary between legal services and land in New Zealand before such services will be supplied "directly in connection with" land in New Zealand.

9. It is noted that the definition of "resident" in s 2 deems a person to be resident in New Zealand to the extent that the person carries on any taxable activity (or any other activity), while having any fixed or permanent place in New Zealand relating to that taxable activity (or other activity). Owning land in New Zealand can, in certain circumstances, therefore, affect the residence status of the purchaser. This Ruling does not consider the application of the residence provisions. Rather, it proceeds on the basis that the purchaser is non-resident.

Application of the Legislation

Meaning of "directly in connection with"

10. In *Case E84* (1982) 5 NZTC 59,441 at 59,446, Judge Bathgate discussed the meaning of the phrase "in connection with" in the context of the Income Tax Act 1976 in the following terms:

> … It is a matter of degree whether, on the interpretation of a particular statute, there is a sufficient relationship between subject and object to come within the words "in connection with" or not. **It is clear that no hard and fast rule can be or should be applied to the interpretation of the words "in connection with". Each case depends on its own facts** and the particular statute under consideration.
>
> …
>
> Its proper interpretation depends on the context in which the phrase is used. It may mean "substantial relation in a practical business sense", or it may have a far more restricted meaning, depending on its context.
>
> …
>
> [Emphasis added]

11. Judge Bathgate considered that it is a question of fact and degree and impression whether a sufficient relationship exists between two things for them to be "in connection with" each other. He held that the evaluation of whether two things are "in connection with" each other requires a common sense assessment of the factual situation.

12. However, in s 11A(1)(k)(i) the phrase "in connection with" is qualified by the word "directly".

13. The interpretation of the phrase "directly in connection with" in the GST context was considered in *Auckland Regional Authority v CIR* (1994) 16 NZTC 11,080 (HC), *Wilson & Horton Ltd v CIR* (1994) 16 NZTC 11,221 (HC) (appealed as (1995) 17 NZTC 12,325 (CA)), *Case S88* (1996) 17 NZTC 7,551 (appealed as *CIR v Suzuki New Zealand Ltd* (2000) 19 NZTC 15,819 (HC) and (2001) 20 NZTC 17,096 (CA)), *Malololailai Interval Holidays New Zealand Ltd v CIR* (1997) 18 NZTC 13,137 (HC) and *Case T54* (1998) 18 NZTC 8,410. These cases illustrate how the phrase is to be interpreted in the context of s 11A(1)(k)(i)(A).

14. The issue considered in the *Auckland Regional Authority* case was whether landing dues, terminal services charges and international garbage disposal charges levied by the ARA (the operator of Auckland International Airport) were paid for services that were supplied "directly in connection with" the service of international transportation. Barker J held that landing dues (which were paid for the use of runways, turnoffs, taxiways and holding bays) were supplied "directly in connection with" international transportation. This was because the service of international transportation could not be supplied without the provision of runways etc. However, he considered that the terminal services charge (which related to the use of terminals and equipment used for embarkation or disembarkation from international aircraft, maintenance and cleaning of luggage carousels, gate lounges, baggage makeup, distribution and storage areas) were "ancillary" to the supply of international transportation. This was in the sense of being secondary or subservient. Barker J also considered that the garbage disposal service was a separate service from the supply of international transportation services. That is, although an essential service, it was ancillary to the service of transportation.

15. The *Auckland Regional Authority* case is not directly on point. This is because it addresses the issue of whether two services are supplied "directly in connection with" each other, rather than whether a service is supplied "directly in connection with" land or other goods in New Zealand. However, by analogy, the case suggests that a service would not necessarily be "in connection with" an item even if the service could not have been performed without the existence of that item.

16. In *Wilson & Horton* (HC), the issue was whether the supply of advertising space in a newspaper was "directly in connection with" the goods advertised. In the High Court, Hillyer J considered that the goods that were the subject of the advertising were "at least one step removed from the services supplied by the newspaper proprietor" (at 11,224). Therefore, the advertising services were not supplied "directly in connection with" land or any moveable personal

property situated in New Zealand. Hillyer J saw a distinction between the painting of a vessel (which would be directly connected with the vessel) and services supplied to the passengers or crew of the vessel (which would not be directly connected with the vessel).

17. On appeal, it was accepted by both parties that the High Court's conclusion on this was correct. Therefore, this aspect of the High Court's judgment was not addressed by the Court of Appeal.

18. The legislation was amended to overturn the result in *Wilson & Horton*. The amendment was based on the Court of Appeal's interpretation of the phrase "for and to", which was previously contained in s 11(2)(e) (now s 11A(1)(k)). However, the phrase "directly in connection with" was retained in the provision. This arguably suggests that the "one step removed" test applied by the High Court in *Wilson & Horton* reflects the intention of the legislation.

19. In *Case S88*, Judge Barber considered the phrase "directly in connection with" for an arrangement involving warranties on imported vehicles. The non-resident manufacturer (MC), from whom the importer (SNZ) purchased vehicles, provided a service warranty to SNZ under which it agreed to reimburse SNZ for certain repairs. SNZ on-sold the vehicles to a dealer, who in turn sold the vehicles to the public. The warranty given by SNZ was wider than the warranty that SNZ received from MC. If SNZ was required to reimburse the dealer for the cost of repairs covered by SNZ's warranty and the particular repairs were also within MC's warranty, SNZ would claim reimbursement from MC. The issue was whether the payment received from MC was for services supplied "directly in connection with … moveable personal property" (the vehicles) in New Zealand.

20. Judge Barber considered that the service provided by SNZ was the repair of the vehicles. This was carried out by the dealer on behalf of SNZ. He held that there was a direct relationship between the repair service and the vehicle. At 7,558, he noted that the repair service could not be performed but for the existence of the vehicle:

> In my view, **the repair services effected by the dealer are directly in connection with the vehicles** originally manufactured by MC but which, at the time of repair, are owned by the customer as purchaser from the dealer. The latter has, shortly before, purchased the vehicle from the objector. The moveable personal property in question is the repaired vehicle. **There is a direct relationship or connection between the service of the repairs and the vehicle**. Accordingly, the said "proviso" to s 11(2)(e) must apply to the facts of this case and prevent the objectors from relying on the zero-rating provisions of the s 11(2)(e). **The repair service could not be performed but for the existence of the vehicle.** The repairs were carried out for the objector (and others) which was carrying them out for MC (and others). **The objector was not merely arranging for the repairs to be carried out, but was responsible under warranty to make the repairs** — as was MC. That activity, or supply, meets the statutory nexus between goods and the service. **The service is the actual repair of vehicles even though that work was performed by a contractor — usually the dealer.**
>
> I agree … that s 11(2)(e) requires the existence of a linkage between the non-resident for whom the services are supplied and the moveable personal property, situated in New Zealand, in relation to which the services are performed. However, there is no requirement in s 11(2)(e) or anywhere else, that at the time the services are performed, the moveable property must be owned by the non-resident person, or that the non-resident person must be entitled to use or possession of the property.
>
> [Emphasis added]

21. The High Court upheld Judge Barber's decision (*CIR v Suzuki New Zealand Ltd*). At 15,830, McGechan J considered that the repair services provided by the importer were analogous to the "painting the ship" example given in *Wilson & Horton*:

> I have no doubt that **repair services were carried out directly in connection with moveable personal property situated in New Zealand at the time the services were performed**. Quite simply, they were repairs carried out on cars within New Zealand. **The situation equates [to] "painting the ship". The nexus could not be closer**. … The duality involved is not prohibitive. … while there was one repair, it arose under and met two quite separate contracts with two different persons. So far as SMC is concerned, the repair was a service to SMC, quite irrespective of the other contract with an SNZ customer likewise discharged. I see no reason why a provision of services to SMC under one contract should be viewed differently because of provision of services to a customer under another. They are concurrent but different supplies. The facts that SMC is non-resident, and a non-owner, are of no present consequence given the way s 11(1)(e)(ii) is worded.
>
> [Emphasis added]

22. The Court of Appeal agreed that the repair services were supplied "directly in connection with" moveable personal property in New Zealand. Blanchard J, giving the judgment of the court, said at 17,102–17,103:

> **There is a nexus in both cases between the performance and the consideration given by the other party.** In the present case there is a more than sufficient financial and legal connection, as demonstrated by the

> evidence, between SMC's payments and the carrying out of the repairs on behalf of SNZ by its dealers. **The repairs may have been done for the customers**, in practical terms, under SNZ's standard warranty, **but they were also done for SMC under its warranty**.
>
> …
>
> It follows from what we have said that we also reject the argument, made in relation to s 11(2)(e), that the services were not supplied directly in connection with movable personal property situated in New Zealand. **The repair services were obviously supplied in relation to goods, namely motor vehicles, which were situated in New Zealand. The supply of repairs could hardly be more directly connected with the motor vehicles.** The fact that they may have no longer been owned by SMC or SNZ is irrelevant. Section 11(2)(e) therefore has no application.
>
> [Emphasis added]

23. In *Malololailai Interval Holidays*, a New Zealand company had supplied services relating to the marketing of timeshare interval holidays at a resort in Fiji to another New Zealand company. The issue was whether the marketing services were "supplied directly in connection with land, or any improvements thereto, situated outside New Zealand". If so, the services would be zero-rated under s 11(2)(b) (now s 11A(1)(e)). As the phrase "directly in connection with" has the same meaning throughout s 11A (*Wilson & Horton* (HC) at 11,224), the *Malololailai* case is relevant to the interpretation of the phrase in the context of s 11A(1)(k)(i).

24. In *Malololailai* at 13,144, Neazor J referred to Case E84:

> A good deal of the debate in that case about whether a narrow or wide interpretation of the statutory phrase was appropriate might have been seen as unnecessary if the word "directly" had been used, as it is in s 11 of the *Goods and Services Tax Act* 1985.

25. These comments highlight the importance of the addition of the word "directly". The word "directly" narrows the scope of what might be considered to be "in connection with" the land and confirms that a direct relationship must exist between the relevant services and land.

26. The *Malololailai* case also confirms that the recipient of a service need not acquire a legal interest in land before the service can be "directly in connection with" the land. At 13,143 Neazor J commented:

> It is not in my view necessary to consider the first point of Mr McLay's argument further than that, because the issue is not whether the purchaser acquires land or an interest in land, but whether the services provided by the marketer on behalf of the objector are "directly in connection with land", which may involve much less than acquiring an interest in the land. By way of example, the provision of gardening services would surely come within the statutory words.

27. Neazor J considered that a transaction between the New Zealand vendor and the purchaser of an interval holiday would be "directly in connection with" land outside New Zealand, but that the marketing services supplied by the marketing company (although essential to bring together the vendor and purchaser and although closely related to the sale and purchase transaction) were not "directly in connection with" the land. The marketing services merely facilitated a transaction that was directly connected to the land (the transaction between vendor and purchaser). At 13,146, Neazor J considered that (as with the advertising services in *Wilson & Horton*) the marketing services were one step removed from a transaction that directly related to the land:

> **I would regard the contractual transaction between [the New Zealand selling company] and the purchaser of an interval holiday as within the descriptive words "directly in connection with land or any improvement thereto"**, although that determination is not essential to this decision, but when attention is paid to the services supplied by [the marketing company] to [the NZ selling company] consider that those services are not within the statutory description. What [the marketing company] does is to advertise and promote interval holidays for [the NZ selling company] and negotiate the contract for individual holidays (including the consideration for that contract between the purchaser and [the NZ selling company]) up to the point where the contract is effected between those two parties.
>
> The services provided by [the marketing company] are not *directly* in connection with the land or the improvements. The transaction of those considered which would be in that category is the transaction between [the NZ selling company] and the purchaser. **The transaction between [the marketing company] and [the NZ selling company] is one which brings about the transaction which has direct effect**, but in my view is of a kind to which Hillyer J's words may properly be applied — it is **one step removed from the direct transaction**.
>
> If one of the analogies referred to needs to be chosen I would take that of the publication of advertisements in the *Wilson & Horton* case. The newspaper proprietor's services facilitated or opened the way to the transactions between vendor and purchaser, and that in my view is what [the marketing company] did, although it was more closely involved in the transaction to which the statutory words apply than the publisher of an advertisement would be. Nevertheless the transaction having direct effect was not that of the publisher, or in ths case of the sales agent.
>
> [Emphasis added]

28. The *Malololailai* case was decided before the High Court and the Court of Appeal judgments in *Suzuki*. Although *Malololailai* was referred to in submissions to the High Court in *Suzuki*, the High Court did not discuss it in detail and the Court of Appeal did not refer to it. The Commissioner considers that the approach in *Malololailai* is consistent with the approach taken in *Wilson & Horton* and is not inconsistent with the *Suzuki* decisions. These cases support a narrow interpretation of the phrase "directly in connection with".

29. *Case T54* concerned the service of producing a video of Japanese honeymoon couples holidaying in New Zealand supplied by a Japanese company. Judge Barber considered that the services were not supplied "directly in connection with" the video camera or the blank tape used to create images (which were later edited to create the final video). Judge Barber considered that the video camera and blank tape were merely tools used to carry out the services and were not the object or objective of the services. He considered that the service provided was the creation of the final video. The judge concluded that the taxpayer had not provided services "directly in connection with" moveable personal property situated in New Zealand at the time the services were performed. This was because the video did not come into existence until after the taxpayer's services had been performed and at that time the video was outside New Zealand. At 8,414–8,415, Judge Barber said:

> The resultant video cassette did not come into existence until after the relevant services had been performed. It was not "situated inside New Zealand at the time the services are performed". Until then it was only a blank tape. There is no other relevant moveable personal property to which the objector's service could be regarded as supplied "directly in connection with". Insofar as there is a connection between the said videoing services and the said blank tape (which fills up during the day) and camera and equipment, that connection is not a "direct" connection. That particular tape is only part of the equipment involved in the process of creating another tape — the resultant videotape cassette. Tools and equipment are aids to the supply of such videoing services, and are not the objects of such services. Those services could be regarded as supplied directly in connection with the Japanese tourists who, of course, are not moveable personal property.

30. *Case T54* is distinguishable on its facts from the types of situations addressed in this item, because it is not possible to argue that land did not exist before legal services are provided (an argument that was accepted in *Case T54*).

Test of whether services are "directly in connection with" land in New Zealand

31. The *following* principles on the interpretation of the phrase "directly in connection with" can be drawn from the above cases:

- Whether there is sufficient relationship between two things, so as to be "in connection with" each other, is a matter of fact and degree and impression and the evaluation of whether there is a sufficient relationship between these two things requires a common sense assessment of the factual situation. Each case depends on its own facts and the particular statute under consideration (*Case E84*).
- The inclusion of the word "directly" in section 11A(1)(k)(i) indicates that a close connection would be required between a service and land for the service to be regarded as a service that is supplied "directly in connection with" the land (*Malololailai*).
- Although there must be a direct relationship between the service and the property, for the service to be directly in connection with that property, the non-resident to whom the service is provided need not own or be entitled to the use or possession of the particular property (*Suzuki*).
- Services that are "directly in connection with" land clearly include services that have a physical effect on the land, such as gardening or repairs to improvements to land (*Malololailai*).
- Services that merely bring about or facilitate a transaction that has direct effect on land and which are one step removed from a transaction that has a direct effect on the land are not supplied "directly in connection with" the land (*Wilson & Horton*, *Malololailai*). This though is a matter of fact and degree as discussed above.
- If the service could not have been performed but for the existence of the land, this may suggest that the service is supplied "directly in connection with" the land, but this factor is not conclusive (*ARA*; *Suzuki*).

32. As a close relationship is required between the relevant services and land in New Zealand, the services must be supplied directly in connection with specific land to fall within s 11A(1)(k)(i)(A).

Legal services

33. Legal services that may be supplied to non-residents include:

- *Legal services relating to transactions involving the sale and purchase of land in New Zealand*

  An analogy can be drawn between the marketing services considered in the *Malololailai* case and legal services for the sale and purchase of land in New Zealand. In *Malololailai*, the court held that the marketing services did not have a direct effect on the land and that they merely facilitated a transaction that had a direct effect on the land (that is, the sale and purchase between the vendor and purchaser). Legal services relating to the sale and purchase of land facilitate or give effect to a transaction between the vendor and purchaser. These have a direct effect on the land but are one step removed from that transaction. Accordingly, legal services relating to the sale and purchase of land in New Zealand (including the drafting of an agreement for the sale and purchase of land in New Zealand, legal advice in relation to a sale and purchase transaction and ancillary or related services leading up to the completion of a sale and purchase transaction) are not services that are supplied "directly in connection with" the land that is the subject of the transaction. Therefore, such services are zero-rated under s 11A(1)(k).

- *Legal services relating to transactions involving the lease, licence or mortgage of land in New Zealand or legal services relating to easements, management agreements, construction agreements, trust deeds, guarantees and other agreements concerning land in New Zealand*

  The same reasoning as above applies to legal services relating to transactions involving the lease, licence or mortgage of land in New Zealand or legal services relating to easements, management agreements, construction agreements, trust deeds, guarantees and other agreements concerning land in New Zealand. These services are provided to a person who enters into a transaction that would have direct effect on the land. However, such legal services are at least one step removed from the land that is the subject matter of the transactions. These services merely assist in bringing about or facilitating a transaction that has direct effect on the land. Accordingly, legal services relating to transactions involving the lease, licence or mortgage of land in New Zealand or legal services relating to easements, management agreements, construction agreements, trust deeds, guarantees and other agreements concerning land in New Zealand (including the drafting of agreements relating to these transactions and the provision of legal advice for such transactions) are not supplied "directly in connection with" the land that is the subject of these transactions. Such services are zero-rated under s 11A(1)(k).

- *Legal representation in disputes in relation to land in New Zealand*

  Legal services involving representation in disputes relating to land in New Zealand (including drafting court documents, court appearances, representation in negotiations and settlements, and general advice) are also one step removed from the land to which the dispute relates. These services may be supplied as a consequence of a transaction that has direct effect on the land. However, consistent with the approach taken in *Malololailai*, the services are not supplied "directly in connection with" the land to which the dispute relates. Therefore, these services are also zero-rated under s 11A(1)(k).

Subsections (2), (3) and (3B)

34. The Arrangement to which this Ruling applies states that the non-resident recipient of the supply is outside New Zealand at the time the services are performed. Sections 11A(2), 11A(3) and 11A(3B) are relevant when considering whether a person is outside New Zealand or whether the services are received in New Zealand.

35. Section 11A(2) ensures that GST is charged on the supply of services that are consumed in New Zealand but are contracted for by a non-resident who is outside New Zealand. It provides that s 11A(1)(k) does not zero-rate services supplied to a non-resident if another person (including an employee or company director of the non-resident) receives the performance of those services in New Zealand.

36. Section 11A(3) defines the phrase "outside New Zealand" for s 11A(1)(k). It relates to non-resident companies and unincorporated bodies and provides that a non-resident company or unincorporated body that has a minor presence in New Zealand, or whose presence is not effectively connected with the supply of services, will remain outside New Zealand.

37. Section 11A(3B) also defines the phrase "outside New Zealand" for s 11A(1)(k). This provision relates to natural persons and provides that a natural person who has a minor presence in New Zealand that is not directly in connection with the supply of services will remain outside New Zealand.

38. The phrase "directly in connection with" has been considered for s 11A(1)(k). It will have the same meaning in the context of s 11A(3B).

39. What constitutes a minor presence will be determined very much by the facts of the particular case. "Minor" is a relative expression. What is minor is therefore

a question of degree and should be regarded as relative to the size or volume of the supplies. A "minor presence" is a presence that is relatively small or unimportant or incidental to the services being supplied. In determining whether a presence is minor, the relative size or importance of the presence of the entity or person when compared with the presence of the New Zealand supplier must be considered. This will involve a consideration of, inter alia, the relative numbers of people connected with the supply, the amount of time spent in connection with the supply by those people and the relative importance of the people to the services being supplied.

40. The test of "effectively connected" is also a question of fact. The relationship of the supply with the presence in New Zealand must be more than remotely connected, but can be more than one step removed from the presence. The phrase is therefore broader than the phrase "directly in connection with". If the presence is attributable to the supply in question, then it is very likely that the presence will be effectively connected with that supply.

41. Discussion of these provisions and some relevant examples are set out in:

- "GST – Treatment of Exported Services" *Taxation Information Bulletin* Vol 11, No 9 (October 1999): 12, and
- "Zero-rated Services Supplied to Non-Residents" *Taxation Information Bulletin* Vol 26, No 7 (August 2014): 98.

Example

42. Steve, who is a US resident, comes to New Zealand with a view to purchasing land for investment purposes. He returns to the US and continues to carry on negotiations for the purchase of land from a distance. Tracey, a New Zealand solicitor, arranges for searches of the land in Land Information New Zealand's records to be carried out and obtains a LIM report from the local authority. She provides advice on tax issues relating to the purchase, whether Overseas Investment Commission consent to the purchase is required and general legal advice regarding the transaction. Tracey then drafts an agreement for sale and purchase, which is signed by both parties. She also advises Steve regarding a mortgage to be secured over the land, drafts a transfer to be signed by the vendor and attends to settlement of the transaction.

43. After settlement, Steve telephones a real estate agent and arranges for the property to be leased. Tracey drafts the lease and negotiates with the lessee's solicitor regarding the form of the lease. The lease is signed and the lessee takes occupation of the property.

44. The legal services provided by Tracey either facilitate transactions between Steve and the vendor, the mortgagee or the lessee that have a direct effect on the land (by creating or changing legal interests in the land) or arise as a consequence of these transactions. However, Tracey's legal services are one step removed from transactions that directly affect the land. The legal services are not supplied directly in connection with land in New Zealand. Therefore, the services will be zero-rated under s 11A(1)(k), provided Steve:

- remains a non-resident; and
- is outside New Zealand at all times when these services are performed, or
- has only a minor presence in New Zealand that is not directly in connection with the supply of the services.

References

Expired Rulings
BR Pub 07/03 "Legal services provided to non-residents relating to transactions involving land in New Zealand" *Tax Information Bulletin* Vol 19, No 6 (July 2007): 4
BR Pub 10/09 "Legal services provided to non-residents relating to transactions involving land in New Zealand" *Tax Information Bulletin* Vol 22, No 9 (October 2010): 2
Subject references
Legal services; Zero-rating provisions
Legislative references
Goods and Services Tax Act 1985 – ss 11A(1)(k), 11A(2), 11A(3), 11A(3B)
Case references
Auckland Regional Authority v CIR (1994) 16 NZTC 11,080 (HC)
Wilson & Horton Ltd v CIR (1994) 16 NZTC 11,221 (HC); (1995) 17 NZTC 12,325 (CA)
Case S88 (1996) 17 NZTC 7,551
Case T54 (1998) 18 NZTC 8,410
CIR v Suzuki New Zealand Ltd (2000) 19 NZTC 15,819 (HC); (2001) 20 NZTC 17,096 (CA)
Malololailai Interval Holidays New Zealand Ltd v CIR (1997) 18 NZTC 13,137 (HC)

APPENDIX – LEGISLATION

1. Section 11A(1)(k)(i) provides:

11A Zero-rating of services

(1) A supply of services that is chargeable with tax under section 8 must be charged at the rate of 0% in the following situations:

…

(k) subject to subsection (2), the services are supplied to a person who is a non-resident and who is outside New Zealand at the time the services are performed, not being services which are—

(i) supplied directly in connection with—

(A) land situated in New Zealand or any improvement to the land; or

(B) moveable personal property, other than choses in action or goods to which paragraph (h) or (i) applies, situated in New Zealand at the time the services are performed; or

2. Sections 11A(2), 11A(3) and 11A(3B) provide:

(2) Subsection (1)(k) and (1)(l) do not apply to a supply of services under an agreement that is entered into, whether directly or indirectly, with a person (person A) who is a non-resident if—

(a) the performance of the services is, or it is reasonably foreseeable at the time the agreement is entered into that the performance of the services will be, received in New Zealand by another person (person B), including—

(i) an employee of person A; or

(ii) if person A is a company, a director of the company; and

(b) it is reasonably foreseeable, at the time the agreement is entered into, that person B will not receive the performance of the services in the course of making taxable or exempt supplies.

(3) For the purpose of subsection (1)(k), (1)(l) and (1)(ma), and subsection (1)(n) as modified by subsection (4)(b), **outside New Zealand**, for a company or an unincorporated body that is not resident, includes a minor presence in New Zealand, or a presence that is not effectively connected with the supply.

(3B) For the purpose of subsection (1)(k), **outside New Zealand**, for a natural person, includes a minor presence in New Zealand that is not directly in connection with the supply.

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.

2015 INTERNATIONAL TAX DISCLOSURE EXEMPTION ITR26

Introduction

Section 61 of the Tax Administration Act 1994 ("TAA") requires taxpayers to disclose interests in foreign entities.

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

To balance the revenue forecasting and risk assessment needs of the Commissioner with the compliance costs of taxpayers providing the information, the Commissioner has issued an international tax disclosure exemption under section 61(2) of the TAA that applies for the income year corresponding to the tax year ended 31 March 2015. This exemption may be cited as "International Tax Disclosure Exemption ITR26" ("the 2015 disclosure exemption") and the full text appears at the end of this item.

Scope of exemption

The scope of the 2015 disclosure exemption is the same as the 2014 disclosure exemption.

Application date

This exemption applies for the income year corresponding to the tax year ended 31 March 2015.

Summary

In summary, the 2015 disclosure exemption **removes** the requirement of a resident to disclose:

- an interest of less than 10% in a foreign company if it is not an attributing interest in a FIF or if it falls within the $50,000 de minimis exemption (see section CQ 5(1)(d) and section DN 6(1)(d) of the ITA). The de minimis exemption does not apply to a person that has opted out of the de minimis threshold by including in the income tax return for the income year a FIF income or loss.

  Please note that a person opting out of the de minimis threshold needs to include FIF income or loss in any of the four subsequent income years even if the total cost of all attributing interests is $50,000 or less.
- if the resident **is not** a widely-held entity, an attributing interest in a FIF that is an income interest of less than 10%, if the foreign entity is incorporated (in the case of a company) or otherwise tax resident in a treaty country or territory, and the fair dividend rate or comparative value method of calculation is used.
- if the resident **is** a widely-held entity, an attributing interest in a FIF that is an income interest of less than 10% if the fair dividend rate or comparative value method is used for the interest. The resident is instead required to disclose the end-of-year New Zealand dollar market value of all such investments split by the jurisdiction in which the attributing interest in a FIF is held or listed.

The 2015 disclosure exemption also removes the requirement for a non-resident or transitional resident to disclose interests held in foreign companies and FIFs.

Commentary

Generally, residents who hold an income interest or a control interest in a foreign company, or an attributing interest in a FIF are required to disclose these interests to the Commissioner. These interests are considered in further detail below.

Attributing interest in a FIF

A resident is required to disclose an attributing interest in a FIF if FIF income or a FIF loss arises through the use of one of the following calculation methods:

- attributable FIF income, deemed rate of return or cost methods; or
- fair dividend rate or comparative value methods, if the resident is a "widely-held entity"; or
- fair dividend rate or comparative value methods, if the resident is not a widely-held entity and the country in which the attributing interest is incorporated or otherwise tax resident is in a country or territory

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

with which New Zealand **does not** have a double tax agreement[2] in force as at 31 March 2015.

The 39 countries or territories that New Zealand does have a double tax agreement in force as at 31 March 2015 are listed below.

Australia	India	Russian Federation
Austria	Indonesia	Singapore
Belgium	Ireland	South Africa
Canada	Italy	Spain
Chile	Japan	Sweden
China	Korea (Republic of)	Switzerland
Czech Republic	Malaysia	Taiwan
Denmark	Mexico	Thailand
Fiji	Netherlands	Turkey
Finland	Norway	United Arab Emirates
France	Papua New Guinea	United Kingdom
Germany	Philippines	United States of America
Hong Kong	Poland	Viet Nam*

* The Viet Nam double tax agreement applies for withholding taxes from 1 January 2015 and for all other provisions from 1 April 2015.

No disclosure is required by non-widely-held taxpayers for attributing interests in FIFs that are income interests of less than 10% and are incorporated or otherwise tax resident in a tax treaty country or territory, if the fair dividend rate or comparative value methods of calculation are used.

A "widely-held entity" for the purposes of this disclosure is an entity which is a:

- portfolio investment entity (this includes a portfolio investment-linked life fund); or
- widely-held company; or
- widely-held superannuation fund; or
- widely-held group investment fund ("GIF").

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

The disclosure required, by widely-held entities, of attributing interests in FIFs which use the fair dividend rate or the comparative value method of calculation is that, for each calculation method, they disclose the end-of-year New Zealand dollar market value of investments split by the jurisdiction in which the attributing interest in a FIF is held, listed, organised or managed. In the event that tax residence is not easily determined, a further option of a split by currency in which the investment is held will also be accepted as long as it is a reasonable proxy—that is at least 90–95% accurate—for the underlying jurisdiction in which the FIF is held, listed, organised or managed. For example, investments denominated in euros will not be able to meet this test and so euro-based investments will need to be split into the underlying jurisdictions.

FIF interests

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

- rights in a foreign company or anything deemed to be a company for the purposes of the ITA (eg, a unit trust)
- an entitlement to benefit from a foreign superannuation scheme, if a person acquired the interest before 1 April 2014, treated the interest as a FIF interest in a return of income filed before 20 May 2013 and for all subsequent income years
- an entitlement to benefit from a foreign superannuation scheme, if a person's interest in the scheme was first acquired whilst the person was tax resident of New Zealand
- an entitlement to benefit from a foreign life insurance policy
- an interest in an entity specified in schedule 25, part A of the ITA (no entities were listed when the *Tax Information Bulletin* Vol 27, No 3 went to press).

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

- an income interest of 10% or more in a CFC (although separate disclosure is required of this as an interest in a foreign company)
- certain interests in Australian resident companies listed on an approved index of the Australian Stock Exchange and required to maintain a franking account (refer to the IR 871 form that can be found on Inland Revenue's website **www.ird.govt.nz** (search keywords: other exemptions or IR871))
- an interest in an Australian unit trust that has an New Zealand RWT proxy with either a high turnover or high distributions
- an interest of 10% or more in a foreign company that is treated as resident, and subject to tax, in Australia (although separate disclosure is required of this as an interest in a foreign company)
- a beneficial interest in a foreign superannuation scheme which was first acquired whilst a person was not a tax resident of New Zealand and which has not been treated as an attributing interest in a FIF by the person

[2] For the avoidance of doubt, the term "double tax agreement" does not include tax information exchange agreements or collection agreements and is limited to the double tax agreements negotiated with the 39 countries or territories listed in this 2015 disclosure exemption.

- certain foreign pensions or annuities (see Inland Revenue's guide *Overseas pensions and annuity schemes (IR 257)* for more information)
- an interest in certain venture capital investments in New Zealand resident start-up companies that migrate to a grey-list country
- an interest in certain grey-list companies owning New Zealand venture capital companies
- an interest in certain grey-list companies resulting from shares acquired under a venture investment agreement
- an interest in certain grey-list companies resulting from the acquisition of shares under an employee share scheme
- an interest held by a natural person in a foreign entity located in a country where exchange controls prevent the person deriving any profit or gain or disposing of the interest for New Zealand currency or consideration readily convertible to New Zealand currency.

De minimis

Interests in foreign entities held by a natural person not acting as a trustee also do not have to be disclosed if the total cost of the interests remains under $50,000 at all times during the income year. This disclosure exemption is made because no FIF income under section CQ 5 of the ITA or FIF loss under section DN 6 arises in respect of these interests. This de minimis exemption does not apply to a person who has opted out of the de minimis threshold by including in the income tax return for the year a FIF income or loss. Please note that a person opting out of the de minimis threshold is generally required to continue to apply the FIF rules in each subsequent tax year. If a person has less than $50,000 of attributing interests in FIFs, they will not be required to apply the FIF rules if, for each of the four previous tax years:

- the person had no attributing interests in FIFs (for example, they had no foreign shares, or only had foreign shares which were exempt from the FIF rules); and/or
- the person had more than $50,000 in attributing interests in FIFs (note that for these years they would have been required to apply the FIF rules).

Format of disclosure

The forms for the disclosure of FIF interests are as follows:

- IR 443 form for the deemed rate of return method
- IR 445 form for the fair dividend rate method (for widely-held entities)
- IR 446 form for the comparative value method (for widely-held entities)
- IR 447 form for the fair dividend rate method (for individuals or non-widely-held entities)
- IR 448 form for the comparative value method (for individuals or non-widely-held entities)
- IR 449 form for the cost method
- IR 458 electronic form for the attributable FIF income method (this form can also be used to make electronic disclosures for all other methods).

It is now possible to download a spreadsheet as a working paper or complete the disclosures online. If you're downloading the spreadsheet you will be able to save it as a working paper on your computer and when completed submit the form by using Inland Revenue's online services.

You will still be able to complete the disclosure online without downloading a spreadsheet by directly entering the disclosure online.

The IR 445 and IR 446 forms, which reflect the disclosure for fair dividend rate and comparative value for *widely-held entities*, must be filed online. As discussed above this disclosure is by country rather than by individual investment as is the general requirement of section 61. In order to be exempt from the general requirements, the alternative disclosure must be made electronically.

The IR 447, IR 448 and IR 449 forms, applying to the fair dividend rate and comparative value methods for *individuals or non widely-held entities* as well as the cost method for all taxpayers, may be completed online.

As noted above, all of the above disclosures can now be filed using the IR 458 electronic disclosure.

The online forms can be found at **www.ird.govt.nz** "Get it done online", "Foreign investment fund disclosure".

Income interest of 10% or more in a foreign company

A resident is required to disclose an income interest of 10% or more in a foreign company. This obligation to disclose applies to all foreign companies regardless of the country of residence. For this purpose, the following interests need to be considered:

a) an income interest held directly in a foreign company

b) an income interest held indirectly through any interposed foreign company

c) an income interest held by an associated person (not being a controlled foreign company) as defined by subpart YB of the ITA.

To determine whether a resident has an income interest of 10% or more for CFCs, sections EX 14 to EX 17 of the ITA should be applied. To determine whether a resident has an income interest of 10% or more in any entity that is not a CFC, for the purposes of this exemption, sections EX 14 to EX 17 should be applied to the foreign company as if it were a CFC.

Format of disclosure

Disclosure of all interests in a controlled foreign company is required using a *Controlled foreign companies disclosure (IR 458)* form. This form, which involves uploading a prescribed spreadsheet, can cater for up to 500 individual disclosures.

The IR 458 form must be completed online at **www.ird.govt.nz** (search keyword: ir458). Please note that electronic filing is a mandatory requirement for CFC disclosure.

Overlap of interests

It is possible that a resident may be required to disclose an interest in a foreign company which also constitutes an attributing interest in a FIF. For example, a person with an income interest of 10% or greater in a foreign company that is not a CFC is strictly required to disclose both an interest held in a foreign company and an attributing interest in a FIF.

To meet disclosure requirements, only one form of disclosure is required for each interest. If the interest is an attributing interest in a FIF, then the appropriate disclosure for the calculation method, as discussed previously, must be made.

In all other cases, where the interest in a foreign company is not an attributing interest in a FIF, the IR 458 for controlled foreign companies must be filed.

Interests held by non-residents and transitional residents

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

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

Under the international tax rules, non-residents and transitional residents are not required to calculate or attribute income under either the CFC or FIF rules. Therefore disclosure of non-residents' or transitional residents' holdings in foreign companies or FIFs is not necessary for the administration of the international tax rules and so an exemption is made for this group.

PERSONS NOT REQUIRED TO COMPLY WITH SECTION 61 OF THE TAX ADMINISTRATION ACT 1994

This exemption may be cited as "International Tax Disclosure Exemption ITR26".

1. Reference

This exemption is made under section 61(2) of the Tax Administration Act 1994. It details interests in foreign companies and attributing interests in foreign investment funds ("FIFs") in relation to which any person is not required to comply with the requirements in section 61 of the Tax Administration Act 1994 to make disclosure of their interests, for the income year ended 31 March 2015.

2. Interpretation

For the purpose of this disclosure exemption:

- to determine an income interest of 10% or more, sections EX 14 to EX 17 of the Income Tax Act 2007 apply for interests in controlled foreign companies ("CFCs"). In the case of attributing interests in FIFs, those sections are to be applied as if the FIF were a CFC, and
- double tax agreement means a double tax agreement in force as at 31 March 2015 in one of the 39 countries or territories as set out in the commentary.

The relevant definition of "associated persons" is contained in subpart YB of the Income Tax Act 2007.

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

3. Exemption

i) Any person who holds an income interest of less than 10% in a foreign company, including interests held by associated persons, that is not an attributing interest in a FIF, or that is an attributing interest in a FIF in respect of which no FIF income or loss arises under either section CQ 5(1)(d) or section DN 6(1)(d) of the Income Tax Act 2007, is not required to comply with section 61(1) of the Tax Administration Act 1994 for that interest and that income year.

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

iii) Any person who is not a portfolio investment entity, widely-held company, widely-held superannuation fund or widely-held GIF, who has an attributing interest in a FIF, other than a direct income interest of 10% or more, and uses the fair dividend rate or comparative value calculation method is not required to comply with section 61(1) of the Tax Administration Act 1994 in respect of that interest and that income year, to the extent that the FIF is incorporated or tax resident in a country or territory with which New Zealand has a double tax agreement in force at 31 March 2015.

iv) Any non-resident person or transitional resident who has an income interest or a control interest in a foreign company or an attributing interest in a FIF in the income year corresponding to the tax year ending 31 March 2015, is not required to comply with section 61(1) of the Tax Administration Act 1994 in respect of that interest and that income year if either or both of the following apply:

- no attributed CFC income or loss arises in respect of that interest in that foreign company under sections CQ 2(1)(d) or DN 2(1)(d) of the Income Tax Act 2007; and/or
- no FIF income or loss arises in respect of that interest in that FIF under sections CQ 5(1)(f) or DN 6(1)(f) of the Income Tax Act 2007.

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

This exemption is signed on the 13th of March 2015.

Peter Loerscher
Principal Advisor (International Tax)

SPECIAL DETERMINATION S33: APPLICATION OF THE FINANCIAL ARRANGEMENTS RULES TO THE LONG TERM INCENTIVE PLAN ESTABLISHED FOR SENIOR EXECUTIVES OF NEW ZEALAND COMPANY LIMITED

This determination may be cited as Special Determination S33: "Application of the financial arrangements rules to the long term incentive plan established for senior executives of New Zealand Company Limited".

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

1. This determination relates to an arrangement (the Plan) establishing a long term incentive plan for senior executives of New Zealand Company Limited (Company). The following persons are parties to the Plan:
   - Company;
   - Parent Limited (Parent);
   - certain employees of Company (Participants); and
   - Trustee Limited (Trustee).
2. The Plan comprises four components:
   - A loan from Company to each Participant, paid to Trustee as agent for each Participant (Loan).
   - Acquisition of shares in Parent (Shares) by the Trustee on behalf of each Participant, using the relevant Participant's loaned funds. The Trustee will do this by either acquiring shares on-market, subscribing for shares in Parent, or transferring shares from its unallocated shareholding for the benefit of each Participant.
   - Trustee will then hold the Shares on trust for each Participant for a restrictive period. The shares will vest in each Participant upon certain vesting criteria being met.
   - The grant of a put option (Put Option) by Trustee to each Participant in respect of each Participant's beneficial interest in the Shares. This is in consideration for the grant of a call option (Call Option) by each Participant to Trustee in respect of each Participant's beneficial interest in the Shares. The options may be exercised where vesting criteria are not met.
   - Payment of a bonus (Bonus) by Company to the Participant, in accordance with the employment contract entered into between Company and the relevant Participant (Employment Contract), where vesting criteria are met.
3. This determination prescribes:
   - the amount of consideration that is solely attributable to the Shares;
   - the amount of consideration that is solely attributable to the Put Options or Call Options (as relevant); and
   - the amount of consideration that is solely attributable to the Employment Contracts.

2. Reference

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

3. Scope of determination

1. This determination applies to Company, Trustee and each Participant in respect of the Plan (more fully described in private ruling BR Prv 15/05 issued on 4 February 2015), including the following agreements:
   - letter of invitation from Parent to employees of Company, under which Parent will invite employees to participate in the Plan;
   - Parent long term incentive plan rules (Rules), which set out the terms of the Plan;
   - Parent long term incentive plan trust deed (Trust Deed), under which the Trustee will hold the Shares for the Participants; and
   - Parent long term incentive plan loan agreement (Loan Agreement), under which Company will loan the Participants funds on an interest free basis to enter into the Plan.
2. This determination is made subject to the following condition:
   - The continued application of private ruling BR Prv 15/05 (under s 91EB of the Tax Administration Act 1994).

4. Principle

1. The following components of the Plan are excepted financial arrangements:
   - the Shares under s EW 5(13);
   - the Put Options under s EW 5(13);
   - the Call Options under s EW 5(13); and
   - the Employment Contracts under s EW 5(4).

2. Any amount that is solely attributable to an excepted financial arrangement described in s EW 5(2) to (16) is not an amount that is taken into account under the financial arrangements rules (s EW 6(2)). This determination specifies the amounts that are solely attributable to the Shares, Put Options, Call Options and Employment Contracts, and are therefore not taken into account under the financial arrangements rules.

5. Interpretation

This determination has no specialised terms that need to be defined further. All legislative references in this determination are to the Income Tax Act 2007, unless otherwise stated.

6. Method

1. The following consideration amounts (where relevant) paid in respect of the Shares are solely attributable to the Shares and are not taken into account under the financial arrangements rules:
   - amounts subscribed by the Trustee (as agent for the Participant) for the Shares;
   - amounts paid by the Trustee (as agent for the Participant) to transfer unallocated Shares for the benefit of the Participant;
   - Shares received by the Trustee (as agent for the Participant); and
   - dividends on the Shares received by the Trustee.
2. The following consideration amounts (where relevant) will be solely attributable to either the Put Options or Call Options and are not taken into account under the financial arrangements rules:
   - the issue of a Call Option by any Participant as consideration for the issue of any Put Option by the Trustee (and vice versa);
   - the transfer of any Participant's beneficial interest in Shares to the Trustee; and
   - the purchase price paid by the Trustee for the transfer of any Participant's beneficial interest in Shares.
3. The Bonus received by any Participant is solely attributable to the relevant Employment Contract and is not taken into account under the financial arrangements rules.

7. Example

This example illustrates the application of the method set out in this determination for the Participant.

This example is based on the following parameters:

Loan	$100
Share subscription	($100)
Acquisition of Shares (agreed value)	$100
Dividends over restrictive period	$36
Dividends applied to partially repay Loan	($36)
Put Option exercised: • Transfer of beneficial interest in Shares (agreed value) • Purchase price for beneficial interest in Shares	 ($64) $64
Loan repayment	($64)

The amounts that are solely attributable to an excepted financial arrangement described in s EW 5(2) to (16) and not taken into account under the financial arrangements rules in accordance with s EW 6(2) are:

- the Share subscription;
- the acquisition of Shares;
- the dividends over the restrictive period;
- the transfer of beneficial interest in Shares; and
- the purchase price for beneficial interest in Shares.

The amounts that the Participant must take into account under the financial arrangements rules are:

- the Loan;
- the dividends applied to partially repay the Loan; and
- the Loan repayment.

This Determination is signed by me on the 4th day of February 2015.

Howard Davis
Director (Taxpayer Rulings)

SPECIAL DETERMINATION S34: SPREADING METHOD TO BE USED BY BANK IN RESPECT OF THE NOTES AND VALUATION OF SHARES ISSUED BY BANK AND NZHOLDCO ON CONVERSION.

This determination may be cited as Special Determination S34: Spreading Method to Be Used by Bank in Respect of the Notes and Valuation of Shares Issued by Bank and NZHoldCo On Conversion.

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

1. This determination relates to a funding transaction involving the issue of Notes by the Bank to the public pursuant to a Notes Deed Poll. The Notes will contain an exchange mechanism, so they can be recognised as Additional Tier 1 capital for the purposes of the Reserve Bank of New Zealand and Australian Prudential Regulation Authority frameworks relating to the capital adequacy of banks.
2. At the same time the Notes are entered into, Bank, NZHoldCo, AusHoldCo and Parent will enter into a Coordination Agreement, which will set out the steps that will occur if a Conversion occurs, requiring exchange of the Notes. "Conversion" may be a mandatory conversion, an optional conversion (at the election of Bank) or a trigger event conversion (upon a Non-Viability Trigger Event or a Common Equity Trigger Event).
3. If a Conversion occurs, the relevant number of Notes must be immediately and irrevocably exchanged for ordinary shares in Parent. The Coordination Agreement provides for a series of share subscriptions and payments from Bank to NZHoldCo, from NZHoldCo to AusHoldCo and from AusHoldCo to Parent.
4. The Arrangement is the subject of private ruling BR Prv 15/06 issued on 19 February 2015, and is fully described in that ruling.
5. The share subscriptions provided for in the Coordination Agreement are each a financial arrangement (as defined in s EW 3) and an "agreement for the sale and purchase of property or services" (as defined in s YA 1). The Notes and the Coordination Agreement are, together, a wider financial arrangement.

2. Reference

1 This determination is made under ss 90AC(1)(bb) and 90AC(1)(i) of the Tax Administration Act 1994.

3. Scope of determination

1. This determination applies to a funding transaction involving the issue of Notes by the Bank to the public pursuant to a Notes Deed Poll. At the same time that the Notes are entered into, Bank, NZHoldCo, AusHoldCo and Parent will enter into a Coordination Agreement, which will set out the steps that will occur if a Conversion occurs, requiring exchange of the Notes.
2. If a Conversion occurs, the relevant number of Notes must be immediately and irrevocably exchanged. In summary, the steps for the exchange of the Notes will be as follows:
   a) Each Note (subject to the exchange requirement) will be immediately transferred by the Holder to NZHoldCo.
   b) In consideration for the Holders transferring their Notes to NZHoldCo, Parent will allot and issue a specified "exchange number" of Parent ordinary shares to such Holders for each Note transferred.
   c) Immediately following the transfer referred to in (a), the Notes will become immediately due and payable and Bank will be required to repay the Face Value of the Notes to NZHoldCo as transferee. Under the terms of the Coordination Agreement, the Face Value owed to NZHoldCo will be repaid by being applied on NZHoldCo's behalf to subscribe for ordinary shares in Bank. The number of ordinary shares in Bank to be subscribed for is based on the equity value of Bank, in accordance with a formula in the Coordination Agreement.
   d) Under the Coordination Agreement, NZHoldCo will be required to pay a sum to AusHoldCo equal to the Face Value of each Note transferred to NZHoldCo. This amount will be automatically applied on AusHoldCo's behalf to subscribe for ordinary shares in NZHoldCo. The number of ordinary shares in NZHoldCo to be subscribed for is based on the equity value of NZHoldCo, in accordance with a formula in the Coordination Agreement.
   e) Under the Coordination Agreement, AusHoldCo will be required to pay a sum to Parent equal to the Face Value of each Note transferred to NZHoldCo. This amount will be automatically applied on Parent's behalf to subscribe for ordinary shares in AusHoldCo. The number of ordinary shares in AusHoldCo to be subscribed for is based on the equity value of AusHoldCo, in accordance with a formula in the Coordination Agreement.

f) However, steps (c) to (e) may be deferred if Conversion occurs for a reason other than a trigger event and any of those steps cannot be completed. If completion of the Intragroup Transactions is deferred any such deferral will be reasonable and no longer than is strictly necessary.

3. This determination applies to determine the spreading method to be used by Bank in respect of the Notes. It is made subject to the condition that the restriction for application of the IFRS financial reporting method in s EW 15D(2B) does not apply to the Notes.

4. This determination also applies when shares are issued by Bank to NZHoldCo and by NZHoldCo to AusHoldCo on Conversion, to determine the value of the shares for the purposes of the financial arrangements rules.

4. Principle

1. The Notes and the Coordination Agreement are, together, a financial arrangement (as defined in s EW 3). The subscription for shares in Bank by NZHoldCo and the subscription for shares in NZHoldCo by AusHoldCo in the Coordination Agreement are both an "agreement for the sale and purchase of property or services" (as defined in s YA 1), because they are conditional agreements to acquire property.

2. The share subscriptions are not a "short-term agreement for sale and purchase" (as defined in s YA 1), because settlement will not occur within 93 days of the Coordination Agreement being entered into. Therefore, they are not excepted financial arrangements under s EW 5.

3. The Bank ordinary shares issued to NZHoldCo and the NZHoldCo ordinary shares issued to AusHoldCo on a mandatory conversion, a trigger event conversion or an optional conversion are part of the wider financial arrangement, and are excepted financial arrangements under s EW 5(13).

4. A person who uses IFRS to prepare financial statements and to report for financial arrangements can use the IFRS financial reporting method in s EW 15D.

5. Under s EW 15I, because the financial arrangement includes in part an excepted financial arrangement, s EW 15C(1) does not apply and the Bank must use one of the methods in s EW 15I(2) to allocate an amount of income or expenditure to an income year.

6. One of the methods available under s EW 15I(2) is a determination made by the Commissioner.

7. For the purposes of determining the consideration paid or payable under the financial arrangements rules, the value of the shares issued by Bank and NZHoldCo must be established under s EW 32. None of subs (3) to (5) of s EW 32 applies to the share subscriptions.

8. Under s EW 32(6), the Commissioner is required to determine the value of the property. Both parties are required to use this amount.

5. Interpretation

1 In this determination, unless the context otherwise requires:

- "Bank" means the bank issuing the Notes;
- "NZHoldCo" means the New Zealand incorporated company holding 100% of the shares in Bank;
- "Conversion" has the same meaning as described in private ruling BR Prv 15/06, issued on 19 February 2015;
- "Notes" means Notes issued to the public pursuant to a Notes Deed Poll;
- "AusHoldCo" means the Australian incorporated company holding 100% of the voting shares in NZHoldCo;
- "Parent" means the Australian incorporated parent company of Bank, NZHoldCo and AusHoldCo;
- "IFRS" means a New Zealand Equivalent International Financial Reporting Standard, in effect under the Financial Reporting Act 2013, and as amended from time to time or an equivalent standard issued in its place.
- All legislative references in this determination are to the Income Tax Act 2007, unless otherwise stated.

6. Method

1. The Arrangement does not involve the advancement or deferral of income or expenditure.

2. The IFRS financial reporting method in s EW 15D must be used to allocate income and expenditure over the term of the Notes.

3. For the purposes of s EW 32(6) the value of the shares issued by Bank is equal to the amount NZHoldCo paid for those shares and the value of the shares issued by NZHoldCo is equal to the amount AusHoldCo paid for those shares.

7. Example

This example illustrates the application of the method set out in this determination.

Bank issues Notes having a Face Value of $100 to Holders. Prior to a Conversion, Bank will use the IFRS financial reporting method to allocate income and expenditure over the term of the Notes.

On Conversion, Notes having a Face Value of $100 are transferred to NZHoldCo by the Holders of the Notes.

Bank immediately repays the Face Value of the Notes, by applying the amount on NZHoldCo's behalf to subscribe for ordinary shares in Bank. Bank issues the number of shares to NZHoldCo calculated in accordance with the formula in the Coordination Agreement. The value of the shares, for the purposes of s EW 32, is $100.

NZHoldCo then pays an amount equal to the Face Value of the Notes to AusHoldCo. This amount is automatically applied on AusHoldCo's behalf to subscribe for ordinary shares in NZHoldCo. NZHoldCo issues the number of shares to AusHoldCo calculated in accordance with the formula in the Coordination Agreement. The value of the shares, for the purposes of s EW 32, is $100.

This Determination is signed by me on the 19th day of February 2015.

Fiona Heiford
Manager (Taxpayer Rulings)

DETERMINATION FDR 2015/01: A TYPE OF ATTRIBUTING INTEREST IN A FOREIGN INVESTMENT FUND FOR WHICH A PERSON MAY NOT USE THE FAIR DIVIDEND RATE METHOD (WELLINGTON MANAGEMENT PORTFOLIOS (DUBLIN) PLC: GLOBAL BOND FUND – NZD SHARE CLASS)

Reference

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

Discussion (which does not form part of the determination)

Units in the Wellington Management Portfolios (Dublin) Plc: Global Bond Fund (WMP) – New Zealand dollar denominated share class (NZD Share Class) to which this determination applies, are an attributing interest in a foreign investment fund (FIF) for New Zealand resident investors.

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

WMP invests in global fixed interest securities for which WMP has made foreign currency hedging arrangements to provide investors with a New Zealand dollar denominated return on these debt instruments.

Section EX 46(10)(c) of the Income Tax Act 2007 would, if not for this determination, require the use of the fair dividend rate (FDR) method.

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

On this basis, where a New Zealand resident invests in New Zealand dollar denominated shares in WMP, I consider that it is appropriate for the investor holding that investment in WMP to be excluded from using the FDR method for the 2014–2015 and subsequent income years.

Scope of determination

This determination is issued on the basis of information provided to the Commissioner before the date of this determination and applies to an attributing interest in a FIF held by New Zealand resident investors in a non-resident issuer where:

1. The FIF:
    a) is incorporated in Ireland and issues multiple classes of shares;
    b) is known at the date of this determination as Wellington Management Portfolios (Dublin) Plc: Global Bond Fund (WMP);
    c) invests into an undivided pool of global fixed interest securities;
    d) undertakes hedging in proportion to the shares issued in each currency. The NZD hedging therefore only covers the proportion of the pool of assets that corresponds to the number of NZD shares.
2. The investors in WMP:
    a) invest in that pool of global fixed interest securities through classes of shares that are denominated in various currencies including one which is denominated in New Zealand dollars (NZD shares);
    b) that are New Zealand residents invest in New Zealand dollar class of shares of WMP.

Interpretation

In this determination unless the context otherwise requires:

- "Financial arrangement" means financial arrangement under section EW 3 of the Act;
- "Non-resident" means a person that is not resident in New Zealand for the purposes of the Act; and
- "The Act" means the Income Tax Act 2007.

Determination

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

LEGISLATION AND DETERMINATIONS

Application date

This determination applies for the 2014–2015 and subsequent income years. However, under section 91AAO(3B) of the Tax Administration Act 1994, this determination also applies for an income year beginning before the date of this determination for an investor in WMP that chooses that the determination applies for that year.

Dated this 16th day of March 2015.

John Trezise
Investigations Manager

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 15/01: INCOME TAX – TAX AVOIDANCE AND DEBT CAPITALISATION

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

This Question We've Been Asked is about s BG 1.

Introduction

1. At a tax conference held in November 2013 there was a discussion of whether s BG 1 would apply to certain scenarios. This Question We've Been Asked (QWBA) considers one of those scenarios concerning debt capitalisation. Three other scenarios were the subject of an earlier QWBA QB 14/11: *Income tax – scenarios on tax avoidance*, published in October 2014. [Also published in the *Tax Information Bulletin* Vol 26, No 11 (December 2014).]

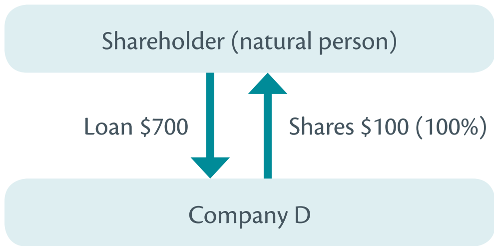
2. In the scenario, the arrangement and the conclusion reached are framed broadly. The objective is to consider the application of the general anti-avoidance provision of s BG 1. Accordingly, the analysis of the scenario proceeds on the basis that the tax effects under the specific provisions of the Act are achieved as stated. Also, the specific anti-avoidance provision of s GB 21 is not considered. However, it should not be presumed that this would always be the case. Also, except where shown below, additional relevant facts or variations to the stated facts might materially affect how the arrangement operates and a different outcome under s BG 1 might arise. Accordingly, the Commissioner's view as to whether s BG 1 applies must be understood in these terms.

3. Section BG 1 is only considered after determining whether other provisions of the Act apply or do not apply. Where it applies, s BG 1 voids a tax avoidance arrangement. Voiding an arrangement may or may not appropriately counteract the tax advantages arising under the arrangement. If not, the Commissioner is required to apply s GA 1 to ensure this outcome is achieved.

4. For a more comprehensive outline of the Commissioner's position on the law concerning tax avoidance in New Zealand, reference should be made to the Commissioner's Interpretation Statement IS 13/01: *Tax avoidance and the interpretation of sections BG 1 and GA 1 of the Income Tax Act 2007* (July 2013). [Also published in the *Tax Information Bulletin* Vol 25, No 7 (August 2013).]

Question

5. Whether s BG 1 applies in the following circumstances:
   - A New Zealand resident individual is the sole shareholder of Company D.
   - Company D is a qualifying company in the following financial position:



Cash	200
Total Assets	**$200**
Shareholder loan	700*
Share capital	100
Accumulated deficit	(600)
Total Equity and Liabilities	**$200**

* The shareholder loan is a "financial arrangement" for the purposes of the financial arrangements rules (FA rules) of subpart EW of the Act and is not part of a wider financial arrangement.

6. Under an arrangement the shareholder and Company D agree that:
   - Company D will issue additional shares;
   - the shareholder will subscribe $500 for the shares;
   - the shareholder's indebtedness to Company D for the share subscription of $500 will be offset against the shareholder loan; and
   - the company will repay the $200 balance of the loan in cash.

Answer

7. The Commissioner's view is that s BG 1 **would potentially apply** to this arrangement.

Explanation

8. The apparent objective of this arrangement is to eliminate the loan owed by Company D to its shareholder in circumstances where Company D issues further shares to that shareholder.

Tax effects

9. The tax effect of the loan ending is that s EW 29(3) requires Company D and the shareholder to each perform a base price adjustment (BPA) under s EW 31 in the income year the loan is eliminated.

10. The BPA is calculated using the formula in s EW 31(5):

    consideration – income + expenditure + amount remitted

11. In this scenario, it can be assumed that the income and expenditure items in the BPA formula are zero. The amount remitted item will also be zero for Company D as it is the borrower and unable to remit the debt. The relevant item in the BPA formula for present purposes is "consideration".

12. "Consideration" is relevantly defined as:

    > ... all consideration that has been paid, and all consideration that is or will be payable to the person for or under the financial arrangement, minus all consideration that has been paid, and all consideration that is or will be payable, by the person for or under the financial arrangement.

13. The consideration paid to Company D is the original amount of the loan of $700. The consideration paid by Company D is the sum of the $200 paid in cash and the $500 offset against the loan balance. Therefore, Company D's BPA calculation is:

    ($700 – ($200 + $500)) – $0 + $0 + $0 = $0

14. The tax effect of the arrangement for Company D is that no income or deduction will arise under the BPA as the calculation returns neither a positive nor a negative figure.

15. Similarly, the tax effect for the shareholder is that there is no income or deduction arising under the BPA as the shareholder's BPA calculation is:

    (($200 + $500) – $700) – $0 + $0 + $0 = $0

Parliament's purposes

16. Parliament's purposes for the FA rules is to require income and expenditure under financial arrangements to be recognised by the parties on an accrued basis over the term of the arrangement and to require them to disregard any distinction between capital and revenue amounts. The FA rules provide the tax outcomes for each of the parties to a financial arrangement. In this scenario, this will be the shareholder and Company D.

17. The Court of Appeal in *Alesco New Zealand Ltd v CIR* [2013] NZCA 40 also noted that the financial arrangements rules recognise the economic effect of a transaction. The court stated as follows (at [71]):

    > **In our judgment, the financial arrangements rules were intended to give effect to the reality of income and expenditure – that is, real economic benefits and costs.** They were designed to recognise the economic effect of a transaction, not its legal or accounting form or treatment. The question is whether the taxpayer has "truly incurred the cost as intended by Parliament".
    >
    > [Emphasis added]

18. One issue that arises is whether the parties to a financial arrangement are looked at in combination as a single economic unit. The Commissioner considers that reaching a view on this issue must be derived from the provision in question. While the FA rules are concerned with the overall economic effects of a transaction, in the Commissioner's view, this requires looking at each of the parties involved in isolation. Aside from company consolidation and amalgamation rules, there is no indication Parliament contemplated that the parties should be considered from the perspective of a single economic unit when it comes to the BPA. This conclusion regarding Parliament's purpose for the FA rules does not mean that where other provisions of the Act are in question Parliament may have contemplated a single economic unit perspective was appropriate.

19. Parliament's specific purpose for the BPA is for it to apply as a "wash-up" mechanism which operates when a financial arrangement matures or is disposed of. It operates to account for any gains or losses that have not already been treated as income and expenditure during the life of the financial arrangement. The BPA ensures that for each financial arrangement, all income is returned and all expenditure is deducted.

20. One situation where the BPA applies as a "wash-up" mechanism relevant to this scenario is where ultimately a financial arrangement is not repaid in full. In that case, the BPA formula item "consideration" will be positive for a borrower on account of the consideration received by them being greater that the consideration paid by them. Leaving aside any effect of the other items in the formula (income, expenditure and amount remitted), this would lead to a positive BPA figure. Under s EW 31(3) a positive BPA is income to the borrower (often referred to where there is a debt remission as "remission income"). In the present

scenario, had the shareholder of Company D forgiven $500 of the loan instead of subscribing for additional shares, Company D would have had remission income of $500 calculated under the BPA as follows:

($700 – $200) – $0 + $0 + $0 = $500

21. As a qualifying company, if Company D did not pay the tax on the remission income, the shareholder would have to meet the liability on account of the company (although nothing turns on the company being a qualifying company in terms of the application of s BG 1).

Facts, features or attributes

22. For the FA rules, a fact, feature or attribute Parliament would have expected to see present in an arrangement bringing a financial arrangement to an end is that there has been a discharge in economic terms of the obligations of each of the parties under the arrangement. That is, the borrower has borne the economic cost of repaying the loan and the lender has received an economic benefit.

23. This means that, on the maturity of a financial arrangement Parliament would expect that the consideration paid or payable by a person actually equalled the consideration received or receivable by another person in an economic sense.

24. Where this does not occur, Parliament therefore intended that income will arise for a borrower where an obligation under a financial arrangement, including principal, is forgiven or otherwise unpaid. This is intended to reflect that the borrower has made an economic gain, or has economically had an increase in wealth, by virtue of not having to repay an amount which they would otherwise be required to pay.

Extrinsic material

25. This view is supported by extrinsic materials including the *Final Report of the Consultative Committee on the Taxation of Income from Capital* (The Valabh Committee, October 1992). The committee proposed that debts remitted should be deemed to be repaid in full so that no remission income should arise. However, this proposal was rejected by the Government. In the foreword to that report, the Ministers of Finance and Revenue stated that this proposal was "inconsistent with [Government's] revenue strategy" (at [16]).

26. In a subsequent discussion document, *The Taxation of Financial Arrangements: A Discussion Document on Proposed Changes to the Accrual Rules*, December 1997 (the discussion document), the asymmetrical tax results arising from retaining the debt remission and bad debt rules were stated to be "an inevitable consequence of maintaining a capital-revenue boundary" (at [11.5]). The discussion document also referred to provisions that ignore remission income in the context of consolidated groups as a "substantial concession to the general rule" (at [11.32]).

Commercial and economic reality of the arrangement

27. Next it is necessary to analyse the commercial and economic reality of the arrangement to see whether the facts, features or attributes Parliament would expect to be present (or absent) to give effect to its purpose are present. In the present scenario this requires ensuring Company D has in reality discharged its obligations under the loan when viewed in a commercially and economically realistic way. If so, the tax effects of the arrangement will be within Parliament's contemplation for the FA rules.

28. Company D has discharged its obligations under the loan to the extent of the $200 cash it has paid to the shareholder and this amount is correctly treated as an item of consideration paid in its BPA calculation. Also, on the face of it, it is accepted that consideration for BPA purposes need not be cash but can be money's worth, such as where mutual obligations have been offset. This has occurred in this arrangement to the extent of the $500 share subscription. A financial arrangement is defined in s EW 3(2) in terms of an arrangement involving "money" being provided or received as consideration. The definition of "money" in s YA 1 specifically includes money's worth, whether or not convertible into money, and s EW 31 includes within the BPA calculation all consideration paid to or by the person.

29. However, a s BG 1 enquiry is not limited to the legal form of the arrangement. The whole of the arrangement is examined to establish its commercial and economic reality. Given the section at issue, the avoidance inquiry examines whether the loan is in reality repaid, as Parliament would expect where there is no remission income. Therefore, the arrangement is examined to see whether Company D repays the loan in a commercially and economically real sense, and whether the shareholder is repaid in a commercially and economically real sense.

30. In the scenario, there is no actual or economic cost to Company D in issuing shares to the existing shareholder. It has not suffered the full economic cost of repaying the loan. The shareholder, in turn, has not received an economic benefit. There is no change to the shareholder's interest in the company so the shareholder will not receive a "gain" in value from

the receipt of the shares commensurate with the face value ascribed to them by the parties. Company D will simply have more shares on issue, and, the existing shareholder will hold more shares in a company in which they already owned all of the shares. The shareholder effectively finances the repayment of $500 of the loan themselves. There is an element of artificiality and contrivance in this aspect of the arrangement.

31. Accordingly, the parties have not given or received full repayment of the loan when viewed in commercial and economic terms. In commercial and economic reality, the effect of the arrangement is that from Company D's perspective it discharges its obligations under the loan thereby eliminating a liability for $700 without it suffering any economic loss or expending money or money's worth beyond the $200 paid. This conclusion does not turn on the fact that Company D is insolvent.

32. When looking at the financial consequences of the arrangement it should be borne in mind that the relevant provision at issue is s EW 31 and the BPA outcome arising for Company D. Parliament's relevant purpose is concerned with a single taxpayer and whether that taxpayer has remission income. As stated at paragraph 18, except for consolidated groups, there is no relevant Parliamentary purpose that provides for the parties to the financial arrangement to be looked at as if they were a single economic unit when determining if remission income has arisen. The FA rules apply to individual taxpayers. When viewed in a commercially and economically realistic way the conclusion is that the loan has, in reality, been remitted by the shareholder to the extent of $500.

33. The Commissioner also considers the commercial and economic reality of the arrangement would be the same even if the shareholder had subscribed for the shares in cash for $500 and Company D had fully repaid the loan in cash.

Applying the Parliamentary contemplation test

34. Accordingly, it is the Commissioner's view that the arrangement does not appear to exhibit the necessary facts, features or attributes that Parliament would have expected to see present to give effect to its purposes for the FA rules and the BPA in particular. Again, in the Commissioner's view, this means the arrangement could be outside Parliament's purposes for the FA rules as it circumvents remission income arising under the BPA. While the Commissioner accepts that arguments could be made to the contrary, on balance, it is considered that the arrangement has tax avoidance as a purpose or effect.

35. It has been suggested that the above conclusion is inconsistent with the view of the High Court in *AMP Life Ltd v CIR* (2000) 19 NZTC 15,940 (HC), where McGechan J commented (at [129]) that a debt capitalisation on its own would not be a tax avoidance arrangement. However, in the Commissioner's view, his Honour's comment does not necessarily reflect a considered judicial view on the issue of debt capitalisation in the context of tax avoidance. The BPA and debt remission income were not at issue in the case, and McGechan J was responding to the arguments before him concerning whether there was actually an "arrangement". The Commissioner also notes that the case was heard and decided prior to the Parliamentary contemplation test being set out authoritatively by the Supreme Court in *Ben Nevis Forestry Ventures v CIR* [2008] NZSC 115. There is no indication that when making his comments concerning debt capitalisation at [129] McGechan J was directly considering what Parliament contemplated for the FA rules in the present context.

Merely Incidental test

36. The next step is to test whether the tax avoidance purpose or effect of the arrangement is merely incidental to a non-tax avoidance purpose or effect. If so, s BG 1 will not apply to the arrangement, even though the arrangement has a tax avoidance purpose or effect. A "merely incidental" tax avoidance purpose or effect is something which follows from or is necessarily and concomitantly linked to, without contrivance, some other purpose or effect.

37. Sometimes, quite general purposes are put forward to explain arrangements, and there is a question how to treat such purposes in the context of the merely incidental test. General purposes that can potentially be achieved in several different ways will not explain the particular structure of the arrangement. Section BG 1, including the merely incidental test, is applied to the specific arrangement entered into. In the present context, the elimination of the shareholder loan or the alleviation of the company's insolvency would be insufficient to explain the particular arrangement and to establish that the tax avoidance purpose or effect is merely incidental to these purposes or effects. This is the situation given the limited facts of the arrangement in this scenario. The tax avoidance purpose or effect appears to be either the sole or the main purpose or effect of the arrangement. Accordingly, the tax avoidance purpose or effect is unlikely to be merely incidental to another purpose or

effect of the arrangement and the arrangement in the scenario fails the merely incidental test.

38. However, the Commissioner accepts that in a particular case it may be possible for any tax avoidance purpose or effect of an arrangement involving debt capitalisation to be merely incidental to some non-tax avoidance purpose or effect. If so, s BG 1 would not apply. For this to be the case, the non-tax avoidance purposes or effects would need to explain the involvement of a debt capitalisation within the particular structure of the arrangement. An example may be where a regulatory body imposes a certain approach to the restoration of solvency to a subsidiary.

Reconstruction

39. If s BG 1 is to apply to give rise to remission income for Company D, it might be thought that there should be a corresponding deduction for the shareholder as part of a reconstruction under s GA 1. However, Parliament has made a deliberate choice for the FA rules that sometimes it will produce an asymmetrical result. An asymmetrical result can arise where the lender is not entitled to a deduction. For instance, had the shareholder in this scenario remitted the $500, the shareholder would not have a negative BPA (a negative BPA is a deduction under s EW 31(4)). This is because the BPA formula item "amount remitted" would include any amount not included in the item "consideration" on account of the amount being remitted by the shareholder. This would give a BPA calculation of:

($200 – $700) – $0 + $0 + $500 = $0

40. For the shareholder to obtain a deduction for remitting the financial arrangement they would need to satisfy the bad debt rules in s DB 31. Relevant to the present scenario, if the parties are associated (as they are here) no bad debt deduction is permitted (s DB 31(3)). To be consistent with this, it would follow that any application of s BG 1 in this scenario would not result in the shareholder being provided with a $500 deduction as a consequential adjustment under s GA 1.

Factual variations

41. This arrangement can be contrasted with the situation where there is an issue of shares to a third party by a solvent company. In that case, it is more likely that the shares issued as consideration will have an economic effect. The existing shareholders of a company would suffer a dilution of their investment. The third party would obtain an equity interest in the company and there may be a change in the effective ownership of the company. This type of situation is more likely to have been contemplated by Parliament as one where no remission income arises under the BPA (although this would need to be considered on a case-by-case basis).

42. Given the above, it might be asked whether the fact that the company is solvent is relevant in the third-party lender situation. The question is answered by considering what facts, features and attributes Parliament would expect to see present. Parliament would expect that a lender receives repayment in a commercially and economically real way. In some situations, depending on the facts, shares in an insolvent company may have some value to a third-party lender. Examples could be where there is the prospect of the company regaining solvency or it has some valuable assets. In most other situations, shares in an insolvent company will not have any value to a third-party lender and so will not constitute repayment of a loan in a real sense.

References

Subject references
Base price adjustment; Consideration; Debt capitalisation; Debt remission; Financial arrangement; Merely incidental; Tax avoidance; Tax avoidance arrangement
Legislative references
Income Tax Act 2007 – ss BG 1, EW 3, EW 29, EW 31, GA 1, s YA 1 definition of "money"
Case references
AMP Life v CIR (2000) 19 NZTC 15,940 (HC)
Alesco New Zealand Ltd v CIR [2013] NZCA 40
Ben Nevis Forestry Ventures Ltd v CIR [2008] NZSC 115
Related rulings/statements
IS 13/01: *Tax avoidance and the interpretation of sections BG 1 and GA 1 of the Income Tax Act 2007* (July 2013)
Other references
Final Report of the Consultative Committee on the Taxation of Income from Capital (The Valabh Committee, October 1992)
The Taxation of Financial Arrangements: A Discussion Document on Proposed Changes to the Accrual Rules, (December 1997)

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.

DIVIDEND STRIPPING ASSESSMENTS UPHELD ON APPEAL

Case	Beacham v Commissioner of Inland Revenue
Decision date	14 November 2014
Act(s)	Income Tax Act 2004, Tax Administration Act 1994
Keywords	Company restructure, dividend stripping, tax avoidance, shortfall penalties

Summary

The taxpayers' appeal of the Taxation Review Authority's ("TRA") decision upholding the Commissioner of Inland Revenue's ("the Commissioner's") assessments was dismissed. The taxpayers admitted that the restructuring of their company ownership was a tax avoidance arrangement but challenged the Commissioner's reconstruction of their income as a "deemed dividend" under s GB 1(3) of the Income Tax Act 2004 ("ITA 2004"). The imposition of shortfall penalties for taking an abusive tax position was also upheld.

Impact of decision

This is the first case in which the Commissioner's reconstruction under the dividend stripping rule in s GB 1(3) of the ITA 2004 has been considered by the High Court. The decision also reconfirms established principles around the wide powers of reconstruction under s GB 1 of the ITA 2004.

Facts

The taxpayers restructured the ownership of their two companies (Beacham Holdings Ltd ("Holdings") and Beacham Jaguar Ltd ("Jaguar")) by selling their shares in those companies to a holding company, Beacham Group Limited ("Group"). Group was incorporated for that purpose following receipt of tax advice. The taxpayers remained 50/50 shareholders and directors of Group as they had been of Holdings and Jaguar.

Prior to the restructuring, Holdings had retained profits of $1,856,277.19 and Dr Beacham's shareholder current account was overdrawn by approximately $1 million. The purchase price for the shares was $1.84 million and payment for the sale of shares was effected by way of journal entry. Group funded the purchase of the shares with an on-demand interest-free loan from the taxpayers. Following the restructure, Dr Beacham's overdrawn current account in Holdings had been repaid and there was a further $500,000 available to be drawn down in the future. The taxpayers treated the amounts received from the sale of their shares in Holdings to Group as capital.

The taxpayers' income in the 2007 income tax year was assessed by the Commissioner on the basis that:

- the $1,735,000 received from Group was deemed to be a dividend under s GB 1(3) of the ITA 2004; or alternatively,
- the amount received would be reconstructed as the taxpayers' income under s GB 1(1) of the ITA 2004.

The Commissioner also imposed shortfall penalties for taking an abusive tax position under s 141D of the Tax Administration Act 1994 ("TAA").

While the taxpayers accepted they sold their shares in Holdings to Group as part of a tax avoidance arrangement, the taxpayers argued that there was no need for any reconstruction of their income for the 2007 income tax year and that the Commissioner had exceeded the scope of her powers of reconstruction in so doing. The taxpayers argued that s BG 1 of the ITA voided the arrangements and thereby eliminated any tax benefit. The taxpayers submitted there was no outstanding tax advantage to be counteracted because the current account loans from Holdings remain payable by them for income tax purposes.

Decision

The appeal was dismissed.

The Court confirmed that s BG 1(1) of the ITA operates to void an arrangement only "as against the Commissioner for income tax purposes" and does not act to void an arrangement as between the parties to an arrangement. Although disregarding some tax avoidance arrangements will be sufficient to negate the tax advantage achieved by a taxpayer, for other arrangements, it may be necessary for the Commissioner to use Part G to counteract a tax advantage obtained from or under a tax avoidance arrangement by using her powers of reconstruction.

The Court found this was a case in which the arrangement being void against the Commissioner did not remove the tax advantage to the taxpayers. In this case the arrangement had the effect of repaying Dr Beacham's overdrawn account in Holdings, leaving the balance of the purchase price for the shares available to be accessed in the future.

Was the reconstruction carried out within the scope of s GB 1(3) or s GB 1(1)?

The only element of s GB 1(3) of the ITA 2004 that was not admitted was whether it was reasonably open for the Commissioner to form the view that the consideration received by the appellants for the sale of their shares in Holdings was "consideration in substitution for a dividend" which the appellants would have derived or might have been expected to have derived.

The Court found that the purpose and effect of the arrangement was to transfer value from the taxpayers' companies to the taxpayers themselves. Had the value been transferred directly, that consideration would have been a taxable dividend. The Court accepted the Commissioner's submissions that the concept of dividend for tax purposes was broader than that under the company law principles. The taxpayers had received the benefit of the consideration for the shares for no economic cost and after the restructure they still own the shares in Holdings (via Group). Therefore, it was reasonably open for the Commissioner to form the view that the consideration received by the taxpayers for the sale of their shares in Holdings was "consideration in substitution for a dividend" and subject to s GB 1(3) of the ITA.

The alternative basis on which the Commissioner made her assessments under the general reconstruction provision in s GB 1(1) of the ITA was also upheld. Where an arrangement is void under s BG 1 of the ITA and the taxable income of any person is affected by that arrangement, the Commissioner is entitled to adjust the amounts included in calculating the taxpayers' taxable income "in the manner the Commissioner thinks appropriate, so as to counteract any tax advantage obtained … under that arrangement".

Shortfall penalties

The Court found that the Commissioner's imposition of shortfall penalties under s 141D of the TAA was correct.

The Court determined that the arrangement was entered into with the dominant purpose of avoiding tax. The taxpayers did not lead any evidence to establish any commercial or other purpose for the restructuring of their companies. Goddard J found it relevant that the taxpayers' tax consultant stated the purpose of the arrangement was "to offset Mr and Mrs Beacham's (G&V) value of the shares against the overdrawn current account in Beacham Holdings Ltd …".

Further features that indicated the dominant purpose of the arrangement was to avoid tax were that:

- the structure of the arrangement meant there was no real or economic cost incurred by the taxpayers;
- the taxpayers retained their ownership or control of all the relevant companies;
- Dr Beacham's overdrawn current account with Holdings was repaid in full; and
- there were no longer any retained profits in Holdings available to be paid directly to the taxpayers.

INPUT TAX DEDUCTIONS LIMITED UNDER S 21HB WHERE THE SUPPLIER AND THE RECIPIENT ARE ASSOCIATED PERSONS

Case	TRA 008/14 [2014] NZTRA 15
Decision date	20 November 2014
Act(s)	Goods and Services Tax Act 1985, Tax Administration Act 1994
Keywords	Associated persons rules, commercial dwelling, input tax credit

Summary

The issue for the Taxation Review Authority ("TRA") was whether the input tax credit claimed by the disputant under s 21HB of the Goods and Services Tax Act 1985 ("GSTA") for the purchase of the house before 1 April 2011 is limited to zero, pursuant to s 3A(3) of the GSTA definition of "input tax", where the supply is from an associated person.

The TRA found that the Commissioner of Inland Revenue's ("the Commissioner's") decision to disallow the input tax credit claimed was correct. The TRA found that s 21HB of the GSTA is intended to have retrospective effect. It is the original acquisition of the goods or services with all of their attaching circumstances that is referred to in s 21HB(3) of the GSTA. Further, the purpose of the transitional rules contained in s 21HB was to put a registered person affected by the 2010 amendments in the same position that they

would have been in had they carried on a taxable activity at the time they purchased the particular goods or services.

Impact of decision

There is now authority that provides s 3A(3)(a) of the GSTA limits input tax deductions claimed under s 21HB where the supplier and the recipient are associated persons.

Facts

This proceeding involved a challenge to the Commissioner's decision to disallow the input tax credit claimed for the purchase price of a property claimed in the disputant's goods and services tax ("GST") return for the period ended 30 September 2011. The property was used for the provision of short-term rental accommodation. The input tax credit claimed was disallowed on the basis it was limited to zero due to the associated person rules.

On 18 February 2005, Mr X purchased a residential property ("the Property") from an unregistered person for $635,000. No GST was included in the transaction as the property was a private residence. Mr X was not registered for GST in his personal capacity. From the date of the purchase until early 2007, Mr X spent in excess of $300,000 and many weekends making capital improvements to the Property.

During 2007, Mr X who then owned 99% of the shares in the disputant transferred the Property to the disputant, an associated person, for $1,100,000. The disputant treated the Property as a "dwelling" for GST purposes and considered the supply to be GST-exempt based on advice received from a tax specialist. An independent valuation of the Property and chattels as at 20 February 2007 showed the total value of the Property as being $1,100,000 (GST inclusive).

In 2010, the definition of "commercial dwelling" in s 2 of the GSTA was amended to include accommodation in homestays, farmstays, bed and breakfast establishments, and serviced apartments with effect from 1 April 2011. The definition of "dwelling" was also amended.

With effect from 1 April 2011, persons or businesses who supply short-term accommodation and whose total supplies in any 12-month period exceed the $60,000 threshold, were required to register for GST and charge GST on their supplies under s 51 of the GSTA. They were also entitled to claim GST input tax based on the various provisions of the GSTA.

Section 21HB of the GSTA was introduced in 2010 to allow taxpayers now falling under the new definition of "commercial dwelling" to apply for input tax credits on goods or services originally not acquired for the principal purpose of making taxable supplies.

On 28 June 2012, the disputant registered for GST with effect from 1 April 2011. The first GST return for the six-month period ending 30 September 2011 was filed on 14 September 2012.

This GST return included an input tax credit claim for the value of the property and for the extensive renovations/ refurbishments carried out by Mr X during his period of ownership and also by the disputant. The portion of the input tax credit claim which relates solely to the acquisition of the Property is $119,622.87.

The disputant's claim for input tax for the period ended 30 September 2011 was allowed in part by the Commissioner but disallowed in relation to the purchase price of the Property on the basis the associated person rules in s 3A(3)(a) of the GSTA limited the GST claimed to zero. The calculation contained in s 3A(3)(a) of the GSTA relating to associated persons is the lesser of the following three amounts:

1. the tax included in the original cost of the goods to the supplier (being zero); and
2. the tax fraction of the purchase price ($119,628.07); and
3. the tax fraction of the open market value of the supply ($119,628.07).

Decision

The disputant argued that the correct interpretation of s 21HB(3) of the GSTA was that the only attribute of the original supply attached to the acquisition was that of cost. The disputant submitted that the acquisition, being the purchase of the property, claimed under s 21HB(3) is a statutory fiction by which the goods or services are deemed to have been acquired on 1 April 2011 at the original cost of supply but with no other attaching attributes of the original supply.

The disputant argued that the Commissioner's interpretation of s 21HB (that the disputant is not eligible for a 15% input tax credit and on any future sale of the property the disputant will only be able to retain 85% of the sale proceeds) effectively deprives the disputant of part of its assets. The disputant argued that this results in unfairness that Parliament could not have intended.

The Commissioner submitted that it is the original acquisition of the goods or services with all of their attaching circumstances that is referred to in s 21HB(3) of the GSTA. The Commissioner argued this interpretation is supported by s 21HB(2) which provides that the disputant is entitled to an input tax deduction under s 20(3C) to the extent to which a deduction has not been made under the old apportionment rules. Such a deduction could only have been made on the original supply of the goods, not a fictional supply.

Further, the Commissioner submitted that in considering s 21HB of the GSTA, it is necessary to consider s 3A(3)(a) and the amended definition of "associated persons" which was intended to remove the incentive for persons to enter into transactions primarily to gain a significant tax advantage. Its specific purpose was to limit the input tax credit available in relation to supplies of secondhand goods between associated parties to remove the tax advantages. While the associated persons limitation in s 3A(3)(a) can be unfair where a taxpayer acquires goods or services from an associated person for legitimate reasons, this unfairness was acknowledged and a conscious choice by Parliament.

In addition, the Commissioner submitted that Parliament was aware when it implemented the associated persons regime that it would create inequity between transactions entered into between associated persons and non-associated persons. However, this inequity was outweighed by the potential revenue consequences of the provisions. The purpose of s 21HB of the GSTA was to put a registered person affected by the 2010 amendments in the same position they would have been in had they carried on a taxable activity at the time they purchased the particular goods or services. To provide an associated person with an input credit deduction in the case of s 21HB of the GSTA would place associated persons in a more advantageous position than if the rules had not been put in place and would be inconsistent with the associated persons regime.

Judge Sinclair found the meaning of ss 21HB(2) and (3) of the GSTA plain and unambiguous. Further, Judge Sinclair was satisfied that on the wording of s 21HB(1) it is clear that s 21HB is intended to have retrospective effect. She accepted the purpose of the transitional rules contained in s 21HB were to put a registered person affected by the 2010 amendments in the same position they would have been in had they carried on a taxable activity at the time they purchased the particular goods or services. She found Parliament has done this by retaining the general input tax definition contained in s 3A(3)(a) which limits input tax deductions where the supplier and the recipient are associated persons.

UNSUCCESSFUL APPLICATION FOR REVIEW

Case	Mawhinney v Commissioner of Inland Revenue
Decision date	3 December 2014
Act(s)	Judicature Act 1908, Tax Administration Act 1994
Keywords	Security for costs, disputes process, strike out

Facts

This decision relates to an application for review of an Associate Judge's decision filed by Peter William Mawhinney as trustee of the Forest Trust ("the Trust"). The decision which the Trust sought to review was that of Associate Judge Christiansen striking out part of the Trust's Statement of Claim in damages and ordering the Trust to pay $40,000 in security for costs (*Mawhinney v Commissioner of Inland Revenue* [2014] NZHC 1554).

The underlying dispute involves a claim for a GST refund of $67,011.65, which the Commissioner of Inland Revenue ("the Commissioner") has reassessed to nil pursuant to s 89C(eb) of the Tax Administration Act 1994 ("TAA").

On 12 July 2012, the Trust filed a statement of claim containing claims for 19 separate breaches of statutory duty; a claim for money had and received; and claims for six breaches of duty of care. The Trust sought damages and/or compensation of $5,113,810.72.

The Trust has filed two further iterations of its Statement of Claim, the third of which contained an additional fourth cause of action purporting to be a challenge under Part 8A of the TAA.

In April 2014, the Commissioner applied to strike out the fourth cause of action and for further security for costs. These matters were heard by Associate Judge Christiansen who delivered his judgment on 4 July 2014 (*Mawhinney v Commissioner of Inland Revenue* [2014] NZHC 1554). Associate Judge Christiansen determined that the fourth cause of action was a duplication of process (being already subject to the TAA disputes procedures, determined by Cooper J (*Mawhinney v Commissioner of Inland Revenue* [2013] NZHC 3564), and before the Court of Appeal (*Mawhinney v Commissioner of Inland Revenue* [2014] NZCA 450; (2014) 26 NZTC 21-101 per Ellen France J), was prima facie vexatious and should be struck out.

Further, the Associate Judge ordered security for costs in the sum of $40,000 to be paid into Court and to be held pending determination of the proceeding. He stayed the proceeding until lodgement of the payment.

Decision

The application for review was dismissed.

Strike-out application

The Trust submitted that the Associate Judge erred in holding that the fourth cause of action was duplicitous in the sense it had already been determined by Cooper J, arguing that the disputes procedure set out in Part 4A of the TAA had been concluded. Further, it said the Associate Judge had erred in striking out the fourth cause of action on the basis that no challenge notice had been issued because only s 138B(3) of the TAA requires the issuance of a challenge notice. The Trust submitted that Cooper J concluded that the dispute should be determined by a challenge under s 138B(1) of the TAA.

The Trust further submitted that the Associate Judge erred in his interpretation of *Allen v Commissioner of Inland Revenue* ([2006] NZSC 19, [2006] 3 NZLR 1, because that was a decision under s 138B(3), not s 138B(1). Once the Part 4A disputes procedure had come to an end, it was up to the taxpayer to choose the forum for a challenge under Part 8A (either the Taxation Review Authority or the High Court) and that adding the fourth cause of action was an appropriate response to Cooper J's decision.

The Commissioner, in reply, pointed out that s 138B(3) of the TAA applies to a situation where the taxpayer is the initiator of the dispute, and as the Trust is the initiator of this dispute, it must apply. The Commissioner also drew Justice Brewer's attention to Cooper J's determination that the Part 4A procedure must be determined by the statutory processes before any challenge under Part 8A arises. Accordingly, no cause of action purporting to invoke Part 8A could stand.

The Court held that the Associate Judge was right to strike out the fourth cause of action as the Trust was bound by the decision of Cooper J that the issue of the assessment of GST which is the subject of the fourth cause of action is to be decided within the statutory disputes and challenge procedures in the Act. Justice Brewer reiterated an assertion that the Part 4A procedure has concluded is itself a matter for the Part 4A process.

Security for costs application

Mr Mawhinney submitted that the Associate Judge erred by focusing on the ability of the Trust to pay an award of costs; rather, he should have focused on whether Mr Mawhinney, as plaintiff, was able to pay costs. This submission is based on the premise that a Trust is not itself a legal person and can only act through trustees.

Mr Mawhinney further submitted that even if security for costs should have been ordered, the Associate Judge should not have directed that the security be paid into Court in money, as security is able to be provided by other means and it is up to the plaintiff how security for costs should be satisfied.

In response, the Commissioner submitted that the Associate Judge was correct to look to the assets of the Trust because the Trust is the plaintiff, not Mr Mawhinney acting in his personal capacity. Even if a trustee is personally liable, the fact that he would have recourse to the assets of a third party (referred to at [15] of Brewer J's judgment) for security might in itself suggest that security is appropriate (*Highgate on Broadway Ltd v Devine* [2012] NZHC 2288, [2013] NZAR 1017); and r 5.45 of the High Court Rules 2008 says that an order for security can be by way of payment or by some other means. The Associate Judge was entitled to prefer cash.

Justice Brewer determined that Associate Judge Christiansen did not make an error in the exercise of his discretion, commenting that having considered the matters he was required to consider, the Associate Judge made the decisions that were open to him.

His Honour found there was no doubt that the Trust could not meet an order for costs out of its own resources and that it was clear that Mr Mawhinney had not provided sufficient evidence to show that he, personally, could meet any award of costs.

Justice Brewer further determined that r 5.45 of the High Court Rules leaves it up to the Judge to decide whether security should be given by paying a sum into Court or by giving some other security.

Addendum

The Court further ordered that the Trust could apply to the Associate Judge to vary his order to allow security for costs to be provided by a second mortgage over the property. However, the Trust would still have to satisfy the Associate Judge that this would constitute proper security.

SUCCESSFUL APPEAL BY THE COMMISSIONER

Case	Commissioner of Inland Revenue v John Curtis Developments Limited
Decision date	28 November 2014
Act(s)	Income Tax Act 2004, Income Tax Act 2007, Tax Administration Act 1994
Keywords	Capital/revenue, supply

Facts

In 1988, the taxpayer (a property developer) purchased a large block of land in Christchurch and began construction of a retail shopping centre on the site.

In 2003, before the development was fully complete, the taxpayer sold the centre to AMP. The agreement for sale and purchase between the taxpayer and AMP ("the Agreement") contained an "option" which required the taxpayer to use its best endeavours to lease and build the undeveloped part of the centre.

The sites to be constructed and completed were described as Future Development Sites ("the FDS") in the agreement.

Between 2004 and 2009, the taxpayer found tenants and procured unconditional agreements to lease. The taxpayer received "development payments" from AMP as the new tenants started paying rent.

The Taxation Review Authority ("TRA") found the following in its decision of 23 October 2013:

1. The Agreement was a single, unitary contract for sale and purchase of the completed centre.
2. The adjustment provisions of the Agreement clearly envisaged the completion of the development and were consistent with the disputant's position that the Agreement provided for the sale and purchase of the completed centre.
3. The development option was not in fact an option that could be exercised. If the taxpayer failed to develop all of the proposed FDS units, it would be in breach of the obligation to use the best endeavours to develop the site.
4. What was supplied was a capital asset as the Agreement was for a single indivisible supply of a completed shopping centre.
5. FDS development payments were not taxable. No shortfall penalties were payable.

The TRA also rejected the alternative submission of the Commissioner of Inland Revenue ("the Commissioner") that the payments were taxable under s CB 3 of the Income Tax Act 2007 as derived from an undertaking entered into for the purpose of making a profit.

The Commissioner appealed the TRA's decision.

Decision

The Court allowed the Commissioner's appeal.

Two preliminary points

The Court began by considering two preliminary points: parole evidence; and the respondent's submission that the Commissioner had impermissibly shifted her grounds in the TRA, departing from her Statement of Position ("SOP").

In relation to the parole evidence issue, Kos J did not consider subjective declarations of the parties as to their intentions during pre-contractual negotiations relevant. His Honour did not consider them to be capable of providing objective guidance as to the intended meaning.

In respect to the second preliminary point, Kos J considered the Court of Appeal's decision in *Commissioner of Inland Revenue v Zentrum Holdings Limited* [2007] 1 NZLR 145 (CA) ("*Zentrum*"), determining that it was binding on the High Court. His Honour then noted that *Vinelight Nominees Ltd v Commissioner of Inland Revenue* [2013] NZCA 655, (2013) 26 NZTC 21,055, distinguished between SOP and pleadings, finding that the Commissioner's SOP need only give an outline of the facts, evidence and propositions of law in sufficient "detail to fairly inform the disputant".

Kos J was satisfied that the Commissioner had done so here and that there was no place in the law for "arid literalism where clear meaning was conveyed despite form".

His Honour stated that even if that was not the case, the pleading would be permitted under s 138G(1) of the Tax Administration Act 1994 ("TAA") as response to the assertion made in the taxpayer's SOP.

One supply or two

The Court noted that a single transaction in a single contract may nonetheless contain two or more supplies for tax purposes. Some receipts may be capital, whereas others are income. Whether that is or not, is to be assessed in accordance with the principles stated in *Wattie v Commissioner of Inland Revenue* (1997) 18 NZTC 13,927 (CA) (upheld on appeal: [1999] 1 NZLR 529 (PC)).

Kos J held that the agreement in this case contains two distinct and separately identifiable supplies. The first is the transfer of land, payment for which is a capital receipt. The second is letting and construction services concerning the still undeveloped FDS land, now owned by a third party.

His Honour did not accept that the Agreement, properly construed, provides simply for the sale and purchase of a completed retail development.

In particular, his Honour did not consider that the clauses in the Agreement relied upon by the disputant provided a clear pointer to the Agreement containing a single indivisible supply; a completed shopping centre. The fact that the parties had used a broad label to describe what is being transacted did not necessarily characterise the whole of the transaction from a taxation perspective.

Kos J instead noted that several clauses in the Agreement showed the "functional and temporal" separation of the two supplies. His Honour disagreed with the TRA's findings in relation to these clauses, concluding as follows:

a) The Agreement divided the consideration into two distinct sums: the purchase price and the development payments. Each clearly attributable to a different type of performance.

b) The adjustment provisions were not a financial penalty for non-completion of the development and did not demonstrate that the taxpayer was compelled to deliver a completed shopping centre.

c) The taxpayer would not be in breach of the agreement if it failed to complete development of the FDS sites, it was only obliged to use best endeavours to develop the FDS under the development option. (The Court adopted the approach to best endeavours clauses taken in *Kingdon Development Ltd v Saiteys McMahon Property Ltd* CIV-2007-404-3760, 17 October 2007 at [21], noting that the development option did not require the taxpayer to develop a site at its own cost in the event that neither the taxpayer nor AMP had been able to find tenants.)

d) After the settlement of the sale of the land, when the development option took practical effect, the land no longer belonged to the taxpayer. It belonged to AMP. Therefore, all work to be done was on land belonging to AMP, not the taxpayer.

e) The Agreement contemplated cancelling the development option separately from the principal agreement.

Kos J considered that the taxpayer, having chosen by its agreement to separate the form and timing of distinct obligations to supply, could not now re-amalgamate them because it better suited its taxation objectives. It could not have it both ways.

Shortfall penalties

The Court also held that the TRA upheld the taxpayer's position in a "cogent and careful" decision. Therefore, the taxpayer's position, while wrong, was rationally arguable so shortfall penalties were not imposed.

DEDUCTION DENIED FOLLOWING CESSATION OF PROPERTY DEVELOPMENT BUSINESS

Case	TRA 008/13 [2014] NZTRA 17
Decision date	9 December 2014
Act(s)	Tax Administration Act 1994, Income Tax Act 2007, Resource Management Act 1990
Keywords	Deductions, expenditure incurred in the ordinary course of business, cessation of business, resource consent

Summary

The taxpayer entered into a sale and purchase agreement to purchase land for the purpose of undertaking a large retail and residential development. The taxpayer obtained resource consent to build the development but the sale and purchase agreement was cancelled following civil litigation between the taxpayer and the vendor of the land. The taxpayer sought to deduct all expenses incurred in relation to the land and subsequent court proceedings with the vendor. The Commissioner of Inland Revenue ("the Commissioner") denied deductions incurred after the taxpayer had sought to cancel the agreement for sale and purchase on the basis it was no longer in business, as it did not have the intention to make a profit once it sought to extricate itself from the agreement.

Impact of decision

The Taxation Review Authority ("TRA") has confirmed that deductions will not be available after the cessation of a business.

Facts

The disputant entered into a sale and purchase agreement ("the Agreement") in February 2006 for a block of land ("the Land") from AB Limited ("the Vendor").

The Agreement was conditional on the Vendor obtaining resource consent for the subdivision of a larger property to be able to provide title to the Land. The disputant and the Vendor subsequently agreed to extend the date for the satisfaction of this condition.

On 10 March 2008, the Vendor's lawyers wrote to the disputant's lawyers recording that the condition relating to the subdivision had not been satisfied and therefore the Agreement was at an end. On 17 March 2008, the disputant's lawyers replied stating that it did not accept the Vendor's purported cancellation of the Agreement.

On 23 April 2008, the disputant was granted resource consent for land use to build a mixed retail/apartment development on the Land.

On 1 May 2008, the disputant issued proceedings against the Vendor seeking an order for specific performance of the Agreement.

On 2 July 2008, resource consent for the subdivision of its property was granted to the Vendor. On 24 July 2008, the disputant's lawyers replied to the vendor stating that "our client now accepts the unlawful termination as repudiation and the contract is therefore at an end subject to the right to seek damages for losses incurred".

The disputant initiated court proceedings in the High Court for specific performance of the Agreement, but later amended its claim (after the contract was declared unconditional) to seek damages from the Vendor. Those proceedings were settled in December 2010.

On 9 December 2011, the disputant entered into an agreement to sell the documentation and resource consent rights related to the project ("the Project Rights Agreement"). However, the Project Rights Agreement did not proceed and the resource consent for land use eventually expired on or about 5 March 2013.

The Commissioner disallowed all income tax deductions claimed by the disputant after 24 July 2008 on the basis that the disputant was not in business after the date it sought to cancel the Agreement.

The disputant claimed that its business did not cease until on or about 5 March 2013 when the resource consent rights for the project expired or when the parties entered into a settlement agreement in December 2010. Alternatively, it argued the expenditure was deductible as a revenue expense.

Decision

The Commissioner's assessments for the 2009, 2010 and 2011 years were confirmed and the imposition of a shortfall penalty for the 2011 year was upheld.

Cessation of business

The TRA found the disputant's focus clearly changed after 24 July 2008 and its time, effort and resources moved from advancing settlement of the purchase of the Land to getting out of the Agreement and recovering the deposit and costs incurred. The TRA did not accept that there was any temporary cessation of business by the disputant after 24 July or that the disputant had any expectation of resuming its business of property development following the High Court proceedings between the disputant and the Vendor.

The TRA dismissed the disputant's alternative argument that it ceased being in business after the cancellation of the Project Rights Agreement in December 2011 or on the expiry of the resource consent. It recognised that the disputant's business was that of property development and not one of selling resource consents.

Land held on revenue account

The disputant also argued that the Land was acquired for the purpose of resale and was therefore held on revenue account. It contended that any gains derived by the disputant would have been taxable under ss CB1, CB3, CB6 or CB7 of the Income Tax Act 2007 ("ITA"). Taxable profit could have been derived from the sale of its equitable interest in the Land, the sale of the Land, damages awarded in the High Court proceeding or from the sale of the resource consent and plans.

The disputant went on to argue that, accordingly, any expenses incurred are on revenue account and deductible under s DA1(1)(a) of the ITA. This would include at [60]:

1. a payment made by the disputant to escape an onerous agreement; or
2. a loss of the disposal of equitable rights in and to the land; or
3. a payment of damages.

The TRA did not consider there to be sufficient nexus between the expenses claimed and any income-earning process undertaken by the disputant. It found that the disputant's payment was to escape the onerous contract after the business had ceased. Furthermore, the only income the disputant earned after 24 July 2008 was interest on the deposit paid. The TRA agreed with the Commissioner that there was no nexus between the disputant's deriving or earning its interest income and the expenditure incurred to extract itself from the Agreement.

The TRA found no income was derived from disposing of the land and therefore s CB6 of the ITA did not apply.

Finally, the TRA did not accept the disputant's argument that payment of damages is an "occupational hazard for property developers" and is therefore an "expected expense".

Expenses incurred before business ceased

The disputant argued that as it paid the deposit of $1,942,655 on 1 June 2007, the loss related to the forfeiture of part of the deposit was an expense to which the disputant had been legally committed from that date (being at a time when the disputant was in business) as were some of the legal fees.

The TRA dismissed this argument, finding there was not sufficient nexus under s DA1(1)(a) of the ITA for two reasons. First, the legal fees were incurred by the disputant trying to get out of the property development project. Second, the settlement sum paid to the Vendor was a negotiated amount paid from the deposit monies held by the disputant's lawyer as stakeholder rather than payment of the deposit.

Section CG4 of the Income Tax Act 2007

At the end of the hearing on 6 August 2014, Mr Carruthers, for the disputant, made oral submissions on the possible application of s CG4 of the ITA. The TRA found that this was a new proposition of law and no explanation has been provided as to why this was not included in its statement of position, meaning it did not need to consider it.

However, the TRA considered the argument and found the disputant was not able to claim a deduction for its legal fees in reliance on s CG4 as the disputant was not in the business of civil litigation, and as such, there was no nexus.

Shortfall penalty

The TRA determined that this case involved the application of established principles and did not raise any novel points of law. In its view, the disputant's claim for deductions for the expenditure incurred in the 2011 income tax year did not have any prospect of being close to a 50% chance of success. Accordingly, the disputant failed to meet the standard of being "about as likely as not to be correct" and is liable for an unacceptable tax position shortfall penalty.

APPLICATION FOR LEAVE TO APPEAL TAXATION REVIEW AUTHORITY DECISION OUT OF TIME DISMISSED

Case	Shearing Services Kamupene Ltd v Commissioner of Inland Revenue
Decision date	15 December 2014
Act(s)	High Court Rules 2009, Tax Administration Act 1994, Taxation Review Authorities Act 1994, Te Ture Whenua Māori Act 1993
Keywords	Strike out, application for special leave to appeal out of time, PAYE, tax evasion, shortfall penalties, Māori sovereignty

Summary

The taxpayer's application for special leave to appeal the Taxation Review Authority's ("TRA's") decisions out of time was dismissed.

Impact of decision

This decision confirms the principles relevant for leave to permit an appeal to proceed out of time. The decision also confirms that new arguments not sufficiently identified in a Statement of Position ("SOP") without earlier being granted leave cannot be used to support a leave application extending the time period for an appeal.

Facts

The taxpayer applied for special leave extending the time period for the appeal of two decisions of the TRA, *Case 9* ([2012] NZTRA 9, (2012) 25 NZTC 1-012) and *Case 7* ([2013] NZTRA 7, (2013) 26 NZTC 2-006). Leave was required because the taxpayer was out of time to file an appeal. The Commissioner of Inland Revenue ("the Commissioner") opposed leave being granted.

The TRA's two decisions relate to the taxpayer's liability for PAYE for shearers and shed hands in the 2005–2007 tax years, as well as associated shortfall penalties.

The Commissioner was successful in striking out the taxpayer's notices of claim in *Case 9* subject to leave being granted for the taxpayer to apply to be heard on two discrete issues. The taxpayer failed to apply to have the matter determined within the one-month timeframe. However, the taxpayer filed a memorandum applying to be heard and to reconfirm its objection. The TRA gave the taxpayer a further opportunity to file briefs of evidence. However, the affidavits filed purported to "evidence a wide ranging and radical case well outside of the scope of the leave granted" (at [21]). In *Case 7*, the Commissioner was successful in striking out the two remaining live aspects of the claim and for summary judgment.

The taxpayer claimed that since January 2005, it has not employed the shearers and shed hands and accordingly, it is not the entity responsible for PAYE. The taxpayer claimed that Maunga Hikurangi Koporeihana (Māori Inc) was responsible instead.

Decision

Mallon J dismissed the taxpayer's application for special leave extending the time period for the appeals.

Principles relevant to leave

Her Honour relied upon the Court of Appeal case *My Noodle Ltd v Queenstown Lakes District Council* [2009] NZCA 224, (2009) 19 PRNZ 518, in her restatement of the following principles:

a) the overriding consideration in determining whether to permit an appeal to proceed out of time is the interests of justice; and

b) relevant to where the interests of justice lie are the prospective merits of the appeal, the conduct of the parties, the reason for the delay and the length of the delay, and the extent of any prejudice flowing from permitting the appeal to proceed out of time.

The merits

Mallon J outlined the procedure by which an assessment may be challenged including the requirement under s 89M(6) of the Tax Administration Act 1994 ("TAA") for a disputant to file a SOP with sufficient detail to fairly inform the Commissioner. Her Honour referred to the Court of Appeal decision of *Vinelight Nominees Ltd v Commissioner of Inland Revenue* ([2013] NZCA 655, (2013) 26 NZTC 21-055 at [31]) in support of the legal proposition that a SOP must identify any given issues "with sufficient clarity to cause a reasonable party to recognise it as such".

Her Honour also referred to s 138G of the TAA, which relevantly provides that a party may only refer to the issues disclosed in the SOPs.

Her Honour held that the new argument advanced by the taxpayer was not advanced in its SOP such that a reasonable party would be able to recognise it.

The taxpayer had submitted that Māori Inc was a valid entity under law as either a quasi-corporation or an unincorporated body (despite not being incorporated under the Te Ture Whenua Māori Act 1993 as a Māori incorporation). Mallon J considered it a "stretch" to say that an intended Māori incorporation, which had not yet been recognised by an order of the Māori Land Court, has a legal status that should be recognised for tax purposes just because in other contexts whanau and hapu have been recognised as having status for some purposes, when the tax legislation does not provide for this.

Her Honour held that a contract with Māori Inc, trading as NZCS, is a contract with those individuals, and any other individuals on whose authority the contract was entered into. The taxpayer had not established that the contracting relationships it relied on existed despite the time and opportunity to do so. In such circumstances Mallon J held that the taxpayer could not discharge its onus to show that the Commissioner's assessments were wrong.

The second issue on which leave was reserved by the TRA in *Case 9* was whether the taxpayer genuinely believed it was not obliged to pay PAYE. Despite the TRA's statement that the taxpayer could not discharge its onus, her Honour said it was clear that the TRA was not reversing the onus on a strike-out application.

Overall, Mallon J held that the merits of the proposed appeal were low and did not point in favour of granting special leave.

Conduct

Her Honour held that the taxpayer's conduct did not support granting leave. The TRA had provided many opportunities for the taxpayer to advance its claim on a proper basis.

The length of and reason for the delay

Her Honour did not consider it clear that an appeal from *Case 9* was necessary, and as the delay in responding to *Case 7* was not long and was explained, her Honour held that if other factors had favoured the granting of special leave then the delay would not have counted against the taxpayer.

Prejudice

The taxpayer drew an analogy with counsel incompetence in the criminal context arguing that there would be a miscarriage of justice if the appeal did not proceed. However, Mallon J did not consider the analogy apt and noted that there was no suggestion that the taxpayer was anything other than content for the Māori sovereignty arguments to be advanced. Nevertheless, her Honour accepted that if the wrong entity had been assessed, this factor would point in favour of granting special leave. However, there would need to be some real prospect that the appeal could succeed and in her Honour's view there was not.

Overall assessment

Mallon J considered that it was not in the interests of justice to grant special leave for the taxpayer to bring its appeal. The argument advanced by the taxpayer evolved over time and was not included in the taxpayer's SOP. The taxpayer had made the choice to advance Māori sovereignty arguments and had had more than an adequate opportunity to alter its course and to seek to advance objections to the assessments on a legally valid basis. In any event, her Honour considered the new argument advanced by the taxpayer to have low prospects of success.

NEW ZEALAND BILL OF RIGHTS APPLICATION BY TRINITY INVESTORS STRUCK OUT BY HIGH COURT

Case	Ben Nevis Forestry Ventures Ltd v Attorney-General
Decision date	10 February 2015
Act(s)	Tax Administration Act 1994, Bill of Rights Act 1990
Keywords	Presumptive bias, Trinity, tax avoidance, collateral attack

Summary

This proceeding concerned an application for orders seeking, amongst other things, to set aside the initial High Court judgment of Venning J in *Accent Management Ltd v Commissioner of Inland Revenue* (2005) 22 NZTC 19,027 (HC) ("*Accent 2004*"). The plaintiffs claimed the judgment was in breach of the Bill of Rights Act 1990 on the basis that Venning J was biased towards the Commissioner, having become beholden to her following non-payment of $4,250 of stamp duty in 1992. Asher J found the High Court did not have jurisdiction to hear the plaintiffs' claim on the basis it was an abuse of process, that the Court did not have jurisdiction and that there was no reasonably arguable case.

Impact of decision

The judgment confirms the position in *Commissioner of Inland Revenue v Redcliffe Forestry Venture Ltd* [2012] NZSC 94, [2013] 1 NZLR 804 ("*Redcliffe 2012*") and *Bradbury v Commissioner of Inland Revenue* [2014] NZSC 174, (2014) 26 NZTC 21-112 ("*Bradbury 2014*") which found a challenge to a concluded judgment that has been the subject of an appellate judgment should not be mounted in the trial court except in the case of a judgment obtained by fraud.

Facts

This proceeding is one in a line of collateral proceedings brought by investors in the Trinity scheme against the judgments of the High Court, Court of Appeal and Supreme Court that the scheme constituted tax avoidance. (The Supreme Court's decision was reported as *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* [2008] NZSC 115, [2009] 2 NZLR 289 ("*Ben Nevis 2008*").)

This particular proceeding concerned an application by Ben Nevis Forestry Ventures Ltd ("Ben Nevis"), Bristol Forestry Venture Ltd ("Bristol"), Clive Bradbury and Gregory Peebles for orders setting aside the initial High Court judgment of Venning J in *Accent 2004*. The plaintiffs claimed the judgment was in breach of the Bill of Rights Act 1990 on the basis that Venning J was biased towards the Commissioner, having become beholden to her following non-payment of $4,250 of stamp duty in 1992.

The defendants applied to strike out the proceeding on the basis it was an abuse of process, that the Court did not have jurisdiction and that there was no reasonably arguable case.

Decision

Asher J found the High Court did not have jurisdiction to hear the plaintiffs' claim.

His Honour placed the claim in the general context of the Trinity litigation. He recognised the proceeding had its genesis in that hearing and was struck out by Katz J in *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* ([2013] NZHC 2361, (2013) 26 NZTC 21-032) where the same factual allegations had been made.

Asher J noted that at the time of the hearing in this matter, Katz J's decision was under appeal, but was subsequently upheld by the Court of Appeal (*Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* [2014] NZCA 350, (2014) 26 NZTC 21,086) with the Supreme Court later declining leave to appeal in *Bradbury 2014*. In that proceeding, the Court of Appeal had determined that the appropriate forum for remedying claims relating to *Accent 2004* was the Supreme Court, relying on *Redcliffe 2012*. The effect of *Redcliffe 2012* was that a challenge to a concluded judgment that had been the subject of an appellate judgment should not be mounted in the trial court except in the case of a judgment obtained by fraud.

Asher J also referred to the Supreme Court's comments in *Bradbury 2014*, that the proceeding was a collateral attack on *Ben Nevis 2008*; that *Redcliffe 2012* was against the plaintiffs; and that, except in the special case of judgments obtained by fraud, there was no authority supporting their position.

His Honour considered he was bound by those decisions. In the absence of fraud, a challenge to *Accent 2004* could only be heard in the Supreme Court and, accordingly, there was no jurisdiction to determine an application filed in the High Court. The Court had no jurisdiction to hear the claim and so the proceeding was struck out.

ITEMS OF INTEREST

FATCA INTERGOVERNMENTAL AGREEMENT UPDATE

New Zealand has received notification from the United States Government of more favourable terms being granted to another jurisdiction. These terms are to form part of the Foreign Account Tax Compliance Act intergovernmental agreement signed between New Zealand and the United States in July 2014.

Notice pursuant to the Agreement between the Government of the United States of America and the Government of New Zealand to Improve International Tax Compliance and Implement FATCA (the Agreement)

New Zealand has, pursuant to Article 7 of the Agreement, received notification from the United States Government that it has granted more favourable terms to a Partner Jurisdiction.

Article 7 provides that more favourable terms apply automatically to the Agreement unless a decision is made to decline them. New Zealand has not declined the application of the terms.

The following paragraphs are therefore to be treated as being included in Section VI of Annex I of the Agreement beginning on 3 July 2014. With reference to paragraph G, no written notice was provided to the United States before 3 July 2014.

The Agreement is available at:

http://taxpolicy.ird.govt.nz/tax-treaties/united-states-america#IGA

G. Alternative Procedures for New Accounts Opened Prior to Entry Into Force of this Agreement.

1. Applicability.

If New Zealand has provided a written notice to the United States prior to entry into force of this Agreement that, as of July 1, 2014, New Zealand lacked the legal authority to require Reporting New Zealand Financial Institutions either: (i) to require Account Holders of New Individual Accounts to provide the self-certification specified in section III of this Annex I, or (ii) to perform all the due diligence procedures related to New Entity Accounts specified in section V of this Annex I, then Reporting New Zealand Financial Institutions may apply the alternative procedures described in subparagraph G(2) of this section, as applicable, to such New Accounts, in lieu of the procedures otherwise required under this Annex I. The alternative procedures described in subparagraph G(2) of this section shall be available only for those New Individual Accounts or New Entity Accounts, as applicable, opened prior to the earlier of: (i) the date New Zealand has the ability to compel Reporting New Zealand Financial Institutions to comply with the due diligence procedures described in section III or section V of this Annex I, as applicable, which date New Zealand shall inform the United States of in writing by the date of entry into force of this Agreement, or (ii) the date of entry into force of this Agreement. If the alternative procedures for New Entity Accounts opened on or after July 1, 2014, and before January 1, 2015, described in paragraph H of this section are applied with respect to all New Entity Accounts or a clearly identified group of such accounts, the alternative procedures described in this paragraph G may not be applied with respect to such New Entity Accounts. For all other New Accounts, Reporting New Zealand Financial Institutions must apply the due diligence procedures described in section III or section V of this Annex I, as applicable, to determine if the account is a U.S. Reportable Account or an account held by a Nonparticipating Financial Institution.

2. Alternative Procedures.

a) Within one year after the date of entry into force of this Agreement, Reporting New Zealand Financial Institutions must: (i) with respect to a New Individual Account described in subparagraph G(1) of this section, request the self-certification specified in section III of this Annex I and confirm the reasonableness of such self-certification consistent with the procedures described in section III of this Annex I, and (ii) with respect to a New Entity Account described in subparagraph G(1) of this section, perform the due diligence procedures specified in section V of this Annex I and request information as necessary to document the account, including any self-certification, required by section V of this Annex I.

b) New Zealand must report on any New Account that is identified pursuant to subparagraph G(2)(a) of this section as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable, by the date that is the later of: (i) September 30 next following the date that the account is identified as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable, or (ii) 90 days after the account is identified as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable. The information required to be reported *with respect to such a New Account is any information that would have been reportable under this Agreement if the New Account had been identified as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable, as of the date the account was opened.*

c) By the date that is one year after the date of entry into force of this Agreement, Reporting New Zealand Financial Institutions must close any New Account described in subparagraph G(1) of this section for which it was unable to collect the required self-certification or other documentation pursuant to the procedures described in subparagraph G(2)(a) of this section. In addition, by the date that is one year after the date of entry into force of this Agreement, Reporting New Zealand Financial Institutions must: (i) with respect to such closed accounts that prior to such closure were New Individual Accounts (without regard to whether such accounts were High Value Accounts), perform the due diligence procedures specified in paragraph D of section II of this Annex I, or (ii) with respect to such closed accounts that prior to such closure were New Entity Accounts, perform the due diligence procedures specified in section IV of this Annex I.

d) New Zealand must report on any closed account that is identified pursuant to subparagraph G(2)(c) of this section as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable, by the date that is the later of: (i) September 30 next following the date that the account is identified as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable, or (ii) 90 days after the account is identified as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable. The information required to be reported for such a closed account is any information that would have been reportable under this Agreement if the account had been identified as a U.S. Reportable Account or as an account held by a Nonparticipating Financial Institution, as applicable, as of the date the account was opened.

H. Alternative Procedures for New Entity Accounts Opened on or after July 1, 2014, and before January 1, 2015.

For *New Entity Accounts opened on or after July 1, 2014, and before January 1, 2015, either with respect to all New Entity Accounts or, separately, with respect to any clearly identified group of such accounts, New Zealand may permit Reporting New Zealand Financial Institutions to treat such accounts as Preexisting Entity Accounts and apply the due diligence procedures related to Preexisting Entity Accounts specified in section IV of this Annex I in lieu of the due diligence procedures specified in section V of this Annex I. In this case, the due diligence procedures of section IV of this Annex I must be applied without regard to the account balance or value threshold specified in paragraph A of section IV of this Annex I.*

REGULAR CONTRIBUTORS TO THE TIB

Office of the Chief Tax Counsel

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

Legal and Technical Services

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

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

Policy and Strategy

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

Litigation Management

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

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

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