Vol 29 No 10 November 2017

TAX INFORMATION Bulletin

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Inland Revenue
Te Tari Taake

ISSN 1177-620X (Online)

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.

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Public Consultation
Office of the Chief Tax Counsel
Inland Revenue
PO Box 2198
Wellington 6140

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IN SUMMARY

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NEW LEGISLATION

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

Compensation for Live Organ Donors Act 2016

Sections CF 1(1)(fb), MA 7(2)(bb) and RD 5(1)(b)(iiib) of the Income Tax Act 2007 and section 14 (1)(a)(ia) of the KiwiSaver Act 2006

Background

The Compensation for Live Organ Donors Act 2016 made several amendments to the Income Tax Act 2007 and the KiwiSaver Act 2006.

The Act seeks to improve New Zealand's rate of organ donation by removing the financial barrier to donation of organs by live donors. The Act also allows convalescing organ donors who were on a benefit before the donation to continue to receive that benefit during their convalescence, without having to meet any work test during their convalescence.

The Act gives eligible donors an entitlement to compensation for loss of earnings from employment while they recuperate from their donor surgery for a period of up to 12 weeks. It also provides for discretionary earnings compensation in limited circumstances relating to loss of earnings in the lead up to donor surgery. The Director-General of Health is responsible for administering the provisions of the Act.

Key features

New section CF 1(1)(fb) of the Income Tax Act 2007 includes payments of earnings compensation under the new Act as income under section CF 1(1). New section RD 5(1)(iiib) of the Income Tax Act 2007 also includes these payments as salary or wages under section RD 5(1). These amendments ensure that payments under the Act are treated the same way as income from employment, so that donors are neither financially advantaged nor disadvantaged by choosing to donate an organ.

Section MA 7(2) of the Income Tax Act 2007 was amended to treat a person who receives payments under the Compensation for Live Organ Donors Act 2016 as a full-time earner for Working for Families tax credits, if that person would have been treated as a full-time earner but for the organ donation. The effect of this provision is to ensure that a person's entitlement to Working for Families tax credits is not affected by their organ donation.

Section 14(1) of the KiwiSaver Act 2006 was amended to clarify that a person who receives payments under the Compensation for Live Organ Donors Act 2016 is not subject to the KiwiSaver automatic enrolment rules.

Application dates

This Act comes into force on the earlier of 5 December 2017 or a date appointed by Order in Council.

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 (IR715)*. You can download this publication free from our website at **www.ird.govt.nz**

Product Ruling – BR Prd 17/04

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

Name of the Person who applied for the Ruling

This Ruling has been applied for by Retirement Income Group Limited.

Taxation Laws

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

This Ruling applies in respect of ss BG 1, CA 1, CD 3 to CD 20, CW 4, CX 56B and HM 47.

The Arrangement to which this Ruling applies

1. The Arrangement is the Lifetime Income Fund (the Fund), which is a managed investment scheme in which investors (Investors) can invest their retirement savings in return for a stream of regular payments (the Lifetime Withdrawal Benefit) for the rest of their life. Investors can elect to commence receiving their Lifetime Withdrawal Benefit at any time from age 60 until age 90. The Lifetime Withdrawal Benefit is calculated as a percentage of the Investor's Protected Income Base. An Investor's Protected Income Base is the Investor's original capital sum invested in the Fund net of any applicable fees and Unplanned Withdrawals, and includes any increase in value during the Deferral Period (the period up to the time the Investor begins receiving payments of the Lifetime Withdrawal Benefit). Each Investor's Lifetime Withdrawal Benefit is paid in two phases:
   a) Protected Income Phase: This period commences on the date the Investor elects for the commencement of Lifetime Withdrawal Benefits (the Initial Regular Payment Date) and ends when all Units held by the Investor in the Fund have been redeemed. During this period, the Lifetime Withdrawal Benefit is paid out of the capital invested by an Investor in the Fund and the Investor's proportion of the Fund's post-tax earnings accumulated as a result of investing the Investor's original capital sum.
   b) Insured Income Phase: This period commences from the end of the Protected Income Phase and ends on the date of death of the Investor. During this period, the Lifetime Withdrawal Benefit is paid from the proceeds of a group life insurance policy that the Manager of the Fund is required to take out in the name of the Supervisor of the Fund for the benefit of Investors.
2. Further details of the Arrangement are set out in the paragraphs below. (Capitalised terms and phrases in the description of the Arrangement should be taken to have the meaning attributed to that term or phrase in clause 1 of the Trust Deed or in the description of the Arrangement.)

Parties to the Arrangement

3. The parties to the Arrangement are:
   a) Lifetime Income Fund;
   b) Retirement Income Group Limited;
   c) Lifetime Asset Management Limited;
   d) Lifetime Income Limited;
   e) Public Trust; and
   f) Investors in the Fund.

Lifetime Income Fund

4. The Lifetime Income Fund (the Fund) is a managed investment scheme as defined in the Financial Markets Conduct Act 2013. The Fund was established by Lifetime Asset Management Limited under the Unit Trusts Act 1960.

5. By trust deed dated 20 November 2015 (the original trust deed), Lifetime Asset Management Limited (as Manager of the Fund) and Public Trust (as Trustee of the Fund) established the terms and conditions applicable to the Fund.

6. As a consequence of the passage of the Financial Markets Conduct Act 2013 and the repeal of the Unit Trusts Act 1960, Lifetime Asset Management Limited and Public Trust have agreed to amend the original trust deed by rescinding and replacing it with the clauses contained in a trust deed dated 12 May 2016 (the May 2016 trust deed).

7. Lifetime Asset Management Limited and Public Trust subsequently agreed to amend the May 2016 trust deed with effect from 17 July 2017 by rescinding and replacing it with the clauses contained in a trust deed 17 July 2017 (the Trust Deed).

8. The Fund has notified the Commissioner under s 31B of the Tax Administration Act 1994 that it has elected to become a portfolio investment entity (PIE) under s HM 71 of the Income Tax Act 2007. The Fund uses the exit calculation option referred to in s HM 42 to calculate its income tax liability for exiting Investors and remaining Investors.

9. The Fund has two portfolios: the Balanced Portfolio and the Cash Portfolio. Each portfolio has its separate assets and liabilities governed by the terms and conditions contained in the Trust Deed. The portfolios are not separate trust funds. The investments of each portfolio must all times be Authorised Investments as set out in schedule 2 of the Trust Deed.

10. The Balanced Portfolio invests through low-cost index funds and exchange-traded funds. The investment mix of the Balanced Portfolio is balanced, investing equally in growth and income assets. The portfolio is actively hedged and in times of extreme volatility may reduce exposure to growth assets in favour of income assets. Target asset exposure is 25% domestic and 75% international.

11. The Cash Portfolio invests in an actively managed portfolio of bank bills, floating rate notes and short-term deposits and securities, with a weighted average duration not exceeding six months.

Retirement Income Group Limited

12. Retirement Income Group Limited (RIG) is incorporated in New Zealand. It is the parent company of the Retirement Income Group and owns 100% of the shares in Lifetime Asset Management Limited and Lifetime Income Limited. RIG undertakes general management for the group, including solvency and capital management.

Lifetime Asset Management Limited

13. Lifetime Asset Management Limited is incorporated in New Zealand and is a wholly owned subsidiary of RIG. Lifetime Asset Management Limited is the Manager and Issuer of the Fund for the purpose of the Financial Markets Conduct Act 2013.

Lifetime Income Limited

14. Lifetime Income Limited (LIL) is incorporated in New Zealand and is a wholly owned subsidiary of RIG. LIL is a licensed life insurer under part 2 of the Insurance (Prudential Supervision) Act 2010.

15. Under clause 6 of the Trust Deed, the Manager is required to effect with LIL, in the name of the Supervisor and for the benefit of Investors, a Policy or Policies to provide regular payment benefits in respect of Investors during their Insured Income Phase on such terms and conditions as the Manager may approve.

16. LIL has issued Master Group Policy GVA01 (with a commencement date of 10 December 2016) to Public Trust on behalf of Investors in the Fund. The Policy was entered into in New Zealand. It was replaced with Master Group Policy GVA01 with a commencement date of 31 May 2017. The replacement Policy was also entered into in New Zealand.

17. An Investor's insurance premium (for single life) is 1.35% per annum of an Investor's Protected Income Base (or 1.75% per annum for joint life). It is subject to change at any time and is calculated on a daily basis. Lifetime Asset Management Limited pays the amount monthly to LIL by redeeming Units held in respect of that Investor in the Fund's Cash Portfolio. No insurance premiums are payable during the Insured Income Phase.

Public Trust

18. Public Trust is the Supervisor of the Fund for the purpose of the Financial Markets Conduct Act 2013. Public Trust is also the trustee (the Trustee) of the Fund.

Investors

19. Investors are members of the public who invest in the Fund.

How the Arrangement operates

20. Units in a Portfolio may, subject to clause 4.2 of the Trust Deed, be issued to any Eligible Person. An Eligible Person is defined in clause 1 of the Trust Deed:

    Eligible Person means a person who:

    (a) lives or normally lives in New Zealand;

    (b) is a New Zealand citizen or is entitled to live in New Zealand indefinitely; and

    (c) is under the age of 90 years.

21. The Manager may, at its discretion, register two persons in a Relationship as the holders of any Unit in which case they are deemed to hold the Unit as joint tenants with benefit of survivorship subject to the provisions of clause 4A of the Trust Deed.
22. Investors must each invest a minimum of $25,000 in the Fund. An Investor can make additional investments of at least $1,000 at any time before they start receiving their Lifetime Withdrawal Benefit. The maximum total investment per Investor is $1,000,000.
23. Investors cannot determine the allocation of their investment between the Balanced Portfolio and the Cash Portfolio. The allocation of investments between the two portfolios is different for each Investor and is determined by the Manager based on the relevant Investor's age and when they intend to start receiving their Lifetime Withdrawal Benefit.
24. Each Investor is entitled to elect to receive a Lifetime Withdrawal Benefit. Lifetime Withdrawal Benefits commence within one month of an Investor's Initial Regular Payment Date. The Initial Regular Payment Date for an Investor shall be any date on or after the Investor's 60th birthday and before the Investor's 90th birthday.
25. Each Investor has a Protected Income Base. An Investor's Lifetime Withdrawal Benefit is calculated as a percentage of their Protected Income Base. Initially, an Investor's Protected Income Base is their total investment in the Fund. On each anniversary of their initial investment, the total value of the Investor's investment in the Fund (their Fund Balance) is compared with the Investor's Protected Income Base. If their Fund Balance exceeds their Protected Income Base, the Investor's Protected Income Base is increased to their current Fund Balance. This means that an Investor's Protected Income Base may rise if positive investment returns or additional contributions increase the value of their investment in the Fund. However, an Investor's Protected Income Base will not fall unless the Investor makes an Unplanned Withdrawal.
26. The age at which an Investor starts receiving their Lifetime Withdrawal Benefit determines the rate of payment for the Lifetime Withdrawal Benefit. The payment rate for an Investor that chooses to start receiving their Lifetime Withdrawal Benefit at age 60 is 4.5% per annum of their Protected Income Base. For each one year increase in the age at which an Investor first starts receiving their Lifetime Withdrawal Benefit, the payment rate increases by 0.1% per annum. (For example, the payment rate for an Investor that starts receiving their Lifetime Withdrawal Benefit at age 70 is 5.5%, at age 80 is 6.5% and at age 90 is 7.5% per annum.)
27. For two persons in a Relationship that are registered as joint holders of the relevant Units, the Lifetime Withdrawal Benefit payment rate for the couple will be based on the age of the younger Investor of the couple.
28. Investors may choose whether Lifetime Withdrawal Benefits are paid to them fortnightly or monthly. Lifetime Withdrawal Benefits may be:

    a) benefits paid during the Protected Income Phase; or

    b) benefits paid during the Insured Income Phase.

Protected Income Phase

29. The Protected Income Phase with respect to an Investor means the period commencing from the Initial Regular Payment Date elected by the Investor under clause 7.7 of the Trust Deed and ending when all Units held by the Investor in the Fund have been redeemed. During this phase Lifetime Withdrawal Benefits are paid from the redemption of Units held by the Investor in the Fund.

Insured Income Phase

30. The Insured Income Phase with respect to an Investor means the period commencing from the end of the Protected Income Phase and ending on the date of death of the Investor.
31. In the policy year that the account value for an Investor is reduced to zero, LIL will make a lump sum payment to Public Trust in respect of the Investor equal to the balance of the Lifetime Withdrawal Benefit still payable to that Investor for that year. Beginning on the next policy anniversary date, LIL will make an annual lump sum payment to Public Trust in respect of all Investors in their Insured Income Phase. This will continue to be paid for each Investor in their Insured Income Phase until the death of that Investor.

32. Under clause 7.13 of the Trust Deed, any money received by the Fund in respect of an Investor (or Investors) under the Policy shall be treated as a subscription on behalf of that Investor (or those Investors) for Units in the Cash Portfolio.

33. Provided payments are received under the Policy in respect of an Investor, all payments to an Investor during the Insured Income Phase will be made by redeeming Units in the Cash Portfolio in accordance with clause 7.10 of the Trust Deed to the Investor until the date of death of the Investor.

Fees

34. Investors are charged the following regular fees for investing in the Fund:
    a) a management fee of 0.70% per annum of the aggregate net asset value of the Fund (across both portfolios) and administration fees;
    b) a supervisor fee of 0.08% per annum of the aggregate net asset value of the Fund (across both portfolios and subject to a $25,000 per annum minimum); and
    c) an administration management fee of 0.17% per annum of the aggregate net asset value of the Fund (across both portfolios and subject to a $35,000 per annum minimum).

35. Investors are also charged the following individual action fees:
    a) Buy/sell spread. When an investor invests in the Fund or makes a withdrawal from the Fund, they are charged a buy/sell spread. This is based on the amount of the investment or withdrawal from the Balanced Portfolio. The buy/sell spread is paid to the Fund and is designed to ensure, to the extent possible, that the costs of buying or selling assets in the Balanced Portfolio incurred as a result of that investment or withdrawal are borne by the relevant Investor and not by other Investors. The buy/sell spread is determined on each application or withdrawal based on the actual costs of buying or selling assets in the Balanced Portfolio. The indicative buy spread is 0.125% of investment allocated to the Balanced Portfolio. The indicative sell spread is 0.125% of the withdrawal allocated to the Balanced Portfolio. There is no buy spread in the Cash Portfolio.
    b) Early withdrawal fee of 1.00% of the total amount invested (that is, the initial and any additional investments) if an Investor makes a full withdrawal within three years of their initial investment. The early withdrawal fee applies in addition to the sell spread.

Internal switching

36. Payment of all Lifetime Withdrawal Benefits to Investors and payment of fees and insurance premiums payable for or in respect of an Investor shall be paid by redemption of units held in respect of that Investor in the Cash Portfolio.

37. The Manager is required to ensure that at all times sufficient Units are held on behalf of an Investor in the Cash Portfolio to meet all payments that are to be made in regard to that Investor under the terms of the Trust Deed, including:
    a) payment of fees;
    b) payment of insurance premiums; and
    c) payment of all benefit payments due to the Investor.

38. The Manager is authorised at any time with respect to an Investor to redeem Units held by that Investor in the Balanced Portfolio and acquire Units for the Investor in the Cash Portfolio for the purpose of payment of fees, insurance premiums and benefit payments due to an Investor. The redemption of Units in the Balanced Portfolio to increase the Cash Portfolio to cover these commitments is usually done on an annual basis.

Unplanned Withdrawals

39. Under clause 7 of the Trust Deed, Investors can make an Unplanned Withdrawal at any time by making an Unplanned Withdrawal Request to redeem the Investor's Units in the Fund.

40. If an Investor makes one or more Unplanned Withdrawal Request(s) that, in total, amount to no more than 20% of the application money paid by the Investor, the Manager must arrange for the redemption of the number or value of Units held by the Investor referred to in the Unplanned Withdrawal Request.

41. If an Investor makes one or more Unplanned Withdrawal Requests with respect to more than 20% of the application moneys paid by the Investor, the Manager must give one month's notice to the Investor of its intention to cause all Units held by the Investor to be redeemed in accordance with clause 7.4.3 of the Trust Deed. The Investor may withdraw their Unplanned Withdrawal Request during this one- month notice period.

Death of an Investor

42. When an Investor dies, if the Investor still holds Units, the Manager shall cause the Supervisor to redeem all Units and shall make payment of the amount payable following redemption of such Units to the personal representative of the Investor's estate. Where an Investor does not hold Units at the time of the Investor's death, the Manager and the Supervisor shall not be obliged to make any payment to the personal representative of the Investor's estate.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

a) The continued application of Private Ruling BR Prv 17/35 issued on 18 August 2017 (including any ruling issued to replace that private ruling, provided the change to the ruling does not affect the application of this product ruling).

b) LIL does not have full reinsurance.

How the Taxation Laws apply to the Arrangement

Subject in all respects to any condition stated above, the Taxation Laws apply to the Arrangement as follows:

a) The Fund will calculate and pay its income tax liability in accordance with s HM 47 on the amount of attributed PIE income or attributed PIE loss for each Investor at the relevant prescribed investor rates that the Investors notify to the Fund.

b) The Lifetime Withdrawal Benefit payments from the Fund to Investors will be excluded income in the hands of Investors under s CX 56B.

c) Any benefit to the Investor from the Fund arranging and meeting the costs of life insurance cover provided by LIL is not a dividend in the hands of the Investor under ss CD 3 to CD 20 or s CA 1.

d) Payment of the Lifetime Withdrawal Benefit by LIL to Investors during the Insured Income Phase is exempt income in the hands of Investors under s CW 4.

e) Section BG 1 does not apply to the Arrangement.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 April 2017 and ending on 31 March 2022.

This Ruling is signed by me on the 18th day of August 2017.

Howard Davis
Director (Taxpayer Rulings)

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 17/08: Are proceeds from the sale of gold bullion income?

This QWBA is about whether disposals of gold bullion will give rise to income under s CB 4. Amounts derived on the disposal of personal property are income under s CB 4 if the property was acquired for the dominant purpose of disposal.

While this QWBA discusses s CB 4 in the context of gold bullion, the same principles are relevant to the disposal of other personal property. Some of the issues discussed are particularly relevant to the disposal of non-income producing assets.

Question

Are amounts derived on the sale of gold bullion income for tax purposes?

Answer

As with any personal property, amounts derived on the disposal of gold will be income under s CB 4 if the gold was acquired for the dominant purpose of disposal.

Key provision

Section CB 4 of the Income Tax Act 2007

Key terms in this item

In the context of this QWBA, gold bullion refers to physical gold bars, coins, or certificates (allocated or unallocated), or direct units in gold (ie, units that give rise to ownership of a certain amount of gold, measured in physical units).

Gold may also be invested indirectly, for example through investment in a fund that owns commodities or benchmarks its return to commodities, or through other derivatives such as forwards, futures or options.

Investments in gold in those or other forms not covered by this QWBA may still give rise to tax implications under s CB 4 or under other tax rules (for example under the financial arrangements rules).

Explanation

1. While the test in s CB 4 is subjective, any assertion that property was not acquired for the dominant purpose of disposal needs to be assessed against the totality of the circumstances. These include the nature of the asset, the person's vocation, the circumstances of the purchase, the number of similar transactions, the length of time the property was held, and the circumstances of the use and disposal of the asset.
2. The nature of the asset is always an important consideration. In the case of gold bullion, the Commissioner considers that this is particularly so, as bullion does not provide annual returns or income while it is held, nor does it confer other benefits (which other investments that do not provide income while held might). The Commissioner therefore considers that, for gold bullion, the nature of the asset is a factor that strongly indicates that it was acquired for the dominant purpose of ultimately disposing of it.
3. In most cases, gold purchased in bullion form will be purchased for the dominant purpose of disposal. However, there may sometimes be situations where the Commissioner may accept that the dominant purpose in acquiring gold bullion was to retain it for reasons other than eventual disposal. For example, there may be circumstances where bullion is acquired for the dominant purpose of building up a diversified portfolio of property that the person will not necessarily realise, or as a long-term investment that the person will not necessarily realise. In such circumstances it may be that the taxpayer can show that the bullion was not purchased with the dominant purpose of disposal.
4. Ascertaining what a person's subjective purpose was at the time they acquired property is a very fact-specific assessment. The particular circumstances of the situation need to be carefully considered, and any assertion that gold was not acquired for the dominant purpose of disposal would need to be supported by clear and compelling evidence.
5. It is also important to bear in mind that merely describing property, or the reason for which it was acquired, in a particular way will not answer the question of whether there was a dominant purpose of disposal. For example, describing property as being acquired as a long-term investment, a hedge against inflation, for portfolio diversification, or as a store of value outside the monetary system is not sufficient to negate a dominant purpose of disposal. The person's underlying motive

should not be confused with their purpose. The key question is whether the person's objective in acquiring the gold is to be achieved through a course of action that will involve disposal at some point, such that, as a matter of fact, the person's dominant purpose is one of disposal. If a taxpayer asserts that they did not acquire gold bullion for the dominant purpose of disposal, the onus is on them to satisfactorily show that.

6. When gold that was acquired for the purpose of disposal is sold, a deduction for the cost of the property is allowed, subject to the normal rules. Just as an increase in value will mean that any profits will be taxed, if gold has decreased in value and is sold for less than it cost, this will result in a deductible loss. Other expenditure may also be deductible, such as interest on money borrowed to purchase the gold, insurance premiums, and storage costs.

What is the relevant taxing provision?

7. Section CB 4 provides that:

> **CB 4 Personal property acquired for purpose of disposal**
>
> An amount that a person derives from disposing of personal property is income of the person if they acquired the property for the purpose of disposing of it.

8. Amounts derived on the disposal of gold will therefore be income under s CB 4 if the gold was acquired for the purpose of disposal.

What types of disposals fall within the scope of s CB 4?

No requirement for purpose of disposal at a profit

9. Before the provision taxing the disposal of personal property acquired for the purpose of disposal was introduced, there was a provision in the tax legislation that taxed disposals of land acquired for the purpose of selling or otherwise disposing of it at a profit. When that provision was expanded to include personal property, one of the changes made was that the property only needed to be acquired for the purpose of sale or disposition (rather than sale or disposition *at a profit*). It is therefore clear that for s CB 4 to apply the purpose in acquiring the property does not need to be sale or disposal *at a profit*.

Purpose of disposal by way of sale or similar

10. However, the Commissioner considers that s CB 4 is limited to situations where there was a purpose of disposal by way of *sale or similar* (eg, by way of barter). While the legislation simply refers to property acquired for the purpose of disposal, prior to the Act being re-written for simplicity and improved clarity (which was done progressively from 1994) the provision stated that it applied to disposals of personal property that was "acquired for the purpose of selling or otherwise disposing of it". The Commissioner considers that in the pre-rewrite wording, "selling" coloured the words "or otherwise disposing of it", indicating that the provision would apply where the purpose in acquiring the property was disposal by way of *sale or similar*. To read the provision more broadly would mean that any personal property acquired to be gifted would be within the tax base, which was clearly not intended and would be absurd. There was no intention to broaden the scope of s CB 4 when the Act was re-written – the provision was intended to continue to have the same effect.[1] As such, the wording of the provision before the Act was re-written must be used to determine the correct meaning of s CB 4.[2] The Commissioner therefore considers that the correct interpretation of s CB 4 is that it will apply to disposals of personal property acquired for the purpose of disposal by way of *sale or similar*.

11. This means that s CB 4 would not apply to disposals of property acquired for the purpose of disposal by way of gift, for example. But it should be noted that if property was acquired for the purpose of disposal by sale or similar and is then gifted, such a disposal would give rise to income under s CB 4. It is the person's purpose at the time they acquire the property that is relevant, not how they ultimately dispose of the property. And subpart FC of the Act ensures that tax-base property cannot be gifted outside of the tax base.

12. Similarly, s CB 4 would not apply to disposals of property acquired for the purpose of being passed to heirs on death. But if property was acquired for the purpose of disposal by sale or similar and ends up being transferred on death, there may be tax consequences arising from that transfer or from a subsequent disposal.[3]

[1] Section YA 3(3) of the Income Tax Act 2004 and schedule 22A (Identified policy changes) to that Act, and s ZA 3(3) of the Income Tax Act 2007 and schedule 51 (Identified changes in legislation) to that Act.

[2] Section YA 3(4) of the Income Tax Act 2004 and s ZA 3(4) of the Income Tax Act 2007.

[3] The specific rules in the Act dealing with property that is transferred on a person's death, or on a distribution by an executor, administrator or trustee of a deceased's estate to a beneficiary are in subpart FC of the Act.

Section CB 4 – main principles

13. The leading case on s CB 4 is *CIR v National Distributors Ltd* (1989) 11 NZTC 6,346 (CA). This was a case about whether various parcels of shares were acquired for the purpose of selling or otherwise disposing of them, so that the proceeds on the sales would be taxable under what is now s CB 4. In discussing the provision, Richardson J noted that:

> Section 65(2) [now s CB 4] is expressed as a deeming provision. The assessable income of the taxpayer is deemed to include profits derived from transactions coming within the respective limb of para (e). The second limb has been in the legislation since 1916. **It brings within the tax net particular transactions which might otherwise escape liability. It does not perpetuate the theoretical distinction between capital and income. It is not to be read down by any preconceptions as to the nature of a tax on income or by importing a requirement that the acquisitions to which it refers should have a business overlay.** The words used must be given their natural and ordinary meaning (see *Lowe v Commissioner of Inland Revenue* [1981] 1 NZLR 326, 342).
>
> [Emphasis added]

14. The main principles on the application of s CB 4 that can be drawn from *National Distributors* are as follows:
    - There is no business overlay to s CB 4; the distinction between capital and revenue is not relevant.
    - All that is required is that the property be acquired **for the dominant purpose of disposal**.
    - The onus is on the taxpayer to show that they did not acquire the property with the dominant purpose of disposal.
    - The test of purpose is subjective, but the taxpayer's assertions as to their purpose need to be assessed against the totality of the circumstances. These will include the nature of the asset, the vocation of the taxpayer, the circumstances of the purchase, the number of similar transactions, the length of time the property was held, and the circumstances of the use and disposal of the asset.
    - **It is important to bear in mind the distinction between motive and purpose; the reason why the taxpayer decided to acquire property with a view to disposal in due course is not relevant** to the statutory inquiry. If the taxpayer's dominant purpose in acquiring the property is to dispose of it in the future, the provision will apply.
    - If at the time the property was acquired the taxpayer did not expect to hold the property forever and contemplated the possibility of sale, this alone would not bring the sale within s CB 4. The property must have been acquired for the dominant purpose of disposal.
    - If the property was acquired for a number of purposes, disposal must be the predominant one for s CB 4 to apply.
    - If the taxpayer can establish that they had no clear purpose in mind when acquiring an asset, s CB 4 will not apply.

Will amounts derived on the disposal of gold bullion be income?

15. While the test of purpose for s CB 4 is subjective, as noted above, any assertion that property was not acquired for the purpose of disposal needs to be assessed against the totality of the circumstances.

16. As noted by Richardson J in *National Distributors*, the nature of the asset is always an important consideration. Assets acquired for private use and enjoyment clearly fall outside the scope of s CB 4. In other situations there may be an element of private use and enjoyment as well as economic reward, and it will be necessary to determine what the dominant purpose on acquisition was. But in some situations it will be clear that the asset is not intended for private use and enjoyment. In that case, it might generally be expected that the asset was acquired for the purpose of deriving income from it while it is held, or with the aim of realising a profit on its disposal sooner or later.

17. In the case of gold bullion, the Commissioner considers that the nature of the asset is a significant consideration in deciding if it was acquired for the dominant purpose of disposal, as bullion does not provide annual returns or income while it is held. Other investments may similarly not provide income while held, for example shares that do not pay dividends, but may confer other benefits such as voting rights. The Commissioner therefore considers that, for gold bullion, the nature of the asset is a factor that strongly indicates that it was acquired for the purpose of ultimately disposing of it.

18. In most cases, gold purchased in bullion form will be purchased for the dominant purpose of disposal. However, there may sometimes be situations where the Commissioner may accept that the dominant purpose in acquiring gold bullion was to retain it for reasons other than eventual disposal. For example, there may be circumstances where bullion is acquired for the dominant purpose of building up a diversified portfolio of property that the person will not necessarily realise, or as a long-term investment that the person will not necessarily realise. In such circumstances it may be that the taxpayer can show that the bullion was not purchased with the dominant purpose of disposal.

19. This will always be a very fact-specific call, and would require consideration of what the person had in mind at the time they acquired the property. Relevant factors to consider in testing this might be things such as the person's means at the time they acquired the property, whether at that time they expect to or are likely to need to realise their investments in the future, and the circumstances surrounding the disposal. Other factors such as the number of similar transactions and the length of time the property was held would also be relevant in testing the veracity of the taxpayer's assertion. Any assertion that gold was not acquired for the dominant purpose of disposal would need to be supported by clear and compelling evidence.

20. It is important to bear in mind that merely describing property or the reason for which it was acquired in a particular way will not answer the question of whether there was a dominant purpose of disposal. For example, describing property as being acquired as a long-term investment, a hedge against inflation, for portfolio diversification, or as a store of value outside the monetary system is not sufficient to negate a dominant purpose of disposal. The person's underlying motive should not be confused with their purpose. The key question is whether the person's objective in acquiring the gold is to be achieved through a course of action that will involve disposal at some point, such that, as a matter of fact, the person's dominant purpose is one of disposal. If a taxpayer asserts that they did not acquire gold bullion for the dominant purpose of disposal, the onus is on them to satisfactorily show that.

21. The table on the following two pages summarises a number of overseas cases that have considered the taxability of gold and silver bullion. While the provisions considered in those cases are not identical to s CB 4, in most cases the tax outcomes would be the same in New Zealand, and they are useful fact scenarios to consider. The table also sets out the Commissioner's view of whether s CB 4 would apply on the same facts, and, if the result would be different in New Zealand, explains why. There are other overseas cases considering the taxability of non-income producing commodities, but the cases set out in the table below[4] are considered the most relevant as they deal with gold or silver bullion.

Case: *Wisdom v Chamberlain* (Court of Appeal (England))

Summary of facts

The taxpayer had invested in silver as a hedge against expected devaluation of the British pound. When the pound recovered, and the risk of devaluation was gone, the taxpayer sold the silver bars at a profit.

Decision

The sales of the silver were an adventure or concern in the nature of trade.

Reasons for decision

The fact that the silver was acquired as a hedge against devaluation did not detract from the transactions being in the nature of trade. Although the investment was a hedge, the transactions were nonetheless entered into on a short-term basis for the purpose of making a profit.

CIR's view of whether s CB 4 would apply

The amount derived on the sale would similarly be income under s CB 4.

This is because while the taxpayer's motivation in acquiring the silver was to protect against expected devaluation of the pound, that aim was to be achieved either by re-sale at a profit if devaluation occurred, or by re-sale if the danger of devaluation passed.

Case: *Southco Holdings v MNR* (Tax Review Board (Canada))

Summary of facts

The taxpayer acquired large quantities of gold bullion over a seven-year period. The representative of the taxpayer company explained that the company was forced to sell the gold to help its parent company pay a substantial tax bill.

Decision

The profits arising from the sales were income from an adventure in the nature of trade, and so income.

[4] *Wisdom v Chamberlain (Inspector of Taxes)* [1969] 1 All ER 332 (CA), *Southco Holdings and Management Ltd et al v MNR* 75 DTC 162 (Tax Review Board), *Case P27* 82 ATC 117 (Board of Review), *Case Q109* 83 ATC 560 (Board of Review), *Victor Harms v MNR* 84 DTC 1666 (TCC), and *Case U145* 87 ATC 844 (AAT).

Reasons for decision

The taxpayers were not in the business of processing gold to make a profit. The gold was therefore only of value to them in that it could be exchanged for money, and it was inconceivable that the taxpayer would buy such a commodity in such a quantity without the intention of reselling it at a profit. The explanation for the sale was not convincing enough to prove that there was a unique reason for the sale which might have supported a conclusion that the transactions were not an adventure in the nature of trade.

CIR's view of whether s CB 4 would apply

The amount derived on the sale would similarly be income under s CB 4.

This is because it was clear (and admitted by the taxpayer) that the gold, which was acquired for peace of mind and as security against inflation, was of no benefit unless it was sold. In the most profitable transactions, the gold was sold after about 15 months, and the reasons given for the sales did not suggest there had been some purpose other than eventual sale at a profit.

Case: *Case P27* (Board of Review (Australia))

Summary of facts

The taxpayer received an early discharge from the army after suffering an injury, and then worked as a public servant. He invested his payout from the army in gold and silver bullion as he wanted to preserve its purchasing power, so that it would more closely approximate what he would have received had he stayed in the army until age 55. It was accepted by the taxpayer in his evidence that to achieve this purpose the bullion had to be sold eventually in whole or in part. The taxpayer ended up selling the gold some two and a half years later to purchase a rural property. His instructions for the sale were given within two hours of hearing a radio message concerning the price of bullion on that day.

Decision

The profits were taxable as the taxpayer acquired the bullion with the dominant purpose of selling it at a profit.

Reasons for decision

While the taxpayer's motive in acquiring bullion was as a hedge against inflation, his dominant purpose was to sell it at a profit when he reached age 55.

CIR's view of whether s CB 4 would apply

The amount derived on the sale would similarly be income under s CB 4.

This is because while the taxpayer's motivation was to secure the value of his payout from the army, his purpose was always to sell the gold and silver.

Case: *Case Q109* (Board of Review (Australia))

Summary of facts

The taxpayers were Asian immigrants to Australia. Against the backdrop of the husband's ill health, they purchased the silver bullion to protect their capital, and to provide for their children's financial futures. This was in keeping with their cultural custom. It was considered that silver or gold would best withstand fluctuations in value over an indefinite period. The price of silver rose unpredictably and substantially. At that time, the taxpayers decided to take advantage of the extraordinary rise in the value of silver and sell some.

Decision

The profits on the sale of the bullion were not income under ordinary concepts, and were not derived from the carrying on or carrying out of a profit-making undertaking or scheme. The bullion was not acquired for the purpose of profit-making by sale.

Reasons for decision

The evidence indicated that the taxpayers' financial position was sound at the time the bullion was acquired, and neither of them could foresee a future situation where it might be necessary for them to sell all or some of the bullion for their personal benefit. Further, at the time of acquisition, it was probably not feasible for anyone to have confidently (if at all) predicted the remarkable rise in the value of silver, particularly over a short period of time.

CIR's view of whether s CB 4 would apply

The amount derived on the sale would similarly be income under s CB 4.

This is because s CB 4 is limited to situations where there was a purpose of sale or some other similar disposal. In this case, the taxpayers acquired the gold to gift to their children at maturity, in accordance with their cultural custom.

Case: *Victor Harms v MNR* (Tax Court of Canada)

Summary of facts

The taxpayer had purchased gold bars and coins with the aim of preserving his capital in the event of what he considered the imminent collapse of the economy, and emergence of a barter system. In the event that this happened, the taxpayer considered that gold would maintain its purchasing power. The taxpayer ended up selling the gold bars and coins when there were indications of economic deflation.

Decision

The profits were not considered to be from an adventure in the nature of trade. The gains the taxpayer made on the sales were held to be capital, not income.

Reasons for decision

There was nothing to indicate that the taxpayer had acquired the gold with the intention of selling it. There was nothing to suggest that the transactions were entered into on a short-term basis or that the taxpayer intended to sell the gold at an opportune time. The court was satisfied that the taxpayer was convinced the economy was going to collapse and that gold would serve as the basis of any barter system that would emerge.

CIR's view of whether s CB 4 would apply

The amount derived on the disposal would be taxed under s CB 4. What is required is a dominant purpose of disposal – which the CIR considers means by way of sale or similar. In this case, the taxpayer acquired the gold for the purpose of disposing of it either by way of barter in the event of economic collapse, or by selling it if a particular scenario eventuated. Either of those alternatives amount to a purpose of disposal by way of sale or similar, so s CB 4 would apply.

Case: *Case U145* (AAT (Australia)

Summary of facts

The taxpayer was a 63 year old bookmaker, with a portfolio of long-term investments including some gold bullion. He bought the bullion to extend and diversify his portfolio, and hoped it would be a good long-term investment. The AAT accepted that he did not acquire the gold intending to sell it, but merely for it to be part of his portfolio which could be used if the taxpayer became unable to work. The taxpayer wanted to work for as long as he could, and gave evidence of a bookmaker who was still working at age 89. The taxpayer ended up selling the gold due to a business liquidity issue, and a large tax liability. He also sold shares, most of them at a loss.

Decision

The taxpayer did not acquire the gold with the predominant purpose of profit-making by sale, so the proceeds were not taxable.

Reasons for decision

At the time the taxpayer acquired the gold, its sale was a possibility that depended on a number of contingencies which were contrary to the taxpayer's expectations (ie, the need to retire). It was also noted that even if such contingencies arose and the sale of part of the taxpayer's portfolio was required, this would not necessarily have included the gold.

The AAT considered that it was apparent that the weakest of the taxpayer's shareholdings (together with the remaining gold) were sold to fund the tax liability.

CIR's view of whether s CB 4 would apply

The amount derived on the sale would not be income under s CB 4. The taxpayer's particular circumstances show that the dominant purpose on the acquisition of the bullion was not disposal.

22. As can be seen, ascertaining what a person's subjective purpose was at the time they acquired property is a very fact-specific assessment. The particular circumstances of the situation need to be carefully considered, and as noted above, the person's motives need to be distinguished from their purposes in acquiring the property.

What if a person has no purpose in acquiring gold bullion?

23. As noted at [14], if someone can establish that they had no clear purpose in mind when acquiring an asset, s CB 4 will not apply (*National Distributors*). The Commissioner considers it unlikely that someone could satisfactorily show that they purchased gold bullion with no clear purpose in mind.

What if gold bullion is purchased as part of a business?

24. Section CB 4 would not be relevant where a taxpayer sells or exchanges gold bullion in the ordinary course of their business, or has the bullion for use in producing stock for sale or exchange (for example, a jeweller who converts gold bullion into other forms for sale). In those situations, the commodity would be the taxpayer's "trading stock" (s EB 2). Business income is taxed under s CB 1, and the timing of deductions for the value of trading stock is determined under the trading stock rules (see in particular s DB 49(2)).

What deductions can be claimed?

25. Property that, if disposed of for valuable consideration, would produce income for a person is generally[5] "revenue account property" (as defined in s YA 1). Personal property that is acquired for the purpose of disposal is therefore revenue account property.

26. Section DB 23 allows a deduction for the cost of revenue account property. This is subject to the "general permission" (s DA 1) being satisfied. The general permission requires a nexus between the expenditure and the derivation of assessable and/or excluded income, or for the expenditure to have been incurred in the course of the person carrying on a business for the purpose of deriving assessable and/or excluded income.

27. Where gold bullion was acquired for the dominant purpose of disposal it will be revenue account property, and the cost of the gold will be deductible under s DB 23. The deduction is allocated to the earlier of the income year in which the property is disposed of or ceases to exist (s EA 2). Just as an increase in value will mean that the profits are taxed, if the gold has decreased in value, and is sold for less than it cost, that would result in a deductible loss.

28. Where gold bullion is acquired for the purpose of being disposed of, the taxpayer would also be able to deduct expenditure (subject to the normal rules) such as interest on money borrowed to purchase the gold, insurance premiums, storage costs, etc, (ss DA 1, DB 6 and DB 7).

29. As noted above, where gold bullion is a taxpayer's trading stock, the timing of deductions for the value of the trading stock is determined under the trading stock rules (see in particular s DB 49(2)).

[5] The exceptions to this are not relevant for present purposes.

Example

The following example is included to assist in explaining how the law applies.

In addition to this example, the table on pages 6 and 7 above sets out the Commissioner's view of whether s CB 4 would apply on the same facts as in the cases set out in the table, and includes examples of situations where s CB 4 would not apply.

30. Between late 2007 and early 2008, Zoë, who lives in New Zealand, purchased gold and silver units issued by an Australian mint. The units gave rise to ownership of a total of 57.986 ounces of gold (purchased for a total of NZD59,585.25) and 879.098 ounces of silver (purchased for a total of NZD18,606.99). Zoë was concerned about volatility in the share market, the economic uncertainty at the time, and the safety of the banking system. She considered that gold and silver provided a stable and low-risk investment option. Zoë did not have any particular timeframe in mind for holding the gold and silver units, as it depended in part on what happened with the equities and commodities markets, but ultimately she hoped to make a profit and so increase her retirement fund.
31. Zoë sold the gold units in mid-2016 to help fund the purchase of a larger residential property. Those units were sold for NZD100,354.05. Zoë sold the silver units later in 2016 to fund her wedding. Those units were sold for NZD20,632.43.
32. Amounts derived on the disposal of personal property are income under s CB 4 if the property was acquired for the dominant purpose of disposal. The Commissioner considers that the amounts Zoë derived on the sales of the gold and silver units are income under s CB 4, because those units were acquired for the dominant purpose of ultimately being disposed of. The units did not provide annual returns or income while being held, and Zoë acquired them with the aim of realising a profit on their disposal sooner or later. There is nothing to suggest that Zoë did not anticipate selling the units at some point. Zoë's aim in acquiring the units was to make a profit on their disposal. In the circumstances, the fact that Zoë had concerns about the share market and considered the units to be a stable investment does not suggest that they were not acquired for the purpose of ultimately being disposed of. The events that prompted Zoë to sell the units are not relevant to the application of s CB 4.
33. Under s CB 4, the amounts derived on the sales of the gold units (NZD100,354.05) and silver units (NZD20,632.43) are therefore income to Zoë in the 2016-2017 income year. Because the gold and silver units are revenue account property, and there is the necessary nexus between the expenditure incurred in purchasing the units and the derivation of income, Zoë is able to deduct the cost of that property under s DB 23. Zoë can therefore deduct NZD59,585.25 (the cost of the gold units) and NZD18,606.99 (the cost of the silver units) in the 2016-2017 income year. She can also deduct other expenditure incurred in deriving the income, for example forex charges or bank transaction fees.

References

Subject references

Income tax, revenue account property, property acquired for the purpose of disposal, gold

Legislative references

Income Tax Act 2007 – ss CB 1, CB 4, DA 1, DB 6, DB 7, DB 23, DB 49(2), EA 2, EB 2, ZA 3(3) and ZA 3(4), subpart FC, the definition of "revenue account property" in s YA 1, and schedule 51 (Identified changes in legislation)

Income Tax Act 2004 – ss YA 3(3) and YA 3(4), and schedule 22A (Identified policy changes)

Case references

Case P27 82 ATC 117 (Board of Review)

Case Q109 83 ATC 560 (Board of Review)

Case U145 87 ATC 844 (AAT)

CIR v National Distributors Ltd (1989) 11 NZTC 6,346 (CA)

Southco Holdings and Management Ltd et al v MNR 75 DTC 162 (Tax Review Board)

Victor Harms v MNR 84 DTC 1666 (TCC)

Wisdom v Chamberlain (Inspector of Taxes) [1969] 1 All ER 332 (CA)

INTERPRETATION STATEMENTS

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

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

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

IS 17/08: Goods and services tax – compulsory zero-rating of land rules (general application)

All legislative references are to the Goods and Services Tax Act 1985 unless otherwise stated. Relevant legislative provisions are reproduced in Appendix 2 to this Interpretation Statement.

Summary

1. The compulsory zero-rating of land (CZR) rules treat certain supplies involving land between registered persons as zero-rated supplies. The CZR rules were introduced to assist in combating so-called phoenix schemes and to help streamline GST cash flows. Most transactions between registered persons involving supplies of land or interests in land are captured by the CZR rules. Cash flows from residential tenancies and commercial leases are generally excluded, although some transactions involving assignments or surrenders of leases may be covered by the CZR rules.

2. Under the CZR rules, a vendor who is a registered person must charge GST at the rate of 0% when:
   - making a supply wholly or partly consisting of land to a purchaser who is a registered person;
   - the supply is made in the course or furtherance of the vendor's taxable activity;
   - the purchaser intends using the goods (including the land) for the purpose of making taxable supplies; and
   - the purchaser (or a relative of the purchaser) does not intend using the land (or any part of it) as their principal place of residence.

3. When a supply wholly or partly consists of land, the purchaser must notify the vendor of certain information at or before settlement. The vendor uses this information to determine the correct GST treatment of the supply. Special rules exist for resolving situations where a supply involving land is incorrectly zero-rated or standard-rated.

4. When a supply between two registered persons is zero-rated, the vendor does not pay output tax for the supply, and the purchaser cannot claim an input tax deduction for the purchase.

Introduction

5. The CZR rules came into effect on 1 April 2011. The intention of these rules is to improve the efficiency of the GST system and remove the risk to the tax base from phoenix schemes. Phoenix schemes typically involve land being sold between associated entities. The purchaser receives a refund of GST, but the vendor deliberately winds up their entity before paying the GST output tax.

6. This interpretation statement addresses the operation of the CZR rules. The examples (from [84]) at the end of the statement illustrate how the CZR rules apply in common situations. The examples along with the flowchart in Appendix 1 are to help taxpayers understand their GST obligations when their supplies involve land.

7. In this interpretation statement, the supplier is usually referred to as the "vendor" and the recipient of the supply is usually referred to as the "purchaser", even though in practice, the recipient of the supply may be the purchaser's nominee. A vendor who is a registered person is usually referred to as a "GST-registered vendor" and, similarly, a purchaser (or their nominee) who is a registered person is referred to as a "GST-registered purchaser". The CZR rules as they relate to nominees are discussed at [24] and [57].

Analysis

What are the CZR rules?

8. Put very simply, the CZR rules require a supply between two registered persons that wholly or partly consists of land to be zero-rated, if at the time of settlement certain requirements are met.

9. When the CZR rules apply, a vendor must include the zero-rated supply in their GST return, but they do not return any output tax for the supply. In turn, the GST-registered purchaser does not claim an input tax deduction for the purchase.

> For example, a GST-registered vendor agrees to sell some land with a warehouse on it to a GST-registered purchaser. Before settlement, the purchaser informs the vendor in writing that they intend using the land and warehouse as their business premises. The notice also confirms the purchaser has no intention of living on the land or in the warehouse. Applying the CZR rules, the supply of the land and warehouse must be zero-rated, so the vendor must charge GST on the supply at 0% and include it as a zero-rated supply in their GST return. This means the vendor will not pay any output tax for the supply, and the purchaser cannot claim an input tax deduction for the purchase.

10. The CZR rules effectively streamline the GST cash flows for transactions involving land and, in so doing, are intended to protect the tax base from phoenix schemes.

How do the CZR Rules work?

11. Usually, a registered person making a supply in the course or furtherance of their taxable activity charges GST at the prevailing standard rate on the supply (s 8(1)). In some situations, zero-rating rules apply, requiring the supplier to charge GST at the rate of 0% on the supply (s 11).

12. The core provision of the CZR rules is s 11(1)(mb). Section 11(1)(mb) provides:

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

    …

    (mb) the supply wholly or partly consists of land, being a supply—

    (i) made by a registered person to another registered person who acquires the goods with the intention of using them for making taxable supplies; and

    (ii) that is not a supply of land intended to be used as a principal place of residence of the recipient of the supply or a person associated with them under section 2A(1)(c); or

13. Under ss 8 and 11(1)(mb), a vendor must zero-rate a supply if:

    - the supply wholly or partly consists of land;
    - the vendor is GST registered (or either will be GST registered or will be treated as GST registered) at the time of settlement;
    - the supply is being made by the vendor in the course or furtherance of their taxable activity;
    - the purchaser is a GST-registered purchaser (or will be GST registered or treated as GST registered) at the time of settlement;
    - the purchaser acquires the goods (including the land) with the intention of using them (in whole or part) for making taxable supplies; and
    - none of the land included in the supply is intended to be used as the purchaser's principal place of residence or the principal place of residence of a relative of the purchaser (see further at [41]).

14. If the supply is **not** made in the course or furtherance of a GST-registered vendor's taxable activity, for example when a GST-registered vendor sells their private home, the supply is generally outside the GST rules.

15. Where a supply made in the course or furtherance of the vendor's taxable activity wholly or partly consists of land, and the supply includes the provision of services, the supply of those services is treated as a supply of goods for the purposes of s 11(1)(mb) (see s 5(24)).

What information must a purchaser provide to a vendor?

16. Under s 78F(2), whenever a supply wholly or partly consists of land, the purchaser must notify the vendor at or before settlement as to whether the purchaser:
    - is, or expects to be, a GST-registered person at the time of settlement;
    - is acquiring the land and any other goods with the intention of using them (wholly or partly) for making taxable supplies; and
    - intends using the land as a principal place of residence for themselves or a person associated with them under s 2A(1)(c) (that is, a relative).
17. This notice is required whenever a supply wholly or partly consists of land regardless of the vendor's GST-registration status, because s 78F applies "where a supply wholly or partly consists of land". In this context notification can take the forms specified in s 14C of the Tax Administration Act 1994, which essentially means notice needs to be given in writing by electronic means or by delivery of a handwritten or printed document. The vendor cannot waive the purchaser's statutory requirement to notify them under s 78F (*Y & P NZ Limited v Wang* [2017] NZCA 280).
18. If the purchaser does not notify the vendor or supplies incorrect information, this will not prevent the CZR rules from applying to zero-rate the supply where, at settlement, the conditions for zero-rating in s 11(1)(mb) were met. This means corrections to the GST treatment of the supply may need to be made (by both the vendor and the purchaser) if a supply is incorrectly standard-rated. (See further at [62].)
19. The vendor is entitled to rely on the purchaser's most recent notice when deciding whether to standard-rate or zero-rate the supply, as appropriate. The vendor's obligations at settlement are discussed further at [57].

How does a purchaser provide the required information to a vendor?

20. In most cases, when a purchaser enters into a transaction with a vendor involving the supply of land, the notice requirements in s 78F are satisfied by the purchaser completing a schedule to the written sale and purchase agreement (for example, Schedule 2 to the standard form agreement for sale and purchase prepared by the Auckland District Law Society and Real Estate Institute of New Zealand).
21. The purchaser is required to notify the vendor at or before settlement (see s 78F(2)). Therefore, in practice, the information provided in the purchaser's notice to the vendor is usually provided on a prospective basis; that is, on the basis of the purchaser's best prediction as to their GST status and intentions at settlement. For example, if a purchaser is not registered for GST when they enter into the sale and purchase agreement but intends to register before settlement, they may indicate in their notice to the vendor that they expect to be registered for GST by the settlement date.
22. If, before settlement, a purchaser's circumstances change so an earlier s 78F notice (eg, the notice provided in Schedule 2 to the sale and purchase agreement) is no longer correct they should notify the vendor in writing of the relevant changes to their circumstances at or before settlement (see *Y & P NZ Limited v Wang* [2017] NZSC 126). This will ensure the purchaser has complied with the requirements of s 78F(2) and will enable the vendor to apply the correct GST treatment to the supply for the parties.
23. A vendor should consider standard-rating a supply involving land if the purchaser fails to notify them in writing about their GST-registration status and their intentions for the land, unless the vendor is confident at settlement the CZR rules will apply to the supply. This ensures the vendor accounts for GST on the appropriate due date rather than having to correct the GST position later. Of course, in so doing, there is a risk a vendor may wrongly decide to standard-rate a supply and corrections will be needed. Therefore, overall, the best approach is for:
    - the vendor to insist on being notified in writing about the purchaser's GST-registration status and their intentions for the land at or before settlement; and
    - the purchaser to provide the correct information in writing to the vendor, and update that information in writing before settlement if their circumstances change.

24. If the purchaser who contracts with the vendor does not intend to receive the goods (including land) themselves, but nominates or intends to nominate a third party to receive the supply, the purchaser may make representations on behalf of the nominated person (see s 78F(5)). A vendor cannot rely on a purchaser's statement where a nomination has occurred, unless the purchaser's statement is about the nominee's position. Ultimately, it is the GST-registration status and intentions of the recipient of the supply that must be communicated in writing to the vendor before or at settlement. This same rule applies when the vendor is making the supply to a person acting as agent for an undisclosed principal who is purchasing the land. The notification requirements in s 78F(2) are met in that case if the agent notifies the vendor that the principal as purchaser will meet the requirements of s 11(1)(mb) at settlement (see s 78F(6)). In nominee or undisclosed principal situations, it is important that the notification requirements in s 78F are about the nominee or undisclosed principal's position. It may be necessary for the s 78F notice to be updated to ensure the vendor has the correct information at settlement.

25. If a supply wholly or partly consisting of land is made by a lender under a power of sale in satisfaction of a debt (see s 5(2)), the purchaser must provide the information required under s 78F to the lender and not the borrower (owner). For example, the information should be provided to the bank under a mortgagee sale. This is because the sale is being undertaken by the lender. (However, for the purposes of determining whether the supply is zero-rated under the CZR rules, s 11(1)(mb) should be applied as if the supply were being made by the borrower (owner) and not by the lender (see s 5(22).)

When will a supply wholly or partly consist of land?

26. Knowing whether a supply wholly or partly consists of land is important for determining whether the CZR rules apply to the supply. The term "land" is defined broadly in s 2 for the purposes of the zero-rating of land rules (that is, including for the purposes of ss 11(1)(mb) and 78F). The definition of "land" includes:

- an estate or interest in land (for example, a freehold estate in land);
- a right that gives rise to an interest in land (for example, a profit à prendre);
- an option to acquire land or an estate or interest in land; and
- a share in the share capital of a flat-owning or office-owning company, as defined in the Land Transfer Act 1952.

27. The definition of "land" excludes:

- mortgages; and
- leases of dwellings.

28. Most commercial leases are excluded from the CZR rules by s 11(8D)(b). As a result, most rental payments under commercial leases continue to be standard-rated. However, commercial leases with characteristics making them substitutable for land sales and transactions involving the assignment, surrender or procurement of commercial leases may be subject to the CZR rules if the conditions in s 11(1)(mb) are met (see s 11(8D)(a), (ab) and (c)).

What if the land is only part of the supply?

29. A supply consisting **wholly** or **partly** of land must be zero-rated when the conditions in s 11(1)(mb) are met; even where the land forms only one part of the supply. This means all the components of a single composite supply must be zero-rated, not only the land component. For example, if land and other assets are sold in a single supply, the whole of the supply must be zero-rated when the conditions in s 11(1)(mb) are met for the land component.

30. Where there are multiple supplies within the same contract (compared with one single composite supply), the GST treatment of each of those separate supplies is determined separately. If any of those separate supplies in whole or in part include land, the CZR rules will need to be considered. Therefore, as a first step, before determining whether the CZR rules apply to a land transaction, it is necessary for the vendor to establish what supplies they are making to the purchaser. (For help on establishing what supplies are being made see *Interpretation Statement 17/03:* Goods and Services Tax - single supply or multiple supplies.)

Supplies including a residence

31. There is a special rule for supplies which include a residence. Before s 11(1)(mb) is applied, a supply including a residence might be deemed to be made up of two (or more) separate supplies (see s 5(15)). Section 5(15) provides:

> **5 Meaning of term supply**
>
> …
>
> (15) When either of the following supplies are included in a supply, they are deemed to be a separate supply from the supply of any other real property that is included in the supply:
>
> (a) a supply of a principal place of residence:
>
> (b) a supply referred to in section 14(1)(d).

32. For the purposes of s 5(15)(b) "a supply referred to in section 14(1)(d)" is essentially a sale of a dwelling that has been used exclusively for making supplies of accommodation for five years or more before the date of supply.

> **14 Exempt supplies**
>
> (1) The following supplies of goods and services shall be exempt from tax:
>
> …
>
> (d) the supply, being a sale, by any registered person in the course or furtherance of any taxable activity of—
>
> (i) any dwelling; or
>
> (ii) the reversionary interest in the fee simple estate of any leasehold land,—
>
> that has been used by the registered person for a period of 5 years or more before the date of the supply exclusively for the making of any supply or supplies referred to in paragraph (c) or paragraph (ca):

33. A supply that includes a principal place of residence or a dwelling that has been rented out by the vendor exclusively for accommodation for at least the preceding five years is deemed to be a separate supply from the supply of any other real property included in the (larger) supply (see s 5(15)).

34. For example, when a farm (which includes the farmer's house and its surrounding curtilage) is sold, under s 5(15) the supply of the farm house and curtilage is deemed to be a separate supply from the supply of the remainder of the farm. The GST treatment of each supply is then determined separately. Usually, the supply of a farm house and curtilage is not subject to GST on the basis the farm house is the farmer's private asset (that is, outside the famer's taxable activity). (Occasionally, the farmer may have claimed an input tax deduction when they acquired the farm house. In that case, an output tax liability may arise on sale (see s 5(16) and (18).) The GST treatment of the supply of the remainder of the farm must also be established. If the conditions of s 11(1)(mb) are satisfied the supply of the remaining portion of the farm must be zero-rated.

35. The Commissioner's view is as follows:
    - The phrase "principal place of residence" in s 5(15)(a) refers to a place occupied as a person's main residence. The plain meaning of the phrase indicates a person may have more than one residence, but at any point in time they can have only one main residence.
    - The application of s 5(15)(a) is not restricted to a place occupied as the vendor's main residence. It is possible for a vendor to supply a principal place of residence that is not their own residence (for example, a house that has been lived in by a farm manager).
    - Section 5(15)(a) is concerned with the **supply** of a principal place of residence. Therefore, for the purposes of s 5(15) the vendor's use of the property is determinative rather than the purchaser's intended use of the property. This is in contrast to how the phrase is used in s 11(1)(mb), which focuses on the purchaser's (or their relative's) intended use of the land (see further at [44]).
    - The inquiry in s 5(15)(a) is objective, based on the available information.

What conditions need to be satisfied for the CZR rules to apply?

36. As stated earlier, certain conditions need to be satisfied for a supply made in the course or furtherance of a vendor's taxable activity to be compulsorily zero-rated. Section 11(1)(mb) provides that a supply that wholly or partly consists of land must be zero-rated, if, at settlement date, the following conditions are satisfied:
    - *GST registration:* The supply is being made by a GST registered vendor (or a vendor who will be or who will be treated as GST registered) at the time of settlement to a GST-registered purchaser (or a purchaser who will be or who will be treated as GST registered) at the time of settlement.
    - *Intention for using to make taxable supplies:* The purchaser acquires the goods (including the land) with the intention of using them (in whole or part) for making taxable supplies.
    - *No intention for using as a principal place of residence:* None of the land included in the supply is intended to be used as the purchaser's principal place of residence or the principal place of residence of a relative of the purchaser (see further at [44]).

37. These conditions for compulsory zero-rating are now considered in more detail.

GST registration

38. For a supply wholly or partly consisting of land to be compulsorily zero-rated both parties must be registered persons (that is, the supply must be made by a vendor who is a registered person to a purchaser (or their nominee) who is a registered person).

39. A "registered person" is defined in s 2 as a person who is registered or liable to be registered under the Act. Therefore, if the parties to the supply are liable to be GST registered at the time of settlement (and the other conditions for compulsory zero-rating are met), the CZR rules will apply regardless of whether one or both are actually registered for GST at that time.

Purchaser's intention for using the goods acquired (including land)

40. The CZR rules require a purchaser who is a registered person to acquire the goods supplied (including land) with the intention of using them for making taxable supplies. For the purposes of applying the CZR rules a purchaser's registration status is determined as at the date of settlement. In the Commissioner's view, the requirement for the purchaser to intend using the goods acquired (including land) for making taxable supplies will be satisfied even where the purchaser does not intend using **all** the goods acquired for making taxable supplies (that is, the goods acquired do not need to be **wholly** applied to the purchaser's taxable activity). This is consistent with the GST apportionment rules. Those rules require a purchaser to make an intial GST output tax adjustment where goods to which s 11(1)(mb) applies are acquired but not intended to be used wholly for making taxable supplies and then possible subsequent adjustments if actual use changes from what was intended (see s 20(3J)). This means that even if a purchaser intends using only some of the goods acquired (including land) for making taxable supplies, the CZR rules will still apply to zero-rate the whole supply if the other conditions of s 11(1)(mb) are met.

Land not intended to be used as purchaser's (or their relative's) principal place of residence

41. A supply consisting of land between parties who are registered persons will not be compulsorily zero-rated if the purchaser intends using the land or any part of it as their principal place of residence or the principal place of residence of a person associated with them under s 2A(1)(c).

42. For the purposes of the CZR rules a person associated with a purchaser under s 2A(1)(c) is a relative of the purchaser. A relative is a person who is connected to the purchaser by:
    - blood relationship;
    - marriage, civil union or de facto relationship; or
    - adoption.

43. Effectively, this means the "principal place of residence" exclusion from the CZR rules is limited to purchasers who are natural persons, because only a natural person can have a principal place of residence or a relative.

44. The phrase "principal place of residence" is used differently in ss 11(1)(mb)(ii) and 5(15) (see [35]). In s 11(1)(mb)(ii), it is the purchaser's intention for the land at the time of settlement that is relevant, rather than the land's existing use in the hands of the vendor as it is under s 5(15).

45. While a person can have only one principal place of residence for their own occupation at any one time (that is, their main residence), s 11(1)(mb)(ii) also includes the situation where a purchaser acquires land intended to be used as a principal place of residence of a relative.

When is a purchaser's intention determined?

46. To know whether a supply involving land must be compulsorily zero-rated, the vendor needs to know how the purchaser intends to use any goods supplied (including the land). The purchaser's intention at settlement for the goods (including the land) is relevant for the purposes of s 11(1)(mb)(i) and (ii) (see s 11(8B)). It also forms the basis of the statements made by the purchaser when they notify the vendor about their intentions at settlement for the goods (including the land) for the purpose of s 78F(2).

47. Usually the purchaser's immediate intention for the use of the goods (including the land) once they have acquired them (ie, at settlement) will provide the best indication of how the goods (including the land) will be used for the purposes of s 11(1)(mb). However sometimes, at settlement, a purchaser may have a well-developed overall plan for the use of the goods (including the land) that clearly evidences how they intend to use them. Where that plan provides a fair and reasonable result for the purchaser's intended use of the goods (including the land), it may be an appropriate indicator of how the goods (including the land) will be used for the purposes of s 11(1)(mb). This interpretation is consistent with the scheme of the Act, in particular with the apportionment rules and the requirement to make an initial adjustment under s 20(3J) based on intended use and possible subsequent adjustments if actual use changes from what was intended (see ss 20(3J) and 21 to 21H).

48. Where s 11(1)(mb) applies to zero rate the supply, s 20(3J) directs the purchaser to make an apportionment adjustment when acquiring a supply of goods and services for making mixed supplies (that is, for making some taxable supplies and some non-taxable supplies). Section 20(3J)(a)(ii) requires the purchaser to apply s 20(3G) to estimate how they intend to use the goods or services at acquisition.

49. Section 20(3G) requires the purchaser to use an approach that leads to a fair and reasonable result:

(3G) In determining the extent to which goods or services are used for making taxable supplies, **a person must estimate at the time of acquisition how they intend to use the goods or services, choosing a determination method that provides a fair and reasonable result**. The determination is expressed **as a percentage of the total use**.

[Emphasis added]

When should a purchaser make output tax adjustments for non-taxable use?

50. Purchasers who acquire goods (including land) that have been compulsorily zero-rated under s 11(1)(mb) may need to make output tax adjustments to account for any non-taxable use of the acquired goods. Adjustments may need to be made:
    - when the goods (including land) are acquired (s 20(3J)(a)); and
    - in later adjustment periods under the apportionment rules in ss 21 to 21H (s 20(3J)(b)).
51. At the time the compulsorily zero-rated goods are acquired, under s 20(3J)(a) the purchaser must identify the "nominal GST component" that would have been chargeable if the supply of goods had been standard-rated. This is done by adding GST at the standard rate to the agreed consideration for the supply. The purchaser is then required to determine the extent to which they intend to use the goods acquired for making taxable supplies and calculate the proportion of the nominal GST component for any non-taxable use of the goods. The non-taxable use proportion of the nominal GST component is an amount of output tax and must be accounted for by the purchaser in their GST return for the period the supply is attributed to (see s 20(4)).
52. To determine the intended non-taxable use of the goods acquired (including land) the purchaser needs to estimate at the time of acquisition how they intend to use the goods, choosing a determination method that produces a fair and reasonable result (see s 20(3G)).
53. Further output or input tax adjustments may be needed under the apportionment rules in subsequent adjustment periods (see ss 21 to 21H). This is done by comparing the intended use of the goods (including land) as determined at the time of acquisition against the actual use of the goods at the end of an adjustment period. Adjustments may not be required where the amounts involved are small (see s 21(2)).
54. Adjustments may be required under s 21E for the concurrent use of land where the purchaser is using the same area of land for making concurrent taxable and non-taxable supplies.

What if the parties agree to treat the supply as a supply of a going concern?

55. The parties to a compulsorily zero-rated supply including land can also agree to treat the supply as the supply of a taxable activity as a going concern. This is because s 11(1)(m) (the going concern rule) and s 11(1)(mb) (the CZR rule) can both apply to the same supply. The application of s 11(1)(mb), which is an objective test, does not exclude the application of s 11(1)(m), or vice versa.
56. However, where both s 11(1)(m) and s 11(1)(mb) do apply to the same supply then the GST-registered purchaser may still need to make an output tax adjustment under s 20(3J). This is because a s 20(3J) adjustment needs to be considered whenever s 11(1)(mb) applies to a supply. The application of s 11(1)(m) in that situation does not prevent an adjustment under s 20(3J).

What are the vendor's obligations under the CZR rules?

57. When making a supply wholly or partly consisting of land, the vendor has to determine whether the correct GST treatment of the supply is that it must be zero-rated under s 11(1)(mb). To do this, the vendor must be aware of their own GST-registration status at settlement as well as that of the purchaser (or their nominee). The vendor should be notified by the purchaser (or their nominee) about the recipient of the supply's registration status and their intentions for the goods (including land) being supplied. The vendor is entitled to rely on the purchaser's notice to standard-rate or zero-rate the supply, as appropriate (see s 78F(3)). This entitlement is intended to make it easier for the vendor to determine their GST treatment of the supply. If the purchaser's most recent written notice to the vendor indicates that the conditions in s 11(1)(mb) are or will be met at settlement, the vendor should generally zero-rate the supply. If the notice indicates otherwise, the vendor should generally standard-rate the supply. While the vendor is not required to rely on the purchaser's notice, in the Commissioner's view, a vendor should only depart from a purchaser's s 78F notice if they know at settlement the departure will result in the correct GST treatment being applied to the supply at settlement. The Commissioner considers this situation will not be common because mostly the vendor should be able to rely on the information provided in the purchaser's notice.

58. If the vendor incorrectly standard-rates or incorrectly zero-rates a supply, corrections to the GST treatment of the supply will need to be made (both by the vendor and the purchaser). (See further at [78].)

What happens if the purchaser does not provide the required information?

59. If the purchaser refuses to or does not provide the required information about their GST-registration status and their intentions for the goods acquired (including land), it is recommended the vendor standard-rates the transaction, unless the vendor is confident at settlement the CZR rules will apply to the supply and that zero-rating is the correct GST treatment of the supply. By standard rating the supply in this situation the vendor ensures that any GST payable for the supply is accounted for by the vendor at the appropriate time. If it is subsequently found that the supply should have been zero-rated, then the GST cash flows can be corrected.

What are the vendor's record-keeping requirements?

60. Under s 75(3B), even where a supply is compulsorily zero-rated, the vendor must keep sufficient records to enable the following details in relation to the supply to be determined:

- the name and address of the purchaser;
- the GST-registration or tax file number of the purchaser (if known);
- a description of the land; and
- the consideration paid for the supply.

61. Where the vendor makes the supply to an agent for an undisclosed principal (the purchaser) they must keep sufficient records to be able to ascertain the name, address and GST registration or tax file number of the agent. In turn, the agent needs to keep sufficient records to do the same for the principal (see ss 75(3C) to 75(3E)).

What happens if the GST treatment is incorrect?

62. Sometimes, for a variety of reasons, a vendor's GST treatment of a transaction involving land may be incorrect. For example, a purchaser's circumstances might change and they fail to notify the vendor of the change before settlement, or a purchaser might enter into an agreement on the basis they will not be GST-registered, but it transpires that, in fact, they will be or should have been GST-registered at or before the settlement date. Sometimes, the Commissioner will back-date a person's GST registration. The consequences of an incorrect GST treatment depend on whether the mistake is discovered before or after settlement. The general rules for correcting incorrectly rated land transactions are summarised in the table at [83].

What happens if either party's circumstances change?

63. For a supply to be zero-rated, the conditions for zero-rating in s 11(1)(mb) must be satisfied at the time of settlement. However, under the time of supply rules in s 9, often a vendor needs to determine whether the supply is standard-rated or zero-rated before settlement.

64. The vendor's decision whether to zero-rate the supply is based on their knowledge of their GST-registration status and the information provided in the purchaser's notice to them. Sometimes after contracting but before settling the transaction, the vendor's or the purchaser's plans or GST-registration status may change. In the Commissioner's view, if the purchaser's intentions or status changes after they provide the s 78F notice to the vendor, the purchaser (or their nominee) should notify the vendor in writing of any relevant changes before settlement so the vendor may reconsider whether the CZR rules apply. (Often this might also be a contractual requirement in the sale and purchase agreement.) The vendor should also advise the purchaser before settlement of any change in their GST-registration status from that notified in the sale and purchase agreement.

65. For example, when the purchaser entered into the sale and purchase agreement they may have notified the vendor that they expected to be GST registered at the time of settlement. The vendor relies on the purchaser's notice and zero-rates the transaction when the deposit is paid (that is, at the time of supply under s 9(1)). However, after the time of supply but before settlement, the purchaser nominates a third person (the nominee) to settle the transaction. (For CZR purposes, the purchaser or the nominated person (the nominee) must provide the s 78F notice about the **nominee's circumstances** (see s 78F(5)).) In this example, this means that an updated s 78F notice is required. The nominee notifies the vendor in writing they will not be a registered person at the time of settlement. The vendor must now standard-rate the supply. Conversely, a situation may arise where the parties become aware that at settlement a transaction should be zero-rated rather than standard-rated.

66. Changes in the GST treatment of a supply can affect the commercial pricing of the transaction. Whether this is the case will depend on the terms of the contract and whether the consideration is stated as being inclusive of GST or "plus GST, if any". Also for a purchaser, the potential application of s 5(23) should be considered.

67. The time for testing the correct GST treatment of a compulsorily zero-rated supply is at the time of settlement (see s 11(8B)). Where the incorrect GST treatment was applied before settlement (for example, when the invoice was issued), the CZR rules do not require the parties to correct the treatment before the settlement date. However, if the mistake is discovered before settlement, voluntarily correcting the GST treatment prevents the GST treatment being incorrect at settlement and will also reduce any potential imposition of shortfall penalties (although the purchaser may still be liable to pay interest on any GST shortfall if a deposit was paid).

*How can the vendor correct the GST treatment **before** settlement?*

68. Where the vendor incorrectly accounts for GST before settlement, voluntary corrections may be made to the parties' tax positions using the credit and debit notes mechanism in s 25. Credit and debit notes are used to adjust the tax payable on supplies in certain situations, including where s 11(1)(mb) is incorrectly applied to the treatment of the supply. A vendor issues a credit note when the tax charged on the tax invoice exceeds the actual tax charged on a supply (that is, when a supply is incorrectly standard-rated). A vendor issues a debit note when the actual tax exceeds the tax charged in the tax invoice for the supply (that is, when a supply is incorrectly zero-rated).

69. Where s 25 applies, and the vendor has accounted for an incorrect amount of output tax, the vendor is required to make an adjustment in the GST taxable period in which it became apparent that the output tax was incorrect.

70. A purchaser must make an adjustment if they have obtained a deduction for an amount of input tax that exceeds the output tax properly charged. The excess is deemed to be tax charged in relation to a taxable supply made by the purchaser. The supply is treated as having been made in the GST taxable period in which the purchaser:

- was issued with a credit note relating to the supply; or
- received other notice or knowledge that the tax invoice they hold for the supply is incorrect.

What happens if the supply was incorrectly standard-rated?

71. If, before settlement, it is found that a supply was standard-rated when it should have been zero-rated, the vendor should correct their GST position in accordance with s 25. If the vendor has issued an invoice showing the supply as standard-rated the vendor must issue a credit note to the purchaser for the GST incorrectly charged on the supply (s 25(3)(a)). If the vendor furnished an incorrect return, the vendor should claim an input tax deduction for the GST output tax they incorrectly paid (s 25(2)(b)). Payment of any resulting refund may be withheld pending any review of the transaction by Inland Revenue (s 46). Inland Revenue may amend the vendor's assessment to ensure correctness.

72. The purchaser must account for output tax for an amount equal to any input tax deduction incorrectly obtained for the supply (s 25(4)). Depending on the underlying reason for the supply being incorrectly standard-rated, the purchaser may be liable for a shortfall penalty.

What happens if the supply was incorrectly zero-rated?

73. If, before settlement, a supply is zero-rated when it should have been standard-rated, the vendor should issue a debit notice to the purchaser (s 25(3)(b)) and pay the correct GST output tax for the supply (s 25(2)(a)). If GST-registered, the purchaser may be able to claim a deduction for a proportion of the input tax paid in relation to the supply subject to the ordinary rules.

*How can the vendor correct the GST treatment **after** settlement?*

74. Sometimes the correct GST treatment of a supply may not be established until after settlement. The consequences of correcting the GST treatment of a supply after settlement are set out below.

What happens if the supply was incorrectly standard-rated?

75. When a supply that should have been zero-rated is standard-rated and the GST output tax has been paid, the vendor may correct their treatment for GST purposes in accordance with s 25.

76. This correction is made by the vendor issuing a credit note to the purchaser for the GST incorrectly charged (s 25(3)(a)) and by claiming an input tax deduction for the GST output tax they incorrectly paid (s 25(2)(b)).

77. The purchaser must account for output tax for an amount equal to any input tax deduction incorrectly obtained for the supply (s 25(4)). Depending on the circumstances giving rise to the error the purchaser may be liable for shortfall penalties.

What happens if the supply was incorrectly zero-rated?

78. Where a supply is incorrectly treated by the parties as zero-rated instead of standard-rated (for example, the purchaser's s 78F notice was incorrect and the vendor relied on it) then in that situation s 5(23) applies. Under s 5(23) the purchaser is treated as though they were the vendor, making the purchaser liable for the GST output tax for the supply on the date of settlement. Section 5(23) states:

> (23) If section 11(1)(mb) is treated as applying to a supply of goods and, after the date on which the relevant transaction is settled, it is found that the provision does not apply, the recipient of the supply is treated as if they were a supplier making, on the date of settlement, a supply of those goods that is chargeable with tax under section 8(1).

79. The value of the supply made under s 5(23) is equal to the consideration for the original supply (s 10(7B)). (For GST purposes, the consideration for the original supply is the full purchase price, even if the amount in the sale and purchase agreement is described as being GST inclusive). The supply is treated as being made at the date of settlement. The purchaser must include the GST output tax in their relevant GST return. The purchaser may be liable to pay interest on the unpaid amount along with any applicable shortfall penalties.

80. A purchaser who is treated as a supplier under s 5(23) and who is not GST registered on settlement date is treated as if they were registered at the date of settlement, and they must apply for registration (see s 51B(4)). If they fail to apply, the Commissioner may register them (see s 51(4)(b)).

81. The purchaser cannot claim an input tax deduction for any deemed supply made under s 5(23), unless they are entitled to remain GST registered or they become registered for GST at a later date and use the relevant goods for making taxable supplies (see s 20(4B)).

82. Once GST is accounted for under s 5(23), the purchaser may request that the Commissioner cancel their GST registration (see s 51B(5)). Usually a person cancelling their registration must account for output tax on any goods and services forming part of the assets of a taxable activity carried on by the person (see s 5(3)). However, under s 51B(6), the rule in s 5(3) does not apply, if:

- the person seeks cancellation of their registration by the end of the taxable period in which they have accounted for output tax under s 5(23); or
- the Commissioner agrees with the person's application that s 5(3) should not apply.

Summary of rules for correcting incorrectly rated land transactions

83. The following table summarises the rules for correcting the GST treatment of incorrectly rated land transactions:

Treatment of supply	BEFORE SETTLEMENT OF TRANSACTION		AFTER SETTLEMENT OF TRANSACTION	
	Vendor	Purchaser	Vendor	Purchaser
Supply treated as standard-rated when it should have been zero-rated	Vendor issues a credit note under s 25(3)(a). If the vendor has furnished an incorrect return, the vendor should claim an input tax deduction for the GST output tax they incorrectly paid (s 25(2)(b) and s 20(3)).	If the purchaser has obtained an input tax deduction, the purchaser makes a s 25(4) adjustment in the period they become aware the standard–rated treatment is incorrect.	Vendor issues a credit note under s 25(3)(a). If the vendor has furnished an incorrect return, the vendor should claim an input tax deduction for the GST output tax they incorrectly paid (s 25(2)(b) and s 20(3)).	If the purchaser has obtained an input tax deduction, the purchaser makes a s 25(4) adjustment in the period they become aware the standard–rated treatment is incorrect.
Supply treated as zero-rated when it should have been standard-rated	The vendor should issue a debit note (s 25(3)(b)) and pay the GST output tax for the supply (s 25(2)(a)).	If the purchaser is not GST registered, no adjustment is necessary. If the purchaser is GST-registered they may be entitled to an input tax deduction, but only *to the extent* the goods are intended to be used for making taxable supplies.	Where s 5(23) applies to the purchaser, the vendor is not required to make any correction.	The purchaser is liable for output tax under s 5(23) where the parties have incorrectly treated the supply as zero-rated. The purchaser is not entitled to an input tax deduction for tax paid under s 5(23), unless they are entitled to remain or later become GST-registered, and then only *to the extent* the goods will be used for making taxable supplies (s20(4B)).

Examples

84. The following examples illustrate how the CZR rules apply to common transactions involving land. They have been simplified to ensure the CZR principles are the focus of the examples. The examples include some GST inclusive transactions and some "plus GST, if any" transactions. This is to illustrate that different GST outcomes can arise for vendors and purchasers based on the different approaches to pricing. **If in doubt, parties should seek professional advice before agreeing the purchase price for a supply.**

Example 1: Zero-rated supply of land to a purchaser's nominee

85. Tidy Motors Limited is moving to bigger premises in Wiri and has agreed to sell its existing building to John. John intends to use the building as a place where he can carry on his joinery business. The agreement provides that the consideration for the supply includes any rates and body corporate fees previously paid by Tidy Motors Limited for the premises before settlement date, apportioned between Tidy Motors Limited and John at settlement.

86. When John agrees to purchase the new premises he completes the sale and purchase agreement as an individual. However, before settlement, he decides to nominate his company, Plane Joinery Limited, to be the actual purchaser. Accordingly, before settlement he notifies Tidy Motors Limited of this change and advises Tidy Motors Limited in writing that Plane Joinery Limited is GST registered, that the company intends using the premises for carrying on its business, and, as the purchaser is a company, no part of the premises will be a principal place of residence.

87. Under s 11(1)(mb), the supply of the premises must be zero-rated as the supply wholly or partly consists of land and:

- Tidy Motors Limited and Plane Joinery Limited are both GST registered;
- the building will be used for the purpose of making taxable supplies; and
- it will not be a principal place of residence for the purchaser, Plane Joinery Limited.

88. The sale of the premises is a supply of land and Tidy Motors Limited treats it as a zero-rated supply (including the apportioned rates and body corporate fees). Tidy Motors Limited makes sure sufficient records about the sale are retained to satisfy its record-keeping requirements. Plane Joinery Limited does not claim an input tax deduction because the supply was zero-rated.

Example 2: Standard-rated supply of a new house

89. Big Sea Developers Limited is a GST-registered property developer in Papamoa. It is in the business of building and selling new homes and has developed a new subdivision. Sally, a GST-registered hairdresser, loves the seaside lifestyle and agrees to purchase a new house from Big Sea Developers Limited. She intends to live in the house but does not intend working from home. Sally makes sure she notifies Big Sea Developers in writing about how she intends to use the property before settlement date.

90. Sally's purchase of a new house from Big Sea Developers should be standard-rated for GST. The supply of the house by the developer is a taxable supply because the house forms part of the developer's taxable activity, so is not an exempt supply. The CZR rules do not apply to zero-rate the supply because, although Sally is GST registered, she does not intend using the house to make taxable supplies and she will be using the house as her principal place of residence. Sally will not be entitled to claim a GST input tax deduction for the purchase because she will not be using the house in her taxable activity.

Example 3: Standard-rated supply of bare land

91. Stephen, a GST-registered property developer, purchases land in his own name from a GST-registered vendor to build a three-storey building. The lower two levels of the new building will be used as Stephen's business premises and the top level will be used as a residence for his son. The supply of the bare land will not be zero-rated because at settlement Stephen intends using part of the land as a principal place of residence for his son. Stephen completes Schedule 2 to the sale and purchase agreement ensuring the vendor knows about his intentions for the land before the settlement date. The supply of the land for the residence is not a separate supply under s 5(15) because the vendor is simply supplying bare land and not an exisiting principal place of residence to Stephen. The supply will be standard-rated.

92. Stephen may claim GST input tax deductions but only to the extent the land will be used for making taxable supplies (see ss 20(3) and 20(3C)).

93. If Stephen purchases the bare land through his development company rather than in his own name, the CZR rules would likely apply to zero-rate the supply, as Stephen's son cannot be a relative of the company. The company cannot intend using part of the land as its principal place of residence. In that case, on acquisition, the company would need to make an output tax adjustment under s 20(3J) for the intended non-taxable use of the land and, subsequently, would need to consider whether any further adjustments are needed at the end of each adjustment period under ss 21 to 21D.

Example 4: Supply of land, business and dwelling

94. Dylan owns a garden centre in Levin that he is selling to his neighbour Sharon. The agreement provides for all of the business assets to be transferrred to Sharon, including the garden centre land, the shop, and a small house and garden that Dylan and his family built when they established the business. Dylan has not treated the house and its curtilage as part of his taxable activity.

95. Both Dylan and Sharon are GST registered. Sharon advises Dylan in writing that she intends using the garden centre assets for the purpose of making taxable supplies. Sharon intends carving off some of the garden centre land adjoining her existing house next door to the garden centre to build a private garage. She also plans to convert Dylan's house into a café, so no one will be living in the house after settlement.

96. Under s 5(15), where a supply includes a principal place of residence, the supply of the principal place of residence is deemed to be a separate supply from the supply of any other real property included in the supply. Accordingly, the supply of Dylan's home and curtilage needs to be treated separately from the supply of the rest of the garden centre assets for GST purposes.

97. Under s 11(1)(mb), the whole of the remaining supply of garden centre assets (that is, other than the house and curtilage) must be zero-rated as the supply wholly or partly consists of land and:

- Dylan and Sharon are both GST registered;
- Sharon intends using at least some of the garden centre assets for making taxable supplies; and
- Sharon does not intend to use the land acquired as a principal place of residence for herself or for any of her relatives.

98. The supply of Dylan's house and curtilage to Sharon is not subject to GST because they never formed part of his taxable activity. Sharon may claim a second-hand goods input tax deduction for the purchase of Dylan's house and curtilage because she will be using them in her taxable activity for making taxable supplies (see s 20(3)(a)(ia)).

99. Dylan returns the sale of the garden centre assets (other than his house and curtilage) as a zero-rated supply, and makes sure he keeps sufficient records about the sale to satisfy the record-keeping requirements.

100. Even though Sharon does not intend to use all the garden centre assets for making taxable supplies, the whole remaining supply of the garden centre assets (that is, other than the house and curtilage) must be zero-rated.

101. On acquisition, Sharon estimated (using a method that produces a fair and reasonable result (s 20(3G)) that she intends using 20% of the remaining garden centre land for her private purposes. On that basis, under s 20(3J), she calculated she needed to pay $30,000 output tax. Sharon accounts for the output tax in her return. Sharon then, in the future, needs to consider making further adjustments under the apportionment rules, if her actual use of that land is different from her intended use (s 20(3J)(b)).

Example 5: Correcting an incorrectly standard-rated supply before settlement – plus GST, if any

102. Max, a GST-registered vendor, agrees to sell land to Geoff for $500,000 plus GST, if any. Geoff informs Max in writing that he does not expect to be GST registered at the time of settlement and has no intention of using the land for taxable purposes.

103. Before settlement, Max issues a tax invoice on the basis that the supply is standard-rated and GST of $75,000 is chargeable on the supply. The invoice triggers the time of supply, and Max pays $75,000 output tax.

104. Following the time of supply but before settlement, Geoff advises Max again in writing that his circumstances have changed and he will be registered for GST at the time of settlement, will use the land for making taxable supplies, and will not use the land as his or his relative's principal place of residence. On this basis, the supply should be zero-rated at settlement. The parties want the correct GST position to be achieved before settlement. Therefore, Max issues a credit note to Geoff under s 25 and makes an input tax deduction of $75,000 for the amount of GST output tax already paid (s 20(3)(a)(iii)). (Note: payment of any resulting refund may be withheld pending settlement (s 46) to ensure the correct treatment has been adopted).

105. Settlement occurs and Geoff pays Max $500,000. Geoff's first return period ends after settlement. Geoff claims no input tax deduction for the supply because it is a zero-rated supply.

Example 6: Correcting an incorrectly zero-rated supply before settlement – plus GST, if any

106. Tamati, a GST-registered property developer, agrees to sell land to Graeme, who is not registered for GST, for $1 million plus GST, if any. In the sale and purchase agreement, Graeme specified that on settlement he would be registered for GST, would acquire the property with the intention of using it for making taxable supplies, and would not use it as his or his relative's principal place of residence. Therefore, the parties treat the supply as zero-rated under the CZR rules.

107. Before the date of settlement, Tamati issues an invoice, triggering the time of supply. Since Tamati treats the transaction as zero-rated, he does not pay any GST output tax.

108. Following the time of supply but before settlement, Graeme informs Tamati that his circumstances have changed and that he will not be registered for GST at the date of settlement. As a result, the correct GST treatment of the transaction is to standard-rate the supply.

109. The parties want the correct amount of GST to be paid before settlement. Tamati issues a debit note under s 25 to Graeme showing the GST on the supply and pays GST output tax of $150,000. Graeme pays Tamati the $150,000 of GST but since Graeme is not registered for GST, he claims no input tax deduction for the purchase.

Example 7: Correcting an incorrectly zero-rated supply before settlement – GST-inclusive contract

110. Troy, a GST-registered property developer, agrees to sell land to Gary, who is not registered for GST, for the GST-inclusive price of $1 million. In the sale and purchase agreement, Gary advises that on settlement he will be registered for GST, will acquire the property with the intention of using it for making taxable supplies, and will not use it as his or any relative's principal place of residence. Therefore, the parties treat the supply as zero-rated under the CZR rules.

111. Before the date of settlement, Troy issues an invoice, triggering the time of supply. Since Troy treats the transaction as zero-rated, he does not pay any GST output tax.

112. Following the time of supply but before settlement, Gary informs Troy in writing that his circumstances have changed and that he will not be registered for GST at the date of settlement. As a result, the correct GST treatment of the transaction is to standard-rate the supply.

113. The parties want the correct amount of GST to be paid before settlement. As the parties agreed the purchase price includes GST, Troy issues a debit note under s 25 to Gary showing the GST tax fraction on the supply. Troy pays GST output tax of $130,435. This reduces the purchase price Troy receives for the sale to $869,565 (GST exclusive). Since Gary is not registered for GST, he claims no input tax deduction for the purchase.

Example 8: Correcting an incorrectly standard-rated supply after settlement

114. Padma, a GST-registered vendor, agrees to sell land to Brent for $200,000 plus GST, if any. Brent informs Padma in writing that he does not expect to be registered for GST at the time of settlement and does not intend to use the land for taxable purposes.

115. Before settlement, Padma issues a tax invoice showing GST of $30,000 for the supply. The invoice triggers the time of supply and Padma pays the output tax. The parties settle the transaction.

116. Shortly after settlement, Brent is investigated by Inland Revenue and it is determined that, in fact, he has been carrying on a taxable activity and should have been GST registered since before he entered in to the sale and purchase agreement with Padma. His GST registration is backdated to before settlement. Since settlement Brent has been using the land for making taxable supplies and not as his (or his relative's) principal place of residence. This means that at the time of settlement, all conditions in s 11(1)(mb) for zero-rating were actually satisfied, so the supply should have been zero-rated rather than standard-rated.

117. On being advised of the incorrect treatment, Padma issues a credit note under s 25 and claims an input tax deduction for the $30,000 output tax she paid before settlement in the return for the taxable period during which it became apparent that the output tax is incorrect. Padma also makes sure she keeps sufficient records about the sale to satisfy the record-keeping requirements for zero-rated supplies involving land. Since Brent has no input tax deduction, he is not required to make any adjustment when he receives the credit note.

Example 9: Correcting an incorrectly

118. Isla agrees to acquire land for a GST-inclusive price of $1 million. In the notice provided to the vendor, Isla indicates she is registered for GST, intends using the land for making taxable supplies and will not use the land as her own or any relative's principal place of residence. On the basis of Isla's information, the vendor zero-rates the supply.

119. The transaction is settled on 1 March 2016. However, after settlement it is determined Isla should not have been registered for GST at settlement as she was not carrying on taxable activity. As a result, the supply was wrongly treated by the parties as being zero-rated. The notice provided by Isla, and relied on by the vendor, was incorrect. The supply should have been standard-rated.

120. In those circumstances, under s 5(23), Isla is treated as making a supply of the land on 1 March 2016 (the date of settlement) and she is required to account for GST output tax on the supply at the standard rate. Isla is treated as if she is registered at the date of settlement and she must apply for registration under s 51(2) (see s 51B(4)). If Isla does not register herself, under s 51(4) the Commissioner will register her.

121. Isla must include the GST output tax based on the value of the supply in her GST return. In this case the value of the supply is an amount equal to the consideration for the original supply (see [79]). For GST purposes, the consideration is $1 million, even if described as a GST-inclusive amount. Therefore the GST output tax Isla must pay is:

    $1 million × 15% = $150,000

122. Isla is not able to claim an input tax deduction on the payment made under s 5(23) as this is denied by s 20(4B).

123. In the same taxable period in which Isla accounts for the output tax under s 5(23), she does not make any other taxable supplies. Therefore, under s 51B(5) she asks the Commissioner to cancel her registration. The Commissioner confirms that Isla's deregistration relieves her from paying any additional tax on deregistration under s 5(3) (see s 51B(6)(a)).

Example 10: Correcting a non-taxable supply after settlement

124. John and Kim have subdivided their lifestyle block into five sections. They are not registered for GST, and have recently just sold their first section privately to their neighbour Grant, who is GST-registered. The parties entered into a standard form sale and purchase agreement. Grant correctly completed the s 78F schedule to the sale and purchase agreement. He notified John and Kim that at settlement his intention was to use the land for making taxable supplies and he did not intend to use the land as his principal place of residence.

125. At settlement no GST was charged on the sale and Grant was preparing to claim a second hand goods deduction for the purchase price when Inland Revenue became aware of the transaction. It became apparent John and Kim should have been GST registered given their subdivision activities. Accordingly, John and Kim were registered with effect from when they began the subdivision activity. As a result, the sale of the section to Grant should have been zero-rated under s 11(1)(mb). This means Grant cannot claim a second hand goods deduction for the purchase.

References

Subject references

Compulsory zero-rating of land
Goods and services tax

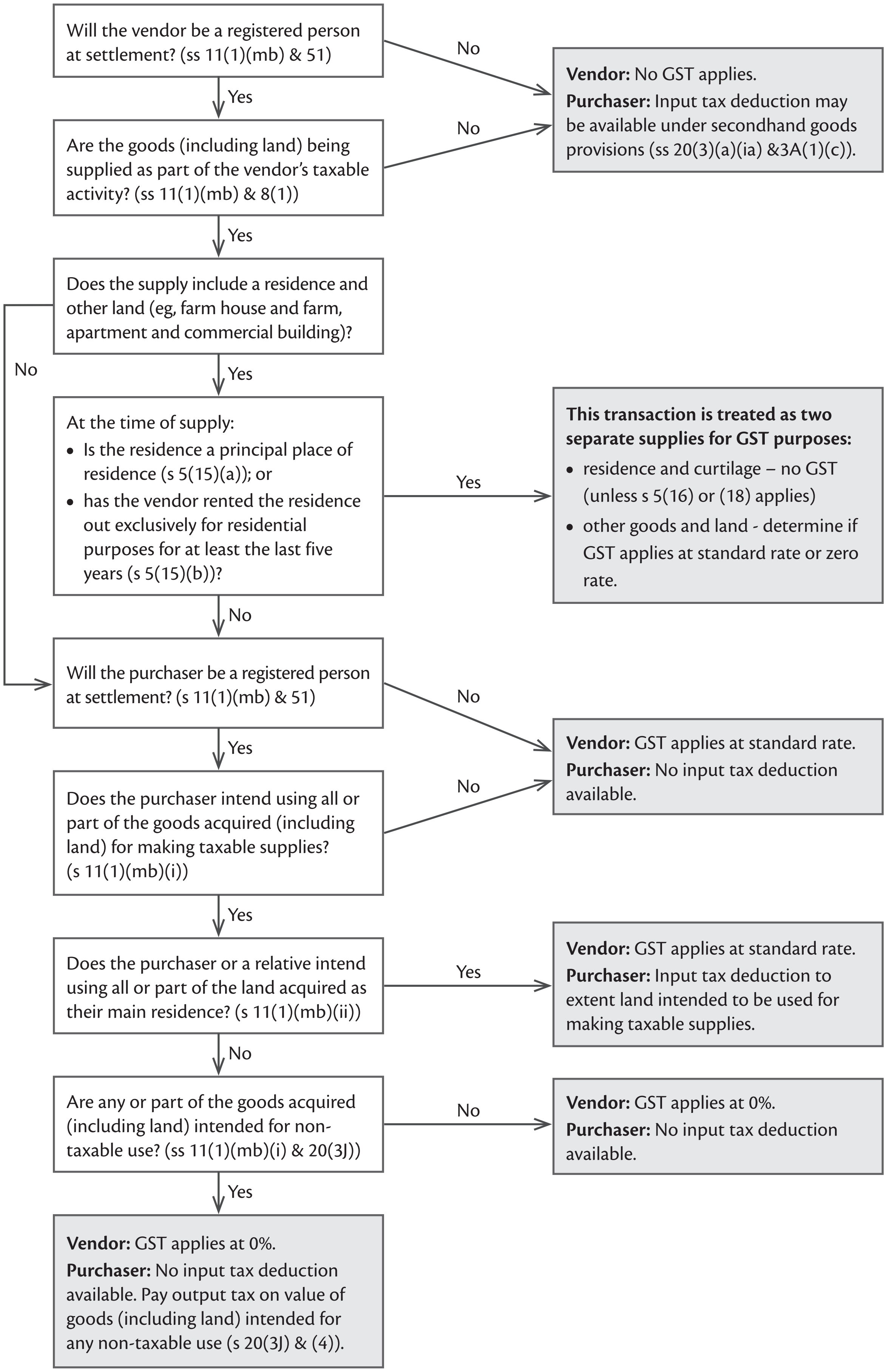
Legislative references

Goods and Services Tax Act 1985, ss 2(1) (definitions of "land" and "zero-rating of land rules"), 2A(1)(c), 5(15) and (22) to (24), 11(1)(m) and (mb),(8B), and (8D), 14(1)(d), 20(3C), (3J), (3G), and (4B), 21 to 21H, 25, 51B(4) to (6), 60B(6), 75(3B) to (3D), and 78F

Case references

Y & P NZ Limited v Wang [2017] NZCA 280
Y & P NZ Limited v Wang [2017] NZSC 126

Appendix 1: Flowchart to determine if a supply including land is compulsorily zero-rated



Appendix 2: Legislation

Goods and Services Tax Act 1985

1. The term "land" is defined in s 2 for the purposes of the zero-rating of land rules:

   land, in the zero-rating of land rules,—

   (a) includes—

   (i) an estate or interest in land:

   (ii) a right that gives rise to an interest in land:

   (iii) an option to acquire land or an estate or interest in land:

   (iv) a share in the share capital of a flat-owning or office-owning company, as defined in section 121A of the Land Transfer Act 1952:

   (b) does not include—

   (i) a mortgage:

   (ii) a lease of a dwelling:

   (iii) [Repealed]

2. The term "zero-rating of land rules" is defined in s 2:

   zero-rating of land rules means sections 5(24), 11(1)(mb), 60B(6), 75(3B), and 78F.

3. Section 2A(1)(c) provides:

   (1) In this Act, associated persons or persons associated with each other are—

   …

   (c) two persons who are—

   (i) connected by blood relationship:

   (ii) connected by marriage, civil union or de facto relationship:

   (iii) connected by adoption:

   (iv) [Repealed.]

4. Section 5(2) provides:

   (2) For the purposes of this Act, where any goods acquired (whether in terms of a hire purchase agreement or otherwise) or produced by a person (that person being referred to hereafter in this subsection as the first person) are sold, under a power exercisable by another person (that person being referred to hereafter in this subsection as the second person), in or towards the satisfaction of a debt owed by the first person, those goods shall be deemed to be supplied in the course or furtherance of a taxable activity carried on by the first person (being deemed a registered person), unless—

   (a) the supply of those goods would not be a taxable supply if those goods were sold by the first person (notwithstanding that the first person may not be the owner of those goods) and the first person has furnished to the second person a statement in writing stating fully and correctly the reasons why that supply would not be a taxable supply;or

   (b) where the second person has not been notified as described in paragraph (a), that person may determine, in relation to any reasonable information held, that the supply of those goods would not have been a taxable supply if those goods had been sold by the first person (notwithstanding that the first person may not be the owner of those goods).

5. Section 5(15) provides:

   (15) When either of the following supplies are included in a supply, they are deemed to be a separate supply from the supply of any other real property that is included in the supply:

   (a) a supply of a principal place of residence:

   (b) a supply referred to in section 14(1)(d).

6. Section 5(16) provides:

   (16) Where a registered person has claimed a deduction in accordance with section 20(3) in respect of the supply of a dwelling, any subsequent supply by the registered person of—

   (a) the dwelling; or

   (b) any land or other part of the dwelling that has ceased or will by reason of the supply cease to be appurtenant to or enjoyed with the dwelling,—

   will, for the avoidance of doubt but subject to subsections (17), (18), and (19)(b), be deemed to be a taxable supply.

7. Section 5(22) provides:

(22) In relation to a supply to which subsection (2) applies, if the supply by the first person would be zero-rated under section 11(1)(mb), the second person must zero-rate the supply in the same way.

8. Section 5(23) provides:

(23) If section 11(1)(mb) is treated as applying to a supply of goods and, after the date on which the relevant transaction is settled, it is found that the provision does not apply, the recipient of the supply is treated as if they were a supplier making, on the date of settlement, a supply of those goods that is chargeable with tax under section 8(1).

9. Section 5(24) provides:

(24) If a supply that wholly or partly consists of land is made, and the supply includes the provision of services, the supply of the services is treated as a supply of goods for the purposes of section 11(1)(mb).

10. Section 11(1)(m) provides:

11 Zero-rating of goods

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

…

(m) the supply to a registered person of a taxable activity, or part of a taxable activity, that is a going concern at the time of the supply, if—

(i) the supplier and the recipient agree that the supply is the supply of a going concern, and their agreement is recorded in a document; and

(ii) the supplier and the recipient intend that the supply is of a taxable activity, or part of a taxable activity, that is capable of being carried on as a going concern by the recipient; or

11. Section 11(1)(mb) provides:

11 Zero-rating of goods

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

…

(mb) the supply wholly or partly consists of land, being a supply—

(i) made by a registered person to another registered person who acquires the goods with the intention of using them for making taxable supplies; and

(ii) that is not a supply of land intended to be used as a principal place of residence of the recipient of the supply or a person associated with them under section 2A(1)(c); or

12. Section 11(8B) and (8D) provides:

(8B) Whether a supply of goods is zero-rated under subsection (1)(mb) is determined at the time of settlement of the transaction relating to the supply.

…

(8D) For the purposes of the zero-rating of land rules,—

(a) a supply that is an assignment or surrender of an interest in land is a supply under subsection (1)(mb) if it meets the requirements set out in that subsection and paragraph (b) does not apply:

(ab) a supply that is a surrender of a right to a payment under an agreement for the supply of an interest in land is a supply under subsection (1)(mb) if the supply of the interest in land meets the requirements set out in that subsection:

(b) a supply of an interest in land that meets the requirements of subsection (1)(mb), and is made under an agreement providing for periodic payments for supplies of the interest in land, is not a supply under that subsection for the purposes of a payment for the supply paid or payable under the agreement if—

(i) each amount payable under the agreement that is not a regular payment is anticipated, when the agreement is entered, to be 25% or less of the consideration specified in the agreement (the term consideration) for all supplies of the interest in land during the period referred to in subparagraph (iv); and

(ii) the payment, if not a regular payment, is 25% or less of the term consideration; and

(iii) each amount that is paid or payable before the payment, and is not a regular payment, is 25% or less of the term consideration; and

(iv) the term consideration is treated as being the amount of consideration calculated under the agreement for supplies anticipated to be made during a period that is the longer of 1 year and the shortest possible fixed term of the agreement:

(c) a supply by a person who is the lessee under a lease agreement is a supply under subsection (1)(mb), despite paragraph (b), if—

(i) the supply is to a person who is not the lessor supplying an interest in land under the lease agreement to the lessee; and

(ii) the supply is made under an arrangement that involves the lessee's surrender of the interest in land to the lessor and the supply by the lessor of the interest in land under another lease agreement to a person other than the lessee; and

(iii) the supplies of the interest in land under the lease agreements meet the requirements set out in subsection (1)(mb):

(d) a registered person who is a non-profit body that is resident in New Zealand and acquires goods is treated, to the extent to which the person acquires the goods with an intention of using them other than for making exempt supplies, as acquiring the goods with the intention of using them for making taxable supplies.

13. Section 14(1)(d) provides:

14 Exempt supplies

(1) The following supplies of goods and services shall be exempt from tax:

…

(d) the supply, being a sale, by any registered person in the course or furtherance of any taxable activity of—

(i) any dwelling; or

(ii) the reversionary interest in the fee simple estate of any leasehold land,—

that has been used by the registered person for a period of 5 years or more before the date of the supply exclusively for the making of any supply or supplies referred to in paragraph (c) or paragraph (ca):

14. Section 20(3C)(a) provides for the apportionment of input tax deductions on acquisition:

(3C) For the purposes of subsection (3), and if subsections (3D) or (3L) do not apply,—

(a) input tax as defined in section 3A(1)(a) or (c) may be deducted to the extent to which the goods or services are used for, or are available for use in, making taxable supplies:

15. Section 20(3J) provides for an output tax adjustment on acquisition of compulsorily zero-rated goods/land:

(3J) For a supply to which section 11(1)(mb) applies, the recipient must,—

(a) on acquisition,—

(i) identify the nominal amount of tax (the **nominal GST component**) that would be chargeable on the value of the supply, as if the value were equal to the consideration charged for the supply, at the rate set out in section 8(1); and

(ii) determine the extent to which they intend to use the goods or services as described in subsection (3G); and

(iii) treat as output tax, for attribution to a taxable period under section 20(4), an amount that is the same proportion of the nominal GST component as the proportion of the use of the goods and services that is non-taxable use; and

(b) for later adjustment periods, make adjustments under the apportionment rules set out in sections 20G and 21 to 21H in relation to the taxable supply referred to in paragraph (a).

16. Section 20(4B) provides:

20 Calculation of tax payable

…

(4B) A person who is treated under section 5(23) as a supplier of goods under section 11(1)(mb) is denied a deduction under subsection (3) in relation to the supply. However, this subsection does not apply to a person required to account for tax under section 5(23) who is either a registered person or later becomes a registered person and uses the relevant goods for making taxable supplies.

17. Section 25 provides a mechanism for issuing credit and debit notes:

25 Credit and debit notes

(1) This section shall apply where, in relation to the supply of goods and services by any registered person,—

(a) that supply of goods and services has been cancelled; or

(aa) the nature of that supply of goods and services has been fundamentally varied or altered; or

(ab) section 11(1)(mb) was incorrectly applied to the treatment of the supply, so that the supply was either zero-rated when it should not have been, or not zero-rated when it should have been; or

(b) the previously agreed consideration for that supply of goods and services has been altered, whether due to the offer of a discount or otherwise; or

(c) the goods and services or part of those goods and services supplied have been returned to the supplier,—

and the supplier has—

(d) provided a tax invoice in relation to that supply and as a result of any 1 or more of the above events, the amount shown thereon as tax charged on that supply is incorrect; or

(e) furnished a return in relation to the taxable period for which output tax on that supply is attributable and, as a result of any 1 or more of the above events, has accounted for an incorrect amount of output tax on that supply.

(2) Where a supplier has accounted for an incorrect amount of output tax as specified in subsection (1)(e), that supplier shall make an adjustment in calculating the tax payable by that supplier in the return for the taxable period during which it has become apparent that the output tax is incorrect, and if—

(a) the output tax properly charged in relation to that supply exceeds the output tax actually accounted for by the supplier, the amount of that excess shall be deemed to be tax charged on a taxable supply made by that supplier and be attributable to the taxable period in which the adjustment is to be made, and not attributable to any prior taxable period:

(b) the output tax actually accounted for exceeds the output tax properly charged in relation to that supply, that supplier shall make a deduction under section 20(3) of the amount of that excess.

(3) Subject to this section, where a tax invoice has been provided as specified in subsection (1)(d), and—

(a) the amount shown as tax charged on that tax invoice exceeds the actual tax charged in respect of that supply, the supplier shall provide the recipient with a credit note, containing the following particulars:

(i) the words "credit note" in a prominent place:

(ii) the name and registration number of the registered person:

(iii) the name and address of the recipient:

(iv) the date on which the credit note was issued:

(v) either—

(A) the amount of consideration for that supply contained in the tax invoice referred to above, the correct amount of consideration for the supply, the difference between those 2 amounts, and the tax charged in respect of that supply to the extent that it relates to the amount of that difference; or

(B) where the tax charged in respect of the supply is the tax fraction of the consideration, the difference referred to above in this subparagraph and a statement that that difference includes a charge in respect of the tax:

(vi) [Repealed]

(vii) a brief explanation of the circumstances giving rise to the issuing of the credit note:

(b) the actual tax charged in respect of that supply exceeds the tax charged shown on the tax invoice, the supplier shall provide the recipient with a debit note, containing the following particulars:

(i) the words "debit note" in a prominent place:

(ii) the name and registration number of the registered person:

(iii) the name and address of the recipient:

(iv) the date on which the debit note was issued:

(v) either—

(A) the amount of consideration for that supply contained in the tax invoice referred to above, the correct amount of consideration for the supply, the difference between those 2 amounts, and the tax charged in respect of that supply to the extent that it relates to the amount of that difference; or

(B) where the tax charged in respect of the supply is the tax fraction of the consideration, the difference referred to above in this subparagraph and a statement that that difference includes a charge in respect of the tax:

(vi) [Repealed]

(vii) a brief explanation of the circumstances giving rise to the issuing of the debit note:

provided that—

(c) it shall not be lawful to issue more than 1 credit note or debit note for the amount of the excess:

(d) if any registered person claims to have lost the original credit note or debit note, the supplier or recipient, as the case may be, may provide a copy clearly marked "copy only":

(e) a supplier shall not be required to provide a recipient with a credit note pursuant to paragraph (a) in any case where and to the extent that the amount of the excess referred to in that paragraph arises as a result of the recipient taking up a prompt payment discount offered by the supplier and that the terms of the prompt payment discount offer are clearly stated on the face of the tax invoice:

(f) in the case of a supply to which subsection (1)(ab) applies, a credit note may not be issued after 7 years from the date of settlement of the transaction relating to the supply.

(3A) Where a recipient, being a registered person, creates a document containing the particulars specified in this section and purporting to be a credit note or a debit note in respect of a supply of goods and services made to the recipient by a supplier, being a registered person, that document shall be deemed to be a credit note or, as the case may be, a debit note provided by the supplier under subsection (3) where—

(a) the Commissioner has granted prior approval for the issue of such documents by a recipient or class or classes of recipients in relation to the supplies or class or classes of supplies to which the documents relate; and

(b) the supplier and the recipient agree that the supplier shall not issue a credit note or, as the case may be, a debit note in respect of any supply to which this subsection applies; and

(c) a copy of any such document is provided to the supplier and another copy is retained by the recipient:

provided that—

(d) where a credit note is issued pursuant to this subsection, any credit note issued by the supplier in respect of that supply shall be deemed not to be a credit note for the purposes of this Act:

(e) where a debit note is issued pursuant to this subsection, any debit note issued by the supplier in respect of that supply shall be deemed not to be a debit note for the purposes of this Act.

(3B) Where the Commissioner is satisfied that there are or will be sufficient records available to establish the particulars of any supply or class of supplies, and that it would be impractical to require that a credit note or a debit note be issued pursuant to this section, the Commissioner may determine that, subject to any conditions that the Commissioner may consider necessary,—

(a) any 1 or more of the particulars specified in paragraph (a) or, as the case may be, paragraph (b) of subsection (3) shall not be contained in a credit note or, as the case may be, a debit note; or

(b) a credit note or, as the case may be, a debit note is not required to be issued.

(3C) Notwithstanding anything in subsection (3) where, in relation to any taxable supplies, or a class or classes of taxable supplies, made by a supplier to a recipient, or a class or classes of recipients,—

(a) the supplier has provided, in terms of section 24, 1 or more tax invoices to a recipient in respect of those taxable supplies; and

(b) the Commissioner is satisfied that there are or will be sufficient records available to establish the particulars of those taxable supplies to a recipient,—

(c) the Commissioner may determine in respect of any recipient, or class or classes of recipients, that, subject to any conditions that the Commissioner may consider necessary, the supplier may issue 1 credit note or debit note to each recipient with respect to those tax invoices.

(4) Where any recipient, being a registered person, has been issued with a credit note pursuant to subsection (3)(a), or has been notified, or otherwise knows that any tax invoice which that registered person holds is incorrect as a result of any 1 or more of the events specified in any of paragraphs (a), (aa), (ab), (b), and (c) of subsection (1), and has made a deduction of any amount of input tax in any taxable period in respect of that supply of goods and services to which the credit note or that notice or other knowledge, as the case may be, relates, the amount of the excess referred to in subsection (3)(a) shall be deemed to be tax charged in relation to a taxable supply made by the recipient attributable to the taxable period in which the credit note was issued, or that notice or, as the case may be, other knowledge was received, to the extent that the input tax deducted exceeds the output tax properly charged.

(5) Where any recipient, being a registered person, has been issued with a debit note pursuant to subsection (3)(b), and has made a deduction of any amount of input tax in any taxable period in respect of that supply of goods and services to which that debit note relates, the recipient shall make a deduction under section 20(3) of the amount of the excess referred to in subsection (3)(b) in the taxable period in which the debit note is issued, to the extent that the output tax properly charged exceeds the input tax deducted.

(6) Where any amount of tax charged is required to be shown on any credit note or debit note, and that amount consists of any number of dollars and cents together with any fraction or part of a cent, that fraction or part of that cent,—

(a) if less than or equal to half of that cent, may be disregarded for the purposes of this section:

(b) if in excess of half of that cent, shall be deemed for the purposes of this section to be an amount equal to 1 cent.

18. Section 51B(4) to (6) provides:

(4) For the purposes of this Act, in relation to a supply to which section 11(1)(mb) applies, a recipient who is treated as a supplier under section 5(23)—

(a) is treated as registered from the date of the supply under section 5(23); and

(b) must apply under section 51(2) to the Commissioner for registration.

(5) A person who is treated as registered under subsection (4)(b) may ask the Commissioner to cancel their registration under section 52(2) once they have accounted for output tax as required under section 5(23).

(6) For the purposes of subsection (5), section 5(3) does not apply if—

(a) the person seeks cancellation of their registration by the end of the taxable period in which they have accounted for the output tax under section 5(23); or

(b) the Commissioner so determines, on application by the person.

19. Section 60B(1) and (6) provides:

(1) This section applies when a person (**person A**) enters into a contract to supply goods and services to another person (**person B**), and person B directs person A to provide the goods and services to a nominated person (**person C**) who is not party to the contract.

…

(6) Despite subsections (2) to (4), for a supply that wholly or partly consists of land, the supply is treated as made by person A to person C.

20. Section 75(3B) to (3E) provides:

(3B) For the purposes of section 11(1)(mb), the supplier must maintain sufficient records to enable the following particulars in relation to the supply to be ascertained:

(a) the name and address of the recipient; and

(b) the registration number of the recipient; and

(c) a description of the land; and

(d) the consideration for the supply.

(3C) Subsections (3D) and (3E) apply when a supply that wholly or partly consists of land is made to a person who is, for the purposes of the supply, an agent acting on behalf of an undisclosed principal.

(3D) The requirements of subsection (3B)(a) and (b) are met if the supplier maintains sufficient records to enable the particulars of the [[name, and address, and registration number or tax file number, as applicable]] of the agent to be ascertained.

(3E) The agent must maintain sufficient records in relation to the undisclosed principal to enable the name, address, and, if the principal is a registered person or expects to be a registered person, the registration number of the principal to be ascertained.

21. Section 78F provides:

78F Liability in relation to supplies of land

(1) This section applies in relation to a supply that wholly or partly consists of land.

(2) At or before settlement of the transaction relating to the supply, the recipient is required to notify the supplier as to whether, at the date of settlement,—

(a) they are, or expect to be, a registered person; and

(b) they are acquiring the goods with the intention of using them for making taxable supplies; and

(c) they do not intend to use the land as a principal place of residence for them or a person associated with them under section 2A(1)(c).

(2B) For the purposes of subsection (2)(a), a recipient who is a registered person, or who expects to be a registered person, must provide their registration number to the supplier at or before the date of settlement.

(3) The supplier may rely on the information provided as required by subsection (2) in determining the tax treatment of the supply.

(4) For the purposes of section 5(2), the notice referred to in subsection (2) must be provided to the second person referred to in section 5(2).

(5) For the purposes of section 60B and a contract for a supply that wholly or partly consists of land, when the person who enters the contract (**person B**) nominates another person (**person C**) to receive the supply, the requirements of subsection (2) are met if—

(a) person B provides the required information as it relates to their expectation of the circumstances of person C:

(b) person C provides the required information.

(6) When a supply is made to a person who is, for the purposes of the supply, an agent acting on behalf of an undisclosed principal, the requirements of subsection (2) are met if the agent notifies to the supplier as to whether, at the date of settlement, the principal as recipient—

(a) is, or expects to be, a registered person; and

(b) is acquiring the goods or services with the intention of using them for making taxable supplies; and

(c) does not intend to use the land as a principal place of residence for them or a person associated with them under section 2A(1)(c).

(7) When a supply is made to a person who is, for the purposes of the supply, an agent acting on behalf of an undisclosed principal, the agent must provide their registration number to the supplier at or before the date of settlement. If the agent does not have a registration number, their tax file number may be provided in its place. On meeting the requirements of this subsection, the person is treated as having met the requirements of subsection (2B).

Tax Administration Act 1994

22. Section 14C provides:

14C Applying or notifying

(1) This section applies when a provision in this Act, the Income Tax Act 2007, or the Goods and Services Tax Act 1985 refers to or describes person A—

(a) applying to person B for something:

(b) notifying person B about something.

(2) Person A may communicate—

(a) by electronic means, if person A complies with the provisions of the Electronic Transactions Act 2002, for an item of information delivered in a way referred to in section 14F; or

(b) in print and delivered in a way referred to in section 14F, whether the document is handwritten, typewritten, or otherwise visibly represented, and whether copied or reproduced on paper; or

(c) in another manner permitted by the Commissioner.

(3) However, communication under this section does not include communication on the internet or by other electronic means, if person B is not directly alerted to the communication in some manner.

(4) Section 14E may apply to override the application of this section.

LEGISLATION AND DETERMINATIONS

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

Special Determination S55: Valuation of Shares Issued by Bank on Conversion

This determination may be cited as Special Determination S55: Valuation of Shares Issued by Bank on Conversion.

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

1.1 This determination relates to a funding transaction involving the issue of Notes by Bank to Parent. The Notes will contain a conversion mechanism, in order to allow them to be recognised as Additional Tier 1 capital for the purposes of the Reserve Bank of New Zealand framework relating to the capital adequacy of banks.

1.2 Bank will enter into an agreement, which will set out the steps that will occur if a Conversion of the Notes occurs. A Conversion may be an optional conversion (at the election of Bank following certain specified events) or an automatic conversion (upon a Capital Trigger Event, a Non-Viability Trigger Event or on certain other events relating to a change in control of Bank).

1.3 If Conversion occurs, the relevant number of Notes must be immediately and irrevocably converted into ordinary shares in Bank.

1.4 The Arrangement is the subject of, and fully described in, the Ruling.

2. Reference

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

3. Scope of determination

3.1 This determination applies to a funding transaction involving the issue of Notes by Bank to Parent. Bank will enter into an agreement, which will set out the steps that will occur on Conversion of the Notes.

3.2 If a Conversion occurs, the relevant number of Notes must be immediately and irrevocably converted into shares in the Bank. In summary, the steps for the conversion of the Notes will be as follows:

(a) Each Note (subject to Conversion) will become immediately due and payable and Bank will be required to repay the face value of the Note.

(b) Under the terms of the Notes, Parent will be required to pay a sum to Bank equal to the face value of each Note converted, to subscribe for ordinary shares in Bank.

(c) The number of ordinary shares in Bank to be subscribed for will be calculated in accordance with a formula set out in the terms of the Notes.

3.3 This determination applies where shares are issued by Bank to Parent on a Conversion of the Notes, to determine the value of the shares for the purposes of the financial arrangements rules.

4. Principle

4.1 The share subscriptions and the Notes are, together, a financial arrangement (as defined in s EW 3). That financial arrangement does not include an excepted financial arrangement (as defined in s EW 5).

4.2 The subscription for shares in Bank by Parent contained in the terms for the Notes is an "agreement for the sale and purchase of property and services" (as defined in s YA 1), as it is a conditional agreement to acquire property. The share subscriptions are not a "short-term agreement for sale and purchase" (as defined in s YA 1), as settlement is not required to occur within 93 days of the terms for the Notes being entered into. As such, they are not excepted financial arrangements under s EW 5.

4.3 For the purposes of determining the consideration paid or payable under the financial arrangements rules, the value of the shares issued by Bank must be established under s EW 32. None of subs (2B) to (5) of s EW 32 apply to the share subscriptions.

4.4 Under s EW 32(6), the Commissioner is required to determine the value of the property. Bank and Parent are both required to use this amount.

5. Interpretation

In this determination, unless the context otherwise requires:

- All legislative references in this determination are to the Income Tax Act 2007, unless otherwise stated.
- **Bank** means the bank issuing the Notes.
- **Parent** means the parent company of Bank.
- **Conversion** has the meaning set out in the terms of the Notes, as described in the Ruling.
- **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.
- **Notes** means the Notes issued to Parent as described in the Ruling.
- **Ruling** mean private ruling BR Prv 17/39, issued on 8 September 2017.

6. Method

For the purposes of s EW 32(6), the value of the shares issued by Bank is equal to the amount paid for those shares by Parent.

7. Example

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

Bank issues Notes having a face value of NZ$1,000. On Conversion, Notes with a face value of NZ$1,000 are to be converted to ordinary shares in Bank. Bank immediately repays the face value of the Notes to Parent.

Parent pays an amount equal to the face value of the Notes to Bank to subscribe for ordinary shares in Bank. Bank issues the number of shares to Parent calculated in accordance with the formula set out in the terms for the Notes. The value of the shares, for the purposes of s EW 32, is the NZ$1,000.

This Determination is signed by me on the 8th day of September 2017.

Fiona Heiford
Manager, Taxpayer Rulings

General Determination DEP102: Depreciation rate for potato cool stores (climate controlled) structure only, excluding climate control plant

Note to Determination DEP102

The Commissioner has recently been asked to consider what depreciation rate should apply for potato cool stores.

Potato cool stores are specialist buildings that control humidity and temperature so that potatoes can be stored for long periods without spoilage occurring. These cool stores are fitted with refrigeration reticulation machinery, air transfer systems and associated electronic componentry (climate control plant).

In appearance, potato cool stores are dome-shaped tunnels. They are usually constructed of zinc coated galvanised steel (corrugated iron). The Commissioner accepts that these specialised buildings are exposed to a humid, corrosive environment that impacts the life of the building's construction material.

For this reason the Commissioner is satisfied that the estimated useful life (EUL) of these specialised buildings is 33.3 years and has set a provisional depreciation rate for these assets accordingly.

It should be noted that it is the Commissioner's view that the climate control plant is not attached to the potato cool store building; it can be easily removed without damaging either the plant or the building. This being so, the various items of climate control plant are separate items of depreciable property and (where appropriate) may be able to be separately depreciated. Further information, regarding whether items of depreciable property form part of a building, may be found in Interpretation Statement *IS 10/01 Residential Rental Properties – Depreciation of Items of Depreciable Property*[1].

General Determination DEP102: tax depreciation rates
General Determination Number DEP102

This determination may be cited as "Determination DEP102 Tax Depreciation Rates General Determination Number DEP102: Potato cool stores (climate controlled) structure only, excluding climate control plant".

1. Application

This determination applies to taxpayers who own items of depreciable property of the kind listed in the tables below:

This determination applies for the 2017/18 and subsequent income years.

2. Determination

Pursuant to section 91AAF of the Tax Administration Act 1994 I set in this determination the rate to apply to the kind of items of depreciable property listed in the table below by:

- Adding into the "Buildings and Structures" asset category, the new asset class, estimated useful life, and general diminishing value and straight-line depreciation rates listed below:

Asset class	Estimated useful life (years)	DV rate (%)	SL rate (%)
Potato cool stores (climate controlled) structure only, excluding climate control plant	33.3	4.5	3

3. Interpretation

In this determination, unless the context otherwise requires, words and terms have the same meaning as in the Income Tax Act 2007 and the Tax Administration Act 1994.

This determination is signed by me on the 27th day of September 2017.

Rob Wells
LTS Manager, Technical Standards

[1] Further information on this statement may be found at www.govt.nz (search term "10/01")

Foreign currency amounts – conversion to New Zealand dollars (for the six months ending 30 September 2017)

This article provides the exchange rates acceptable to Inland Revenue for converting foreign currency amounts to New Zealand dollars under the controlled foreign company ("CFC") and foreign investment fund ("FIF") rules for the six months ending 30 September 2017.

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

- actual rate for the day for each transaction (including close of trading spot exchange rate on the day), or
- rolling 12-month average rate for a 12-month accounting period or income year (see the table **Currency rates 6 months ending 30 September 2017 – rolling 12-month average**), or
- mid-month actual rate as the basis of the rolling average for accounting periods or income years greater or lesser than 12 months (see the table **Currency rates 6 months ending 30 September 2017 – mid-month actual**).

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

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

You must apply the chosen conversion method to all interests for which you use the FIF or CFC calculation method in that and each later income year.

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

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

Note: All section references relate to the 2007 Act.

Actual rate for the day for each transaction

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

- where the 2007 Act does not provide a specific currency conversion rule, then foreign currency amounts can be converted by applying the close of trading spot exchange rate on the date the transaction is required to be measured or calculated (section YF 1(2))
- where a person chooses to use the actual rate for the day of the transaction when calculating their FIF income or loss by applying the comparative value method, fair dividend rate method, deemed rate of return method or the cost method (section EX 57(2)(a))
- where a person chooses to use the close of trading spot exchange rate to convert foreign income tax paid by a CFC (section LK 3(a)) or by a FIF where the attributable FIF income method is used (sections EX 50(8)–(9) and LK 3(a)).

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

The table **Currency rates 6 months ending 30 September 2017 – month end** provides exchange rates for the last day of the month. These are provided for convenience to assist taxpayers who may need exchange rates on those days.

Currency rates 6 months ending 30 September 2017 – rolling 12-month average table

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

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

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

Currency rates 6 months ending 30 September 2017 – mid-month actual table

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

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

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

Example 1

A taxpayer with a 30 September balance date purchases shares in a Philippine company (which is a FIF but does produce a guaranteed yield) on 7 September 2017. Its opening market value on 1 October 2017 or its closing market value on 30 September 2017 is PHP 350,000. Using the comparative value method and applying the actual rate for the day (section EX 57(2)(a)), the opening market value is converted as follows:

PHP 350,000 ÷ 36.6797 = $9,542.06

(In this example, the rate selected is the month-end rate for September 2017 for PHP. Refer to the table "Currency rates 6 months ending 30 September 2017 – month end".)

Example 2

A CFC resident in Hong Kong has an accounting period ending on 30 June 2017. Attributed CFC income for the period 1 July 2016 to 30 June 2017 is 200,000 Hong Kong dollars (HKD), which converts to:

HKD 200,000 ÷ 5.524 = $36,205.65

(In this example, the rate selected is the rolling 12-month average rate for June 2017 for HKD. Refer to the table "Currency rates 6 months ending 30 September 2017 – rolling 12-month average".)

Example 3

A resident individual with a 30 September 2017 accounting period acquired a FIF interest in a Japanese company on 1 October 2016 for 10,500,000 yen. The interest is sold in September 2017 for 10,000,000 yen. Using the comparative value method and applying section EX 57(2)(b), these amounts are converted as:

JPY 10,500,000 ÷ 79.6986 = $131,746.35

JPY 10,000,000 ÷ 79.6986 = $125,472.72

(In this example, the rolling 12-month rate for September 2017 for JPY has been applied to both calculations. Refer to the table "Currency rates 6 months ending 30 September 2017 – rolling 12-month average".)

Example 4

A CFC resident in Singapore was formed on 20 April 2017 and has a balance date of 30 September 2017. During the period 1 May 2017 to 30 September 2017, attributed CFC income of 500,000 Singaporean dollars was derived. For the conversion to New Zealand dollars the taxpayer chooses the method set out in section EX 21(4)(b).

1. Calculating the average monthly exchange rate for the complete months May–September 2017:

   0.9621 + 0.9974 + 1.0074 + 0.9893 + 0.9812 = 4.9374

   4.9374 ÷ 5 = 0.98748

2. Round exchange rate to four decimal places: 0.9875

3. Conversion to New Zealand currency:

   SGD 500,000 ÷ 0.9875 = $506,329.11

(In this example, the rates are from the table "Currency rates 6 months ending 30 September 2017 – mid-month actual", from May to September 2017 inclusive for SGD.)

Currency rates 6 months ending 30 September 2017 – rolling 12-month average

Currency	Code	15/04/17	15/05/17	15/06/17	15/07/17	15/08/17	15/09/17
Australia Dollar	AUD	0.9405	0.9403	0.9404	0.9403	0.9391	0.934
Bahrain Dinar	BHD	0.2673	0.2676	0.2682	0.2689	0.269	0.2689
Britain Pound	GBP	0.5528	0.558	0.5638	0.5656	0.5658	0.5645
Canada Dollar	CAD	0.9313	0.9365	0.9405	0.941	0.9403	0.9342
China Yuan	CNY	4.7934	4.8195	4.8425	4.8593	4.8631	4.8539
Denmark Kroner	DKK	4.844	4.8617	4.8754	4.8725	4.855	4.8298
Euporean Community Euro	EUR	0.6512	0.6536	0.6555	0.6551	0.6528	0.6494
Fiji Dollar	FJD	1.4675	1.4704	1.4724	1.4761	1.4762	1.4743
French Polynesia Franc	XPF	77.6914	77.972	78.1873	78.1644	77.8866	77.4882
Hong Kong Dollar	HKD	5.5017	5.5105	5.524	5.5421	5.5479	5.5501
India Rupee	INR	47.3746	47.277	47.2123	47.1287	47.0019	46.8226
Indonesia Rupiah	IDR	9,391.29	9,399.39	9,417.71	9,446.43	9,471.74	9,477.75
Japan Yen	JPY	77.0656	77.4703	77.9207	78.5923	79.182	79.6986
Korea Won	KOR	813.2473	811.0438	810.4484	812.0254	814.5903	814.9008
Kuwait Dinar	KWD	0.2152	0.2156	0.2162	0.2168	0.2169	0.2169
Malaysia Ringit	MYR	3.0113	3.0313	3.0482	3.0736	3.0937	3.0967
Norway Krone	NOK	5.9479	5.9754	5.9995	5.9976	5.9842	5.9594
Pakistan Rupee	PKR	74.2825	74.3675	74.5532	74.7943	74.8425	74.8914
Phillipines Peso	PHP	34.3028	34.5127	34.7947	35.0783	35.4072	35.6224
PNG Kina	PGK	2.2484	2.2523	2.2579	2.2649	2.2658	2.2668
Singapore Dollar	SGD	0.9849	0.9876	0.9915	0.9955	0.9972	0.9959
Solomon Islands Dollar*	SBD	0.0907	0.0907	0.091	0.0912	0.0912	0.0913
South Africa Rand	ZAR	9.9113	9.7985	9.6784	9.6113	9.615	9.5481
Sri Lanka Rupee	LKR	105.1407	105.6618	106.316	106.9987	107.486	107.88
Sweden Krona	SEK	6.2192	6.2602	6.2986	6.2981	6.2767	6.2438
Swiss Franc	CHF	0.7033	0.7055	0.7077	0.7084	0.7086	0.7077
Taiwan Dollar	TAI	22.3705	22.2494	22.172	22.1301	22.0754	21.9763
Thailand Baht	THB	24.9035	24.8869	24.8604	24.8526	24.7814	24.6669
Tonga Pa'anga*	TOP	1.5527	1.5568	1.5616	1.5668	1.564	1.5622
United States Dollar	USD	0.709	0.7098	0.7113	0.7132	0.7134	0.7133
Vanuatu Vatu	VUV	77.0382	77.2266	77.2763	77.4798	77.4798	77.2795
West Samoan Tala*	WST	1.7822	1.7841	1.7843	1.789	1.7818	1.7786

Notes to table:

1. *All currencies are expressed in NZD terms, ie, 1NZD per unit(s) of foreign currency.*
2. *The currencies marked with an asterisk * are not published on Bloomberg in NZD terms. However, these currencies are expressed in USD terms and therefore the equivalent NZD terms have been generated as a function of the foreign currency USD cross-rate converted to NZD terms at the NZDUSD rate provided.*
3. *The rates provided represent the Bloomberg generic rate (BGN) based on the last price (mid rate) at which the currency was traded at the close of the New York trading day. Where the date specified was not a trading day, then the rate reflects the last price on the preceding business day.*

Source: Bloomberg CMPN BGN

Currency rates 6 months ending 30 September 2017 – mid-month actual

Currency	Code	15/04/17	15/05/17	15/06/17	15/07/17	15/08/17	15/09/17
Australia Dollar	AUD	0.9231	0.9284	0.9511	0.9384	0.9252	0.9115
Bahrain Dinar	BHD	0.2639	0.2595	0.2719	0.2771	0.2729	0.2751
Britain Pound	GBP	0.5589	0.5337	0.5652	0.5608	0.5623	0.5368
Canada Dollar	CAD	0.9322	0.9382	0.9563	0.9289	0.9231	0.8897
China Yuan	CNY	4.8165	4.736	4.9038	4.9663	4.8316	4.7716
Denmark Kroner	DKK	4.9043	4.6645	4.8096	4.7638	4.5852	4.5439
Euporean Community Euro	EUR	0.6595	0.6271	0.6469	0.6406	0.6166	0.6106
Fiji Dollar	FJD	1.4512	1.4535	1.4865	1.5044	1.476	1.4775
French Polynesia Franc	XPF	78.6816	74.7829	77.1679	76.4226	73.5517	72.8358
Hong Kong Dollar	HKD	5.4459	5.3593	5.6205	5.7335	5.6605	5.7031
India Rupee	INR	45.1176	44.2484	46.4928	47.078	46.674	46.6179
Indonesia Rupiah	IDR	9280.77	9162.51	9604.05	9759.28	9739.27	9626.41
Japan Yen	JPY	76.005	78.307	79.964	82.674	80.079	80.88
Korea Won	KOR	795.4585	769.9819	815.2848	829.9303	822.2786	826.4691
Kuwait Dinar	KWD	0.2134	0.2095	0.2189	0.2225	0.2185	0.2198
Malaysia Ringit	MYR	3.0808	2.9831	3.0826	3.1415	3.1319	3.0472
Norway Krone	NOK	6.008	5.8855	6.1328	6.0134	5.7601	5.7249
Pakistan Rupee	PKR	73.5294	71.9424	75.7576	77.5194	76.3359	76.9231
Phillipines Peso	PHP	34.6469	34.2185	35.9449	37.0087	37.4736	37.2607
PNG Kina	PGK	2.2279	2.1895	2.2941	2.3371	2.2967	2.3314
Singapore Dollar	SGD	0.9783	0.9621	0.9974	1.0074	0.9893	0.9812
Solomon Islands Dollar*	SBD	0.0898	0.0874	0.0925	0.0939	0.0927	0.0939
South Africa Rand	ZAR	9.3965	9.0731	9.2839	9.5633	9.6337	9.6107
Sri Lanka Rupee	LKR	106.383	105.2632	109.8901	112.3596	111.1111	111.1111
Sweden Krona	SEK	6.3343	6.076	6.3066	6.105	5.8408	5.8093
Swiss Franc	CHF	0.7037	0.6858	0.703	0.7077	0.7037	0.7004
Taiwan Dollar	TAI	21.2701	20.6789	21.8227	22.2499	21.9264	21.9549
Thailand Baht	THB	24.048	23.7758	24.4778	24.8	24.0942	24.1466
Tonga Pa'anga*	TOP	1.5497	1.5505	1.5808	1.6066	1.5344	1.564
United States Dollar	USD	0.6998	0.6881	0.7208	0.7347	0.7236	0.7299
Vanuatu Vatu	VUV	76.9231	76.3359	77.5194	79.3651	76.9231	76.3359
West Samoan Tala*	WST	1.7266	1.7659	1.8056	1.8396	1.74	1.8143

Notes to table:

1. *All currencies are expressed in NZD terms, ie, 1NZD per unit(s) of foreign currency.*
2. *The currencies marked with an asterisk * are not published on Bloomberg in NZD terms. However, these currencies are expressed in USD terms and therefore the equivalent NZD terms have been generated as a function of the foreign currency USD cross-rate converted to NZD terms at the NZDUSD rate provided.*
3. *The rates provided represent the Bloomberg generic rate (BGN) based on the last price (mid rate) at which the currency was traded at the close of the New York trading day. Where the date specified was not a trading day, then the rate reflects the last price on the preceding business day.*

Source: Bloomberg CMPN BGN

Currency rates 6 months ending 30 September 2017 – month end

Currency	Code	30/04/17	31/05/17	30/06/17	31/07/17	31/08/17	30/09/17
Australia Dollar	AUD	0.9171	0.9536	0.9548	0.9388	0.9032	0.9202
Bahrain Dinar	BHD	0.2588	0.2672	0.2767	0.2834	0.2706	0.272
Britain Pound	GBP	0.5302	0.5496	0.5631	0.5686	0.5551	0.5381
Canada Dollar	CAD	0.9377	0.9564	0.9503	0.9377	0.896	0.8989
China Yuan	CNY	4.7294	4.8312	4.9722	5.0509	4.734	4.7837
Denmark Kroner	DKK	4.6876	4.6873	4.7715	4.7185	4.4818	4.5413
Euporean Community Euro	EUR	0.6301	0.63	0.642	0.6346	0.6027	0.6103
Fiji Dollar	FJD	1.4284	1.4663	1.5081	1.5115	1.4603	1.4702
French Polynesia Franc	XPF	75.213	75.248	76.6512	75.7532	71.9419	72.8247
Hong Kong Dollar	HKD	5.3418	5.5198	5.7265	5.8682	5.6166	5.6321
India Rupee	INR	44.16	45.842	47.417	48.0847	45.6256	47.1454
Indonesia Rupiah	IDR	9154.08	9455.79	9785.19	9984.71	9553.47	9715.85
Japan Yen	JPY	76.54	78.48	82.377	82.824	78.94	81.119
Korea Won	KOR	781.5113	793.1562	840.3612	841.0128	807.3655	825.5441
Kuwait Dinar	KWD	0.2093	0.2149	0.2226	0.2268	0.2165	0.2178
Malaysia Ringit	MYR	2.9809	3.0376	3.1479	3.2058	3.0595	3.045
Norway Krone	NOK	5.8882	5.9759	6.1215	5.9089	5.5724	5.7421
Pakistan Rupee	PKR	71.9424	74.0741	76.9231	79.3651	75.7576	75.7576
Phillipines Peso	PHP	34.4078	35.3607	37.003	37.8207	36.6633	36.6797
PNG Kina	PGK	2.1796	2.2538	2.3341	2.3907	2.2912	2.3037
Singapore Dollar	SGD	0.9595	0.9797	1.0088	1.0181	0.9731	0.9788
Solomon Islands Dollar*	SBD	5.3595	5.5304	5.724	5.8425	5.5378	5.6069
South Africa Rand	ZAR	9.181	9.2729	9.6014	9.9037	9.3358	9.7762
Sri Lanka Rupee	LKR	104.1667	108.6957	112.3596	114.9425	109.8901	109.8901
Sweden Krona	SEK	6.0802	6.1542	6.1822	6.0627	5.699	5.8735
Swiss Franc	CHF	0.6832	0.6855	0.7023	0.7264	0.6883	0.698
Taiwan Dollar	TAI	20.7448	21.3415	22.3039	22.7026	21.6731	21.8715
Thailand Baht	THB	23.7503	24.1159	24.804	25.0185	23.8145	24.021
Tonga Pa'anga*	TOP	1.5354	1.5704	1.5914	1.6049	1.5489	1.5504
United States Dollar	USD	0.6866	0.7085	0.7333	0.7512	0.7178	0.7209
Vanuatu Vatu	VUV	75.188	77.5194	78.7402	78.7402	75.7576	75.7576
West Samoan Tala*	WST	1.7518	1.7928	1.8342	1.8505	1.7575	1.7942

Notes to table:

1. *All currencies are expressed in NZD terms, ie, 1NZD per unit(s) of foreign currency.*
2. *The currencies marked with an asterisk * are not published on Bloomberg in NZD terms. However, these currencies are expressed in USD terms and therefore the equivalent NZD terms have been generated as a function of the foreign currency USD cross-rate converted to NZD terms at the NZDUSD rate provided.*
3. *The rates provided represent the Bloomberg generic rate (BGN) based on the last price (mid rate) at which the currency was traded at the close of the New York trading day. Where the date specified was not a trading day, then the rate reflects the last price on the preceding business day.*

Source: Bloomberg CMPN BGN

Determination CFC 2017/01: Non-attributing active insurance CFC status (TOWER Insurance Limited)

Reference

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

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

Explanation (which does not form part of the determination)

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

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

Section 91AAQ(1)(a) of the Tax Administration Act 1994 allows a person to apply to the Commissioner for such a determination in respect of a CFC, if the CFC satisfies subsection (2). TOWER Insurance Limited has made application in respect of the CFC set out below.

It has been determined, having regard to the matters set out in subsections (4) and (5) of section 91AAQ of the Tax Administration Act 1994, that the CFC satisfies the requirements set out in section 91AAQ(2) of the Tax Administration Act 1994 and is accordingly a non-attributing active CFC for the purposes of section EX 21B of the Income Tax Act 2007.

Scope of determination

The CFC to which this determination applies is:

Name	**Jurisdiction**
TOWER Insurance (Cook Islands) Limited	Cook Islands

Interpretation

In this document, unless the context otherwise requires -

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

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

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

Determination

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

Application date

This determination applies for the 2017-18 and 2018-19 income years.

This determination is signed by me this 6th day of October 2017.

Sharyn Rea
Investigations Manager

Determination CFC 2017/02: Non-attributing active insurance CFC status (TOWER Insurance Limited)

Reference

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

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

Explanation (which does not form part of the determination)

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

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

Section 91AAQ(1)(b) of the Tax Administration Act 1994 allows a person to apply to the Commissioner for such a determination in respect of a CFC, if the CFC satisfies subsection (2). TOWER Insurance Limited has made application in respect of the CFC set out below.

It has been determined, having regard to the matters set out in subsections (4) and (5) of section 91AAQ of the Tax Administration Act 1994, that the CFC satisfies the requirements set out in section 91AAQ(2) of the Tax Administration Act 1994 and is accordingly a non-attributing active CFC for the purposes of section EX 21B of the Income Tax Act 2007.

Scope of determination

The CFCs to which this determination applies are:

Name	**Jurisdiction**
TOWER Insurance (PNG) Limited	Papua New Guinea

Interpretation

In this document, unless the context otherwise requires -

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

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

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

Determination

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

Application date

This determination applies for the 2017-18 and 2018-19 income years.

This determination is signed by me this 6th day of October 2017.

Sharyn Rea
Investigations Manager

Determination CFC 2017/03: Non-attributing active insurance CFC status (TOWER Insurance Limited)

Reference

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

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

Explanation (which does not form part of the determination)

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

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

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

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

Scope of determination

The CFCs to which this determination applies are:

Name	Jurisdiction
National Insurance Company (Holdings) Limited	Fiji
TOWER Insurance (Fiji) Limited	Fiji
Southern Pacific Insurance Company (Fiji) Limited	Fiji

Interpretation

In this document, unless the context otherwise requires -

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

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

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

Determination

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

Application date

This determination applies for the 2017-18 and 2018-19 income years.

This determination is signed by me this 6th day of October 2017.

Sharyn Rea
Investigations Manager

Determination CFC 2017/04: Non-attributing active insurance CFC status (TOWER Insurance Limited)

Reference

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

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

Explanation (which does not form part of the determination)

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

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

Section 91AAQ(1)(b) of the Tax Administration Act 1994 allows a person to apply to the Commissioner for such a determination in respect of a CFC, if the CFC satisfies subsection (2). TOWER Insurance Limited has made application in respect of the CFC set out below.

It has been determined, having regard to the matters set out in subsections (4) and (5) of section 91AAQ of the Tax Administration Act 1994, that the CFC satisfies the requirements set out in section 91AAQ(2) of the Tax Administration Act 1994 and is accordingly a non-attributing active CFC for the purposes of section EX 21B of the Income Tax Act 2007.

Scope of determination

The CFCs to which this determination applies are:

Name	Jurisdiction
National Pacific Insurance (Tonga) Limited	Tonga

Interpretation

In this document, unless the context otherwise requires -

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

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

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

Determination

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

Application date

This determination applies for the 2017-18 and 2018-19 income years.

This determination is signed by me this 6th day of October 2017.

Sharyn Rea
Investigations Manager

The accounting income method (AIM) for paying provisional tax

As part of legislation enacted on 21 February 2017, the Taxation (Business Tax, Exchange of Information, and Remedial Matters) Act 2017, a new method for calculating provisional tax was introduced – the accounting income method (AIM).

The new method for calculating provisional tax will be available alongside existing methods – the standard uplift, the estimate method and the GST ratio method. AIM is not replacing these methods.

A growing number of small businesses use accounting software. Businesses wanting to calculate their provisional tax obligation using AIM will use upgraded software (an AIM-capable accounting system) which will calculate provisional tax based on current year accounting income information. The summary of determinations provides detail for software developers and the minimum tax adjustments required for AIM-capable systems.

The new rules introducing the AIM method of calculating provisional tax have application to the 2018–19 and later income years.

Overview

AIM is designed to fit better within the existing and ordinary processes of a business and is more reflective of the current year to date financial performance of a business.

Under AIM, provisional tax is integrated into business processes and payment amounts are based on current year tax adjusted income. This should provide businesses using AIM with more certainty that they are paying the right amount of tax as it will be paid as income is earned.

AIM is available to taxpayers who:

- have annual gross income of under $5 million (although there is the ability for some exceptions to this rule);
- use an AIM-capable software system;
- have not been liable in one of the last four years for a shortfall penalty in relation to their use of AIM;
- have not returned tax liabilities using the AIM method with the sole purpose or effect of consistently, year-on-year, reducing their tax liabilities below reasonably accurate amounts;
- are not a member of a class of taxpayers excluded from using AIM; and
- for the current year, have not failed more than twice to give the Commissioner information required under the AIM method.

New payment dates for paying provisional tax under the AIM method have been created.

Overpaid amounts of provisional tax paid through AIM can be refunded upon request of the taxpayer before year-end.

AIM taxpayers will provide Inland Revenue with a Statement of Activity on or before each instalment date.

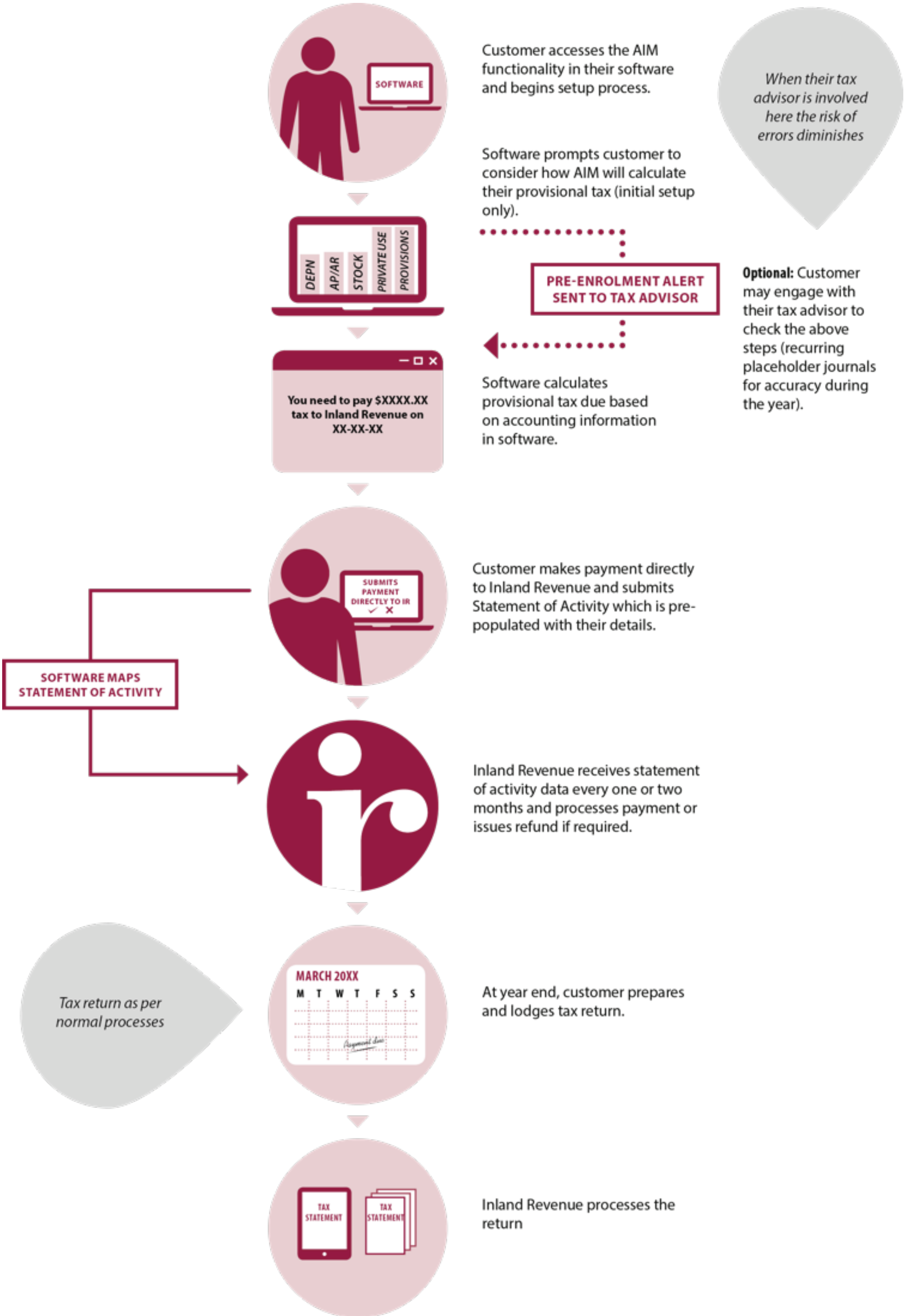
When an AIM taxpayer makes the provisional tax payments calculated by their AIM-capable software they will not have use-of-money interest exposure should the year end residual income tax result in a different tax liability.

AIM provisional tax payments cannot be made through a tax pool, however, tax pooling can be used for terminal tax and reassessment liabilities.

Overpaid provisional tax in an AIM taxpaying company may be transferred to the AIM company shareholders to meet their provisional tax liabilities on the dates that their provisional tax is due.

The Commissioner may approve taxpayers who have gross income over the $5 million threshold to use, or continue to use, AIM where the Commissioner is satisfied there is minimal risk that approval will result in less net revenue collected, this is referred to as large business AIM capable software.

The following graphic illustrates how AIM works in practice.



The following examples display how AIM would apply:

Example 1

Murphy has recently finished a painting apprenticeship and intends to set up his own house painting business. He has no previous business knowledge and his parent suggest he meet with their accountant to get some advice. The accountant suggests Murphy sets up a company, start using a basic accounting software package and elect into paying provisional tax using the AIM approach to help him budget in his first year of business. Murphy's company has a March balance date and will pay GST and provisional tax using the AIM approach on a two-monthly basis. Murphy does not make any profit in the first few months but starts to make a profit towards the end of the year. He will pay provisional tax under AIM as follows:

GST and provisional tax payment dates	28-Jun 2018	28-Aug 2018	28-Oct 2018	15-Jan 2019	28-Feb 2019	7-May 2019	Total prov tax	Terminal tax due
Income earned during current year	Nil	Nil	Nil	20,000	30,000	50,000		28,000
AIM payment amount	Nil	Nil	Nil	5,600	8,400	14,000	28,000	Nil

AIM will help Murphy budget for tax correctly in his first year of operation as he pays tax as he earns income.

Example 2

Sandy has just completed a qualification in graphic design and has decided to set up a business designing websites for customers. Being new to business Sandy approaches an accountant to understand what her tax obligations are and what dates tax payments need to be made.

Her accountant recommends that Sandy use an accounting software package and suggests some options.

Given Sandy is going to use accounting software to keep track of how her business is doing she thinks it makes sense to use an AIM-capable accounting system which also calculates her provisional tax liability.

Sandy's business has a March balance date and will pay GST and provisional tax using AIM on a two-monthly basis. For the first part of the year Sandy makes no profit but as the year progresses Sandy's business starts making a profit. Under AIM Sandy will pay provisional tax as follows:

GST and provisional tax payment dates	28-Jun 2018	28-Aug 2018	28-Oct 2018	15-Jan 2019	28-Feb 2019	7-May 2019	Total prov tax	Terminal tax due
Income earned during current year	Nil	Nil	3,000	7,500	12,000	18,000		6,108
AIM payment amount			315	788	1,855	3,150	6,108	0

Example 3

Benson Electrical Ltd is considering using AIM. They currently use accounting software, pay GST every two months, and have a March balance date. Their accountant talks to them about using AIM due to the unpredictable nature of the contracts they are being awarded. The inability to plan in the past has resulted in exposure to use-of-money interest. They generally have a slow start to the financial year but business picks up in the latter half. Their business is steadily growing and their residual income tax is $180,000 in 2017 and $220,000 in 2018.

They ask their accountant to show them what their provisional tax liability would look like under different methods for the 2019 year and how exposure to use-of-money interest would differ.

In this scenario, their possible use-of-money interest[1] costs range between nil and $6,880.

GST and provisional tax payment dates	**28-Jun**	**28-Aug**	**28-Oct**	**15-Jan**	**28-Feb**	**7-May**	**Total prov tax**		
Income earned during current year	108,000	Nil	178,000	250,000	178,000	143,000			
Implied tax on taxable income	30,240	Nil	49,840	70,000	49,840	40,040	239,960		
Provisional tax methods and due dates for payment	**28-Jun**	**28-Aug**	**28-Oct**	**15-Jan**	**28-Feb**	**7-May**	**Total prov tax**	**Terminal tax due**	**UOMI incurred**
AIM	**30,240**	**0**	**49,840**	**70,000**	**49,840**	**40,040**	**239,960**	**0**	**0**
Uplift 105%		77,000		77,000		77,000	231,000	8,960	737
Uplift 110%		66,000		66,000		66,000	198,000	41,960	3,449
Estimate		40,000		60,000		90,000	190,000	49,960	6,880

AIM providers approval and revocation

Software providers are required to apply under section 15U of the Tax Administration Act 1994 for approval for their AIM-capable accounting systems.

The Commissioner may approve a person as an approved AIM provider if approving the person would not negatively affect the integrity of the tax system. As part of the application process AIM providers are required to complete a statutory declaration, specifying the name of the products, declaring that the products will be regularly updated and any other information required by the Commissioner.

Providers may apply for approval for a product which will deliver AIM to businesses with gross income under $5 million a year or for use by a class of taxpayers with gross income over $5 million a year. The Commissioner will approve an application in the latter circumstance if the Commissioner decides that there is minimal risk that approval will result in less net revenue collectable from the class of taxpayers over time.

The Commissioner may revoke a person's approval as an approved AIM provider in certain circumstances:

- if anything in their statutory declaration is not true or does not continue to be true after it is made;
- if revoking the approval protects the integrity of the tax system.

Where approval is revoked it does not take effect until the next tax year to allow taxpayers using the software to complete the tax year so they are not disadvantaged.

The Commissioner must consult with the provider before revoking their approval so both parties can discuss any concerns and have the opportunity to resolve them.

Software providers may also voluntarily revoke the Commissioner's approval. A person must notify the Commissioner of their choice to revoke the Commissioner's approval under section 15W of the Tax Administration Act 1994. Where a person makes such a choice under section 15W they must notify all end-users of the person's products that will be affected by the revocation. The revocation takes effect in the following tax year.

Under section 15X of the Tax Administration Act 1994 the Commissioner may publish a notice regarding approvals or revocations.

[1] Calculation is based on UOMI rates of 8.22% and 1.02%. It also takes into account the new provisional tax rules of no use-of-money interest for residual income tax less than $60,000 (extension of safe harbour rules) and no use-of-money interest on the first two provisional tax instalments if using uplift.

AIM-capable accounting system

A software system must meet the definition of an AIM-capable accounting system in order to gain approval from the Commissioner.

The term "AIM-capable accounting system" is defined in section RC 7B(3) of the Income Tax Act 2007.

Section RC 7B(3) requires the software system to have a number of features which include the ability to:

- generate and keep comprehensive financial accounts, including accounting income and expenditure, ledger accounts, trial balances, bank account reconciliations, and journals, on an on-demand basis, in accordance with good accounting and tax practices;
- calculate tax liabilities using tax adjustments in accordance with a determination under section 91 AAX of the Tax Administration Act 1994;
- for tax adjustments not included in the determinations, ensure they work towards reasonably accurate assessments of tax liabilities;
- recalculate all financial accounts and liabilities retrospectively and produce reports as required by the Commissioner; and
- communicate electronically with Inland Revenue and provide the right level of customer support to its users.

Section RC 10B of the Income Tax Act 2007 provides that the amount calculated by the AIM-capable accounting system is the amount of provisional tax the taxpayer must pay the Commissioner on the instalment date.

AIM eligibility criteria

The eligibility criteria for using the AIM method are set out in section RC 5 of the Income Tax Act 2007.

To be eligible to use AIM a taxpayer must:

- elect to use it before their first payment date;
- use an AIM-capable accounting package (as defined in section RC 7B) that is up to date;
- have gross income below $5 million or have approval from the Commissioner as a previous user of AIM if their income is over $5 million; or
- be a member of the class of taxpayers with income over $5 million using a software package the Commissioner has approved for AIM (as large business AIM capable software).

A provisional taxpayer does not need to be GST-registered to use AIM. Where a provisional taxpayer chooses to use AIM and is not GST registered they must pay provisional tax on a two-monthly basis.

If a taxpayer misses a payment the existing interest and penalties rules apply to the underpaid amount.

Ineligible to use AIM

In certain circumstances a taxpayer may be excluded from using AIM. Section RC 5(5B) of the Income Tax Act 2007 provides that a taxpayer can be excluded from using AIM if the taxpayer:

- has been liable in 1 of the last 4 years before the current year for a shortfall penalty in relation to their use of AIM;
- has consistently and systematically used AIM to inaccurately assess its tax liabilities;
- is a member of a class of taxpayers which is excluded from using AIM in a determination issued by the Commissioner under section 91 AAY of the Tax Administration Act 1994 (see *Determination A1*);
- has failed more than twice in the current tax year to give the Commissioner information in the prescribed form (Statement of Activity).

The Statement of Activity is important because it demonstrates the robustness of the accounting system behind the amount paid as provisional tax. If this information is not provided to Inland Revenue, there would be no evidence that a comprehensive accounting system is being used by the business to calculate its accounting income results. As the Statement of Activity reports would be cumulative, if one is missed it could be supplied in the following period.

Where a taxpayer is removed from AIM under section RC 5(5C) of the Income Tax Act 2007 they are treated as using the estimation method for the whole of the current income year and may be subject to use-of-money interest.

Determinations

The determinations are an integral part of AIM as they outline the tax adjustments that may be required to accounting income to determine the amount of provisional tax payable for an instalment period. These determinations have recently been signed and are included in this *Tax Information Bulletin* to provide a complete guide to AIM.

Broadly, determinations issued by the Commissioner detail for software developers the minimum tax adjustments required within the AIM capable software to calculate provisional tax payments and the information required to be provided with AIM payments. They also act as a guide for taxpayers and their agents on the options available in calculating their payments.

The Commissioner may issue determinations in two circumstances:

- technical determinations under section 91 AAX of the Tax Administration Act 1994; and
- a determination excluding classes of taxpayers from using AIM under section 91 AAY of the Tax Administration Act 1994.

Technical determinations detail the tax adjustments required for accounting income and expenditure under the AIM method and Inland Revenue's information requirements regarding AIM.

In making technical determinations the Commissioner must have regard to three areas:

- the accuracy resulting from the tax adjustments;
- the compliance costs incurred by taxpayers in making these adjustments; and
- the resources available to the AIM software providers.

In making a determination to exclude classes of taxpayers from using AIM the Commissioner must have regard to the risk that allowing the class of taxpayers to use the AIM method will result in less net revenue collectable from that class of taxpayers over time.

Where a determination is issued under section 91 AAX or 91 AAY the Commissioner must give at least 120 days notice of the implementation date in a publication chosen by the Commissioner.

Determinations issued under either section must also be published within 30 days of the making of the determination in a publication chosen by the Commissioner.

Technical determinations

The AIM method must result in a reasonably accurate assessment of the tax liabilities for a taxpayer.

Accounting income and expenditure does not necessarily equate to net income for tax purposes. For this reason a series of tax adjustments are required to be made to accounting income and expenditure to accurately calculate the provisional tax liability.

Software providers delivering AIM will build these tax adjustments into their software systems. The minimum adjustments that may be required are outlined in the technical determinations section of this *Tax Information Bulletin*.

Adjustments not defined in the technical determinations will be designed by the software providers themselves, with the requirement they always calculate tax liabilities using tax adjustments that result in reasonably accurate assessments of tax liabilities for taxpayers. These may include accruals or estimates for other matters that would typically be adjusted for in the year-end process – for example, entertainment expenditure is not required to be adjusted for but developers may want to include the adjustment to get a more accurate level of provisional tax paid for their customers.

Summary of technical determinations issued by the Commissioner

Examples on how the determinations will apply are included in the technical determinations as interpretation aids.

1. Depreciation – Determination A8

Subpart EE of the Income Tax Act 2007 quantifies the amount of depreciation recovery income that is income under Part C and quantifies the amount of depreciation loss a person is allowed as a deduction where the provisions of Part D are satisfied.

The Commissioner's depreciation determination requires a person to choose for an income year to either calculate depreciation and/or amortisation related amounts using the relevant provisions in the Income Tax Act 2007 or to exclude such amounts from accounting income and expenditure.

An AIM-capable accounting system will have the functionality to allow taxpayers to calculate depreciation and/or amortisation related amounts within their accounting software or calculate such amounts outside their accounting software and then include them as a user defined adjustment in their accounting software.

2. Trading stock – Determination A5

The Commissioner's trading stock determination details the tax adjustment required for trading stock as that term is defined in section EB 2 of the Income Tax Act 2007.

The determination applies to taxpayers who operate a periodic inventory system where their stock-take periods do not align with their AIM instalment periods. It does not apply where a taxpayer has a perpetual inventory system that adjusts accounting income and expenditure to record movements in trading stock for the AIM instalment period, as stock movements using that system should be incorporated into accounting income and expenditure.

Where a person operating a periodic inventory system does not complete a physical stock-take to determine closing stock for the AIM-instalment period the determination requires that a tax adjustment is made so that the person's closing value of their trading stock for the period equals the closing value of their trading stock for the income year before the current income year under section CH 1 of the Income Tax Act 2007. The opening value of the person's trading stock for the next AIM instalment period is equal to the closing stock value.

The tax adjustment in the determination is intended to achieve the same outcome for an AIM instalment period as section EB 23 of the Income Tax Act 2007 achieves for an income year.

The effect of the tax adjustment is to allow a deduction to accounting expenditure for the purchases made during the AIM instalment period.

Where the closing value of a taxpayer's trading stock for the income year before the current income year is materially different from the closing value of a taxpayer's trading stock for the AIM instalment period a physical stock-take should be undertaken to ensure a reasonably accurate calculation of the provisional tax liability for the income year.

An AIM-capable accounting system will have the functionality to allow a user defined adjustment which allows a value for the closing stock to be manually entered into the software.

3. Livestock – Determination A10

The Commissioner has issued a livestock determination which applies to livestock which is excluded from being trading stock due to the application of section EB 2(3)(f) of the Income Tax Act 2007.

Changes in numbers and values of livestock on hand from one year to the next can have a significant impact on a farmer's gross income.

To ensure the provisional tax liability under AIM is calculated with sufficient accuracy where a taxpayer does not have a perpetual inventory system to determine the closing value of livestock for an AIM instalment period, the taxpayer must complete a physical stock-take for the AIM instalment period.

A tax adjustment must be made to record the closing stock value which has been determined by the physical stock-take.

4. Private expenditure – Determination A4

A person is denied a deduction for an amount of expenditure or loss to the extent to which it is of a private or domestic nature. This is set out in section DA 2(2) of the Income Tax Act 2007.

The Commissioner has issued a private expenditure determination which requires a tax adjustment to accounting expenditure to the extent to which that expenditure includes expenditure which is of a private or domestic nature.

5. Losses – Determination A7

The AIM provisional tax method calculates the provisional tax liability based on year-to-date accounting income and expenditure for the current income year.

Where a loss arises in an earlier AIM instalment period that loss may be carried forward and offset against accounting income and expenditure for the next AIM instalment period until the loss is fully utilised. This should automatically occur within the AIM-capable software as it will calculate year-to-date income and expenditure.

In the event that a taxpayer has a loss balance under section IA 3(4) of the Income Tax Act 2007 from a prior income year, that loss becomes available to the taxpayer using AIM on the date the income tax return for the prior income year is assessed. The loss balance carried forward is allowed as a tax adjustment to increase accounting expenditure in the instalment period the assessment takes place.

The utilisation of losses that arose in a prior AIM instalment or prior income year are still subject to the commonality and continuity rules in the Income Tax Act 2007. Where these rules mean that a loss is not available in an AIM instalment period, a system or user defined adjustment will be required to ensure the software system calculates the provisional tax liability for the income year correctly.

Companies are not permitted to use loss offsets or subvention payments in AIM.

6. Accounts receivable and accounts payable – Determination A6

The Commissioner has issued a determination detailing a tax adjustment for accounts receivable and accounts payable.

The determination provides that where a taxpayer is not registered for GST or is registered for GST on the payments basis they are not required to accrue accounts receivable and accounts payable in calculating accounting income and expenditure.

Where a taxpayer is registered for GST on the hybrid basis they are required to accrue receivables when calculating accounting income and are required to calculate accounting expenditure on a cash basis.

For taxpayers not registered or registered on the payments or hybrid basis an election may be made to accrue accounts receivable and accounts payable in calculating accounting income and expenditure. If an election is made it cannot be revoked.

Taxpayers registered for GST on an invoice basis must accrue accounts receivable and accounts payable when calculating accounting income and expenditure under AIM.

7. Provisions – Determination A9

As a general principle a provision will not meet the test of being incurred and therefore will not be deductible for tax purposes due to the application of section DA 1 of the Income Tax Act 2007.

The Commissioner has issued a determination which requires that where accounting expenditure includes a provision, a tax adjustment is made to exclude that expenditure.

However, the determination permits a provision to be included in accounting expenditure where the provision relates to expenditure on employment income for a shareholder of a company.

A deduction for such expenditure is limited to the extent to which the company pays tax as an agent of the shareholder in relation to the provision for shareholder remuneration income.

8. Tax rates – Determination A3

The Commissioner's tax rates determination prescribes the tax rates which an AIM-capable accounting system must apply to a taxpayer's net positive accounting income and expenditure (after tax adjustments) for an AIM instalment period.

An AIM-capable accounting system calculates the provisional tax liability on a year to date basis using the tax rates set out in schedule 1, part A, of the Income Tax Act 2007.

9. Information and form – Determination A2

The Commissioner's information and form determination sets out the information required and prescribed for the purposes of sections 45 and 45B of the Tax Administration Act 1994 by AIM taxpayers and providers.

Further details are set out below regarding the information which AIM taxpayers and providers will be required to provide to the Commissioner.

Exclusion determination

Under section 91 AAY of the Tax Administration Act 1994 the Commissioner may determine that a class of taxpayers must not use the AIM method.

The Commissioner has issued a determination under section 91 AAY *(Determination A1)* excluding the following classes of taxpayers from using the AIM method:

- trustees and beneficiaries of a trust;
- partnerships;
- taxpayers who have investments in foreign investment funds or controlled foreign companies for the income year;
- Māori authorities;
- portfolio investment entities; and
- superannuation funds.

Payment dates

Taxpayers who use the AIM method are required to make provisional tax payments more often—in line with their GST filing dates.

Taxpayers registered for monthly GST will make payments twelve times a year and those not registered, registered two or six-monthly for GST will make payments six times a year.

The payment dates for each AIM instalment are prescribed by section RC 9(4B) of the Income Tax Act 2007 and align with the payment dates for GST.

Refunds

Under section RM 6B of the Income Tax Act 2007 the Commissioner can refund amounts of overpaid AIM provisional tax throughout the income year where the AIM payments to date are greater than the AIM calculation of the tax liability year-to-date.

There is no requirement for a taxpayer to file an imputation credit account return mid-year to access an overpayment of AIM provisional tax.

Section 120 VB of the Tax Administration Act 1994 provides that no use-of-money interest is payable to the Commissioner on overpaid AIM provisional tax.

Information requirements

Information will be provided to Inland Revenue by both the AIM taxpayer and the AIM provider.

Under section 45 of the Tax Administration Act 1994 taxpayers using the AIM method are required to provide the Commissioner with a Statement of Activity on or before each AIM instalment date.

An AIM-capable accounting system will have the functionality to map ledger accounts into a Statement of Activity form which is provided to the Commissioner through the software itself.

The Statement of Activity form is not a tax return. It is a summary of what is in the accounting software at the date the Statement of Activity is provided to the Commissioner.

Under section 45B of the Tax Administration Act 1994 AIM providers must provide information to the Commissioner when and if requested in relation to their AIM-capable software products. The Commissioner cannot require taxpayer-specific information to be provided under this section. Information required by the Commissioner under section 45B must be provided within six months of the end of the tax year. Collection of this information will assist the Commissioner with further policy development and improvements to AIM.

Interest and penalties

Where an AIM taxpayer makes the payments calculated by their AIM-capable accounting software by the instalment date section 120 KBC of the Tax Administration Act 1994 provides that they will not be exposed to use-of-money interest should the year-end residual income tax liability result in a different tax liability, until their terminal tax date.

This is subject to the taxpayer not having entered a provisional tax interest avoidance arrangement which is defined in section 120 KBB(4) of the Tax Administration Act 1994.

If an AIM taxpayer pays less than what their AIM-capable accounting software calculates, use-of-money interest will be imposed on the shortfall from the date of underpayment.

Late payment penalties may also apply if a payment of provisional tax is made after the AIM instalment date.

Section RC 5C of the Income Tax Act 2007 provides that where an AIM provisional taxpayer has been removed from AIM they will be required to use the estimate method and will be subject to use-of-money interest.

Section 120 VB of the Tax Administration Act 1994 provides that no use-of-money is payable by the Commissioner on overpaid AIM provisional tax.

The definition of "tax position" in section 3(1) of the Tax Administration Act 1994 has been amended so that the use of the AIM provisional tax method, including the use of the software, is within the meaning of the term "tax position" in the Tax Administration Act 1994.

This will require that taxpayers take reasonable care in the calculation of their provisional tax payments throughout the year in terms of section 141A of the Tax Administration Act 1994.

However section 141B of the Tax Administration Act 1994 has been amended to provide that a taxpayer does not take an unacceptable tax position merely by using the AIM method and an approved AIM provider's AIM-capable accounting system. Taxpayers paying AIM provisional tax using a large business AIM-capable accounting system or who have been approved to continue using AIM as their income has grown over $5 million will continue to be subject to the unacceptable tax position penalty.

Under section 119(1)(cb) of the Tax Administration Act 1994 the Commissioner may determine the amount of provisional tax due under AIM if the tax liabilities calculated are not reasonably accurate assessments of tax liabilities for the relevant income and expenditure.

Example 4

Tussock Socks Ltd has been paying its provisional tax using AIM. On its third AIM provisional tax payment date, the software calculated that Tussock Socks Ltd owed $500 in provisional tax to Inland Revenue and submitted the Statement of Activity showing this amount to be due. Instead of paying $500 to Inland Revenue, Tussock Socks Ltd only paid $100.

Tussock Socks Ltd will be liable for UOMI and late payment penalty on the $400 underpayment until it is paid (or the liability is extinguished by a future instalment period).

Example 5

Cameo Jewels Ltd is a small jewellery company using AIM to pay its provisional tax. It calculates its provisional tax payments using software, and makes the payments accordingly. At year-end the company meets with its accountant who discovers their depreciation was calculated incorrectly and a bad debt had not been written off, resulting in additional income tax due of $300. Cameo Jewels Ltd pays this amount of terminal tax and has no UOMI or shortfall penalty applied. As these errors are simple oversights it is likely Cameo Jewels Ltd has taken reasonable care in the calculation of its tax liability.

Example 6

Tiger Fins Corporation is a fishing company that uses specialised fishing industry software approved by Inland Revenue as large business AIM capable (for businesses whose turnover is over $5 million). It has discovered that if it categorises its catch in different fish quantities and qualities it can lower its income tax liability. Upon receipt of the company's Statement of Activity and audit queries, this misuse of the company's software is brought to Inland Revenue's attention.

Tiger Fins Corporation (as a large business AIM-capable taxpayer) would be removed from AIM, placed in the estimate method, be subject to UOMI and late payment penalties on what the company's income was determined to be by the Commissioner. It is also likely the company would be considered to have taken an unacceptable tax position in the calculation of its tax liability.

Tax pooling

Sections RP 17 and RP 17B of the Income Tax Act 2007 provide that tax pooling cannot be used for AIM provisional tax.

However, tax pooling can continue to be used for terminal tax and reassessments.

Transfers of overpaid provisional tax

Under section LA 6(2)(db) of the Income Tax Act 2007 a company using AIM may transfer excess tax credits to shareholders and reduce the shareholders' use of money interest liability.

Section 120 LB of the Tax Administration Act 1994 provides that the amount transferred does not give rise to a tax credit for the shareholder but is treated as transferred tax paid for the year that the provisional tax credit relates to. The total amounts transferred to the shareholder are pro-rated against all of their provisional tax instalments for the year.

The transfer is treated as a refund for the purposes of the AIM Company's imputation credit account.

Example 7

Bogart Bugles Ltd is a retailer that sells musical instruments, owned equally by John and Lynn. They elect to use AIM for their businesses and in the income year ending 31 March 2019 make the following overpayments in AIM. All parties have a March balance date.

Provisional tax payment dates	28-Jun 2018	28-Aug 2018	28-Oct 2018	15-Jan 2019	28-Feb 2019	7-May 2019
Bogart Bugles Ltd AIM overpayments	$100	$100	$100	$100	$100	$100
Shareholder provisional tax liability due dates		$200		$200		$200

In this instance, Bogart Bugles Ltd can easily transfer its overpaid provisional tax at year-end to John and Lynn to meet their provisional tax liabilities. As the dates align there will be no UOMI charges on John and Lynn.

Example 8

Murray's Mutts Ltd is a dog breeding operation owned by Sarah and Gareth. Murray's Mutts Ltd has an agreed July balance date, as is common in the dog breeding industry. Sarah and Gareth have standard March balance dates. The payment schedule for the 2019 income year would look as follows:

Provisional tax payment dates	28-Aug 2018	28-Oct 2018	15-Jan 2019	28-Feb 2019	7-May 2019	28-Jun 2019	28-Aug 2019
Murray's Mutts Ltd AIM overpayments		$100	$100	$100	$100	$100	$100
Shareholder provisional tax liability due dates	$150		$150		$150		

In this instance, Murray's Mutts Ltd would be able to transfer its excess provisional tax payments to Sarah and Gareth despite there being a mismatch in their provisional tax dates. These transfers would be calculated and transferred at Murray's Mutts Ltd's year-end.

Murray's Mutts Ltd's transfer is limited to the amount of overpaid tax in Murray's Mutts Ltd – that is, the company cannot transfer more than $450 as the transfer cannot be more than Sarah and Gareth's provisional tax underpayment for the year. Payments can be transferred to Sarah and Gareth at their 2019 provisional tax dates, negating any UOMI exposure.

Determination A1: Classes of taxpayers that must not use AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers may calculate their provisional tax payments by using accounting software if they do not belong to a class of taxpayers that must not use the AIM method in a determination made under section 91AAY of the Tax Administration Act 1994.

(2) This determination details the classes of taxpayers that must not use the AIM method.

2. Application

This determination applies for the 2018-19 and later income years.

3. Classes of taxpayers that must not use the AIM method

The following classes of taxpayers must not use the AIM method for an income year:

(a) trustees and beneficiaries of a trust:

(b) partnerships:

(c) taxpayers who have investments in foreign investment funds or controlled foreign companies:

(d) Māori authorities:

(e) portfolio investment entities:

(f) superannuation funds.

4. Interpretation

(1) Any word or term that is defined in a Revenue Act and used, but not defined, in this determination has the same meaning as in that Act.

(2) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A2: AIM information and form

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

1. Scope

(1) Under section 91AAZ of the Tax Administration Act 1994, the Commissioner may determine, for the purposes of section 45 of the Tax Administration Act 1994, information and form required or prescribed under section 45.

(2) This determination requires and prescribes information and form for the purposes of section 45 of the Tax Administration Act 1994.

2. Application

This determination applies for the 2018-19 and later income years.

3. Information and form

The information required and prescribed for the purposes of section 45 of the Tax Administration Act 1994 is described in the *Inland Revenue AIM-capable software technical specifications*, as amended from time to time.

4. Interpretation

(1) Any word or term that is defined in a Revenue Act and used, but not defined, in this determination has the same meaning as in that Act.

(2) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A3: Tax rates for AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations made under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the applicable tax rate to apply to year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

2. Application

This determination applies for the 2018-19 and later income years.

3. Tax rates

(1) For a person, an AIM-capable accounting system must apply the applicable tax rate in subclause (2) or (3) to the person's net positive accounting income and expenditure year-to-date, after tax adjustments, to calculate their current instalment period payment, as provided by subclause (7).

(2) If the person is a company that schedule 1, part A, clause 2 of the Income Tax Act 2017 applies to for the tax year to which the current instalment period relates, the tax rate for the instalment period is the basic rate provided by schedule 1, part A, clause 2 of that Act.

(3) If the person is a person that schedule 1, part A, clause 1 applies to for the tax year to which the current instalment period relates, the tax rate for the instalment period is given by the following formula:

full-year tax ÷ full-year net positive amount.

(4) In the formula—

full-year tax is the amount of tax a person would have for the tax year related to the current instalment period from applying table 1 of schedule 1, part A of the Income Tax Act 2007 to the full-year net positive amount:

full-year net positive amount is the amount given by the formula in subclause (6).

(5) For the purposes of calculating the full-year net positive amount, the formula is—

annual instalments × year-to-date net positive amount ÷ instalments year-to-date.

(6) In the formula—

annual instalments is the number of instalment periods for the relevant tax year:

year-to-date net positive amount is the net positive accounting income and expenditure, after tax adjustments, for instalment periods, including the current instalment period, year-to-date:

instalments year-to-date is the number of instalment periods, including the current instalment period, year-to-date.

(7) For the purposes of calculating the current instalment period payment, the formula is—

year-to-date net positive amount × tax rate – (payments + refunds)

(8) In the formula—

payments is the amount of provisional tax paid for the income year, year-to-date:

refunds is the amount of provisional tax refunded for the income year, year-to-date:

tax rate is the tax rate provided by subclause (2) or (3):

year-to-date net positive amount is the net positive accounting income and expenditure, after tax adjustments, for instalment periods, including the current instalment period, year-to-date.

Example:

Emma is a sole trader who uses AIM to calculate her provisional tax liability. She pays provisional tax in 6 instalments during the year.

Emma is in her 3rd instalment period, August/September 2018.

For the AIM instalment periods April/May 2018, June/July and August/September 2018 Emma has the following net positive accounting income (after accounting expenditure and tax adjustments):

AIM Instalment Period	Net positive accounting income ($)
April/May 2018	5,000
June/July 2018	7,510
August/September 2018	14,250
Total	**26,760**

At the end of the June/July period, Emma has made AIM payments totalling $2,500.

The full-year net positive amount for the purposes of clause 3(4) of this determination is calculated using the formula in clause 3(5)—

annual instalments × year-to-date net positive amount ÷ instalments year-to-date.

For Emma, the full-year net positive amount is—

6 × 26,760 ÷ 3 = 53,520

Having calculated the full-year net positive amount the full-year tax can be calculated. For Emma the full-year tax is—

Income tax rate	Income	Tax
Income up to $14,000, taxed at 10.5%	$14,000	$1,470
Income over $14,001 and up to $48,000, taxed at 17.5%	$34,000	$5,950
Income over $48,001 and up to $70,000, taxed at 30%	$5,520	$1,656
Remaining income $70,001 onwards, taxed at 33%	$0	$0
Total	**$53,520**	**$9,076**

The full year-tax for Emma therefore is $9,076.

The tax rate applicable to the net positive accounting income for the instalment period is calculated using the formula in clause 3(3)—

full-year tax ÷ full-year net positive amount.

The tax rate for Emma therefore is calculated in the following way—

9,076 ÷ 53,520 = 16.9581%

Emma's tax rate therefore is 16.96% for the current instalment period.

Emma applies this rate, on a year-to-date basis, to calculate her payment due for the current August/September 2018, using the formula in clause 3(7)—

year-to-date net positive amount × tax rate

26,760 × 0.1696 = 4,538

Emma has paid $2,500 year to date and received no refunds year to date, so her payment for August/September 2018 is—

4,538 – (2,500 + 0) = 2,039

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this notice, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date.

(2) Any word or term that is defined in the Income Tax Act 2007 and the Tax Administration Act 1994 and used, but not defined, in this determination has the same meaning as in those Acts.

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A4: Tax adjustments for private expenditure under AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations made under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the tax adjustment for private expenditure to calculate year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

(3) The private limitation is set out in section DA 2(2) of the Income Tax Act 2007 and provides that a person is denied a deduction for an amount of expenditure or loss to the extent to which it is of a private or domestic nature.

(4) If accounting expenditure includes an amount of private expenditure, a tax adjustment is necessary to exclude that expenditure.

2. Application

(1) This determination applies for the 2018-19 and later income years.

(2) This determination does not make tax adjustments relating to entertainment expenditure to which section DD 1(1) of the Income Tax Act 2007 applies.

3. Tax adjustments: private expenditure not included

(1) This clause requires tax adjustments to the extent to which a person's accounting income and expenditure does not already accord with the adjustments described in this clause.

(2) For a person, for an instalment period, accounting expenditure must not include an amount of private expenditure.

Example 1:

Kelvin uses an AIM-capable accounting system to calculate his provisional tax liability.

From his logbook, Kelvin knows that 17% of his travel in his motor vehicle is private travel. Kelvin applies this percentage to the cost code for motor vehicle expenses in his accounting software.

An AIM-capable accounting system will exclude 17% of Kelvin's motor vehicle expenses because 17% of this expenditure is private in nature.

Example 2:

Jennifer uses an AIM-capable accounting system to calculate her provisional tax liability.

During the instalment period April/May, Jennifer paid for her children's school trip from her business's bank account. Jennifer has excluded the costs of the school trip from accounting expenditure by recording these costs against her shareholder current account.

For the April/May instalment period, a tax adjustment is not required to accounting expenditure to exclude the cost of the school trip.

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this determination, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date:

private expenditure, for a person, is the expenditure for which the person is denied a deduction under section DA 2(2) of the Income Tax Act 2007.

(2) Any word or term that is defined in a Revenue Act and used, but not defined, in this determination has the same meaning as in that Act.

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A5: Tax adjustments for trading stock under AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations made under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the tax adjustment for trading stock to calculate year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

(3) This determination details a tax adjustment for trading stock as defined in section EB 2 of the Income Tax Act 2007. It applies for people who operate a periodic inventory system where the stock-take periods do not align with their AIM instalment periods.

(4) This determination does not apply to a person who has a perpetual inventory system that adjusts accounting income and expenditure for movements in trading stock at the end of their AIM instalment periods. A person who has a perpetual inventory system must value closing stock as determined by that system at the end of each AIM instalment period.

2. Application

This determination applies for the 2018-19 and later income years.

3. Tax adjustments: periodic inventory systems

(1) This clause requires tax adjustments to the extent to which a person's accounting income and expenditure does not already accord with the adjustments described in this clause.

(2) If a person has a periodic inventory system and they do not complete a stock-take for the purposes of accounting for closing stock for an AIM instalment period in an income year (the **current income year**), the tax adjustment provided in subclause (3) must be made for the period.

(3) For the AIM instalment period, the person must make a tax adjustment to accounting income and expenditure on the basis that the closing value of their trading stock for the period equals the closing value of their trading stock for the income year before the current income year under section CH 1 of the Income Tax Act 2007. Opening value of the trading stock for the next AIM instalment period is equal to the closing value.

(4) If a person has a periodic inventory system and they complete a stocktake for the purposes of accounting for closing stock for an AIM instalment period (the **current period**), opening value of the trading stock for the next AIM instalment period is equal to the closing value for the current period.

Example 1:

Ava uses an AIM-capable accounting system to calculate her provisional tax liability.

The stock turnover in Ava's business is low though the value of each item of stock is relatively high. She uses an inventory system that does not track each individual stock movement as they occur. In each AIM instalment period Ava completes a stocktake to determine the closing value of her stock on hand. Ava then manually records the value of her closing stock in her accounting software.

The AIM-capable accounting system that Ava uses will include the value of closing stock from the stocktakes Ava completes when calculating the cost of goods sold for each AIM instalment period.

Example 2:

Mason uses an AIM-capable accounting system to calculate his provisional tax liability.

For the 2018 income year Mason's closing stock was $5,000 under section CH 1 of the Income Tax Act 2007.

He uses an inventory system that does not track each individual stock movement as they occur.

Due to the relatively low value of Mason's closing stock during the 2019 income year he does not wish to complete a stocktake at the end of each AIM-instalment period.

In these circumstances under clause 3(2) of this determination a tax adjustment will be made to accounting income and expenditure to reflect a closing value of trading stock for the AIM-instalment period equal to $5,000. The opening value of Mason's trading stock for the next AIM instalment period will be $5,000.

Example 3:

Keith uses a perpetual inventory system in his "Gadgets are us" store. This perpetual system interfaces with his AIM capable accounting software which uses those inventory records in calculating his income and expenditure for a period. Keith does not need to make any adjustment as his income and expenditure already includes a closing stock adjustment.

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this determination, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date:

periodic inventory system, means a system which does not track each individual stock movement as they occur but relies on periodic stocktakes to determine the closing value of trading stock and calculate accounting income and expenditure in relation to it:

trading stock has the same meaning as in section EB 2 of the Income Tax Act 2007.

(2) Any word or term that is defined in a Revenue Act and used, but not defined, in this determination has the same meaning as in that Act.

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A6: Tax adjustments for accounts receivable and accounts payable under AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations made under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the tax adjustment for accounts receivable and payable to calculate year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

(3) Where a person is registered for GST on a payments basis or is not registered for GST, they are not required to accrue accounts receivable and accounts payable in calculating accounting income and expenditure. They may however elect to accrue accounts receivable and accounts payable in calculating accounting income and expenditure, and, where an election is made, that election cannot be revoked for the income year.

(4) A person that is registered for GST on an invoice basis must account on an accrual basis.

(5) A person that is registered for GST on a hybrid basis may account on a hybrid basis or on an accrual basis.

2. Application

This determination applies for the 2018-19 and later income years.

3. Tax adjustments: choices and adjustments

(1) This clause requires tax adjustments to the extent to which a person's accounting income and expenditure does not already accord with the adjustments described in this clause.

(2) Subclauses (3), (4), and (5) apply to adjust accounting income and expenditure, if such income and expenditure is assessable or deductible.

(3) A person who is not registered for GST or is a registered person who must account for GST on a payments basis must account for accounting income and expenditure on a money received and paid basis for an income year, unless they make an election to account on an accounts receivable and accounts payable basis (**accrual accounting basis**) for an income year. For instalment periods in the income year, tax adjustments to accounting income and expenditure must be made to account for their elected basis.

(4) A registered person who must account for GST on an invoice basis for an instalment period must use the accrual accounting basis using tax invoices, debit notes, and credit notes, received and issued as the basis for accounts receivable and payable (**registered accrual accounting basis**). For the instalment period, tax adjustments to accounting income and expenditure must be made to account for the registered accrual accounting basis.

(5) A registered person who must account for GST on a hybrid basis must choose, for an income year, to account for accounting income and expenditure on either an accrual accounting basis or on a money paid and accounts receivable basis. For an instalment period in the income year, tax adjustments to accounting income and expenditure must be made to account for their basis.

Example:

Trish uses an AIM-capable accounting system to calculate her provisional tax liability and is registered for GST on the invoice basis.

For her AIM instalment period August/September Trish had invoiced sales (excluding GST) of $12,000.

Of her total invoiced sales during the AIM-instalment period she received payments of $7,520.

Trish has accounts payable during the AIM-instalment period (excluding GST) of $8,000. Of that, Trish paid $6,750 during the AIM-instalment period.

An AIM-capable accounting system must ensure that accounting income for sales is $12,000 making an adjustment of $5,461 to income on top of her cash accounting basis position ($6,539).

Similarly her accounting expenditure is $8,000 not $6,750.

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this determination, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date.

(2) Any word used, but not defined, in this determination has the same meaning as in the Income Tax Act 2007 or the Tax Administration Act 1994 (as appropriate), unless the context otherwise requires.

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A7: Tax adjustments for losses under AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations made under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the tax adjustment for losses to calculate year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

(3) A taxpayer is allowed an increase in accounting expenditure on account of a loss balance carried forward under section IA 3(4) of the Income Tax Act 2007. A loss balance carried forward becomes available when the previous tax year's assessment has been made.

(4) Grouping of tax losses by companies is not permitted in AIM.

2. Application

This determination applies for the 2018-19 and later income years.

3. Tax adjustments: previous assessed year

(1) This clause requires tax adjustments to the extent to which a person's accounting income and expenditure does not already accord with the adjustments described in this clause.

(2) For a person, for the instalment in the current income year in which the date of assessment for the previous tax year falls, the previous tax year's assessed loss is allowed as a tax adjustment to increase accounting expenditure in that instalment period.

Example:

Graeme assesses a loss balance for the 2020-21 tax year of $1m, to be carried forward to the 2021-22 tax year. His assessment is dated 20 December 2021. It occurs part way through the 3rd of 6 instalment periods for his 2021-22 income year. Graeme has $1m expenditure in his 3rd instalment for his 2021-22 income year.

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this determination, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date:

previous tax year's assessed loss is the loss balance carried forward to the tax year corresponding to the current income year from the previous tax year.

(2) Any word or term that is defined in a Revenue Act and used, but not defined, in this determination has the same meaning as in that Act:

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A8: Tax adjustments for depreciation loss and depreciation recovery income under AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations made under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the tax adjustment for depreciation loss and depreciation recovery income to calculate year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

(3) It provides that, for tax adjustment purposes, accounting income and expenditure must not include any depreciation- or amortisation-related amounts unless a person chooses to use the relevant provisions in the Income Tax Act 2007.

(4) Subpart EE of the Income Tax Act 2007 quantifies the amount of depreciation recovery income that is income under Part C of the Income Tax Act 2007 and quantifies the amount of depreciation loss a person is allowed as a deduction where the provisions of Part D of the Income Tax Act 2007 are satisfied.

(5) Where a person chooses to use tax depreciation, this determination provides an appropriate tax adjustment, consistent with subpart EE of the Income Tax Act 2007, for—

(a) accounting income, commensurate with the amount of depreciation recovery income arising under Part C of the Income Tax Act 2007:

(b) accounting expenditure, commensurate with the amount of depreciation loss arising under Part D of the Income Tax Act 2007.

(6) If a person chooses to not use tax depreciation, this determination provides a tax adjustment such that accounting income and expenditure does not include any depreciation- or amortisation-related amounts.

2. Application

This determination applies for the 2018-19 and later income years.

3. Tax adjustments: no depreciation or choose tax depreciation

(1) This clause requires tax adjustments to the extent to which a person's accounting income and expenditure does not already accord with the adjustments described in this clause.

(2) A person must choose, for an income year, to either—

(a) not account for any depreciation- or amortisation-related income and expenditure in relation to any of their depreciable property; or

(b) account for depreciation- and amortisation-related income and expenditure in relation to all of their depreciable property using, for each instalment period in the income year, the amounts of depreciation recovery income and depreciation loss calculated, for the relevant period, under the Income Tax Act 2007.

(3) If a person uses the choice in subclause (2)(b), the amount of depreciation loss is limited to the amount calculated on a year-to-date basis.

(4) For an instalment period in the income year, tax adjustments to accounting income and expenditure must be made to account for their choice.

Example 1:

Sharon uses an AIM-capable accounting system to calculate her provisional tax.

The accounting software which Sharon uses calculates depreciation recovery income and depreciation loss consistent with subpart EE of the Income Tax Act 2007.

For the AIM instalment period December/January 2019, Sharon's accounting software has calculated a depreciation loss of $2,000 for the 2 months year-to-date.

In these circumstances clause 3 of this determination will allow the depreciation loss of $2,000 as accounting expenditure in the December/January 2019 AIM-instalment period.

Example 2:

Keith uses an AIM-capable accounting system to calculate his provisional tax.

He chooses to account for depreciation and amortisation related income and expenditure under clause 3(2)(b).

He has one asset in his business. The opening tax book value of the asset in his AIM-capable software at the beginning of the year is $3,200 and he uses the diminishing value method of depreciation.

The diminishing value rate of depreciation for the asset is 50%. Under clause 3(3), Keith is only permitted a deduction for the depreciation calculation year-to-date. His current AIM instalment period is his second 2-month period for the income year. Thus, the year-to-date amount is for 4 months.

Keith's software automatically calculates the depreciation charge for the year (being 50% of $3,200) as $1,600 and apportions that charge for the 4 months year-to-date.

Keith has expenditure of $533.33 for depreciation for the year-to-date. This automatically feeds into his accounting income and expenditure from his fixed asset register so no separate tax adjustment is required.

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this determination, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date.

(2) Any word or term that is defined in the Income Tax Act 2007 and the Tax Administration Act 1994 and used, but not defined, in this determination has the same meaning as in those Acts.

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A9: Tax adjustments for provisions under AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the tax adjustment to provisions to calculate year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

(3) A provision, as a general principle, will not meet the test of being incurred and therefore will not be deductible for tax purposes.

(4) Where accounting expenditure includes a provision, a tax adjustment is necessary to exclude that expenditure.

(5) However a provision is permitted if it relates to expenditure on employment income for a shareholder of a company. A deduction for accounting expenditure is limited to the extent to which the company pays tax as an agent of the shareholder in relation to the provision for shareholder employment income.

2. Application

This determination applies for the 2018-19 and later income years.

3. Tax adjustments: choices and adjustments

(1) This clause requires tax adjustments to the extent to which a person's accounting income and expenditure does not already accord with the adjustments described in this clause.

(2) For a person, for an instalment period, accounting expenditure must not include an amount on account of a provision.

(3) Despite subclause (2), an instalment period's accounting expenditure may include an amount on account of a provision to the extent to which the person is a company and the provision relates to expenditure on employment income for a shareholder-employee of the company. The amount of the provision allowed as an adjustment to increase accounting expenditure for the instalment period is the lesser of—

(a) the provision; and

(b) the amount of tax paid during the instalment period as agent for the shareholder-employee divided by the rate given by subclause (4).

(4) The tax rate for the purposes of subclause (3)(b) is given by the following formula—

full-year tax ÷ full-year income.

(5) In the formula—

full-year tax is the amount of tax the shareholder-employee would have for the tax year related to the current instalment period from applying table 1 of schedule 1, part A of the Income Tax Act 2007 to the full-year income:

full-year income is the amount given by the formula in subclause (6).

(6) For the purposes of calculating the full-year income, the formula is—

annual instalments × year-to-date net positive amount ÷ instalments year-to-date.

(7) In the formula—

annual instalments is the number of instalment periods for the company for the relevant tax year:

year-to-date net positive amount is the total amount of provisions allowed under this determination for the shareholder-employee for instalment periods, including the current instalment period, year-to-date:

instalments year-to-date is the number of instalment periods, including the current instalment period, year-to-date.

Example:

Oliver's Apples Limited (**OAL**) uses AIM to calculate its provisional tax payments which it pays in 6 instalments during the year. OAL has 2 shareholder's Oliver and Emily.

For the first AIM-instalment period April/May 2018-19, OAL has net accounting income before shareholder remuneration of $20,000.

It is intended that for the AIM-instalment period April/May 2018-19 OAL will make provisions for shareholder remuneration of $11,500 for Oliver and $8,500 for Emily that form part of the accounting expenditure for the instalment period. It is also intended that the tax liability relating to both shareholders' remuneration will be paid by OAL as agent for each shareholder.

A person's full-year income amount is calculated using the formula in clause 3(6).

For Oliver the full-year income is—

$6 \times 11{,}500 \div 1 = 69{,}000$

For Emily the full-year income is—

$6 \times 8{,}500 \div 1 = 51{,}000$

The full-year tax in clause 3(5) of this determination is calculated by applying table 1 of schedule 1, part A of the Income Tax Act 2007 to the full-year income amount.

For Oliver the full-year tax amount is—

Income tax rate	Income	Tax
Income up to $14,000, taxed at 10.5%	$14,000	$1,470
Income over $14,001 and up to $48,000, taxed at 17.5%	$34,000	$5,950
Income over $48,001 and up to $70,000, taxed at 30%	$21,000	$6,300
Remaining income $70,001 onwards, taxed at 33%	$0	$0
Total	**$69,000**	**$13,720**

Based on a full-year tax amount for Oliver of $13,720 OAL makes a decision to make a payment as agent for Oliver of $2,286.67 ($13,720 ÷ 6 = $2,286.67).

For Emily the full-year tax amount is—

Income tax rate	Income	Tax
Income up to $14,000, taxed at 10.5%	$14,000	$1,470
Income over $14,001 and up to $48,000, taxed at 17.5%	$34,000	$5,950
Income over $48,001 and up to $70,000, taxed at 30%	$3,000	$900
Remaining income $70,001 onwards, taxed at 33%	$0	$0
Total	**$51,000**	**$8,320**

Based on a full-year tax amount for Emily of $8,320, OAL makes a decision to make a payment as agent for Emily of $1,386.67 ($8,320 ÷ 6 = $1,386.67).

Having calculated the full-year tax and full-year income for each shareholder the tax rate for the purposes of clause 3(3)(b) of this determination can be calculated.

The formula in clause 3(4) provides that the tax rate is calculated by dividing a person's full-year tax by their full-year income.

For Oliver the rate for the current instalment period is calculated in the following way:

$13{,}720 \div 69{,}000 = 0.198841$.

For Emily the rate for the current instalment period is calculated in the following way:

$8{,}320 \div 51{,}000 = 0.163137$.

Under clause 3(3), OAL's accounting expenditure for the current instalment period is increased by the lesser of—

(a) the provision; and

(b) the amount of tax paid during the instalment period as agent for the shareholder-employee divided by the rate given by clause 3(4).

The amount of tax paid during the April/May AIM-instalment period for Oliver is $2,286.67 and for Emily is $1,386.67.

The tax OAL pays as agent for Oliver and Emily will result in an increase to OAL's accounting expenditure of $11,500 ($2,286.67 ÷ 0.198841 = $11,500) and $8,500 ($1,386.67 ÷ 0.163137 = $8,500).

Oliver's personal residual income tax under the Income Tax Act 2007 is reduced by $2,286.67.

Emily's personal residual income tax is reduced by $1,386.67.

The reductions in residual income tax arise under the agency arrangement between OAL, and Oliver and Emily, in accordance with paragraph (a) of the definition r**esidual income tax** in section YA 1 of the Income Tax Act 2007.

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this determination, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date:

provision means an amount of accounting expenditure provided to meet expenditure not yet incurred.

(2) Any word used, but not defined, in this determination has the same meaning as in the Income Tax Act 2007 or the Tax Administration Act 1994 (as appropriate), unless the context otherwise requires.

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

Determination A10: Tax adjustments for livestock under AIM

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

1. Scope

(1) Under the Accounting Income Method (**AIM**), taxpayers can calculate their provisional tax payments by using accounting software if that software is in accordance with determinations made under section 91AAX of the Tax Administration Act 1994.

(2) An AIM-capable accounting system calculates provisional tax using year-to-date accounting income and expenditure adjusted for tax purposes (if required). The purpose of this determination is to detail the tax adjustment for valuing livestock on hand to calculate year-to-date net positive accounting income and expenditure, after tax adjustments, for an AIM instalment period.

(3) This determination applies to livestock that is excluded from being trading stock due to the application of section EB 2(3)(f) of the Income Tax Act 2007.

2. Application

This determination applies for the 2018-19 and later income years.

3. Tax adjustments: some periodic inventory systems

(1) This clause requires tax adjustments to the extent to which a person's accounting income and expenditure does not already accord with the adjustments described in this clause.

(2) If a person does not use a perpetual inventory system to determine the closing value of livestock and calculate accounting income and expenditure in relation to it for an AIM instalment period, the tax adjustment provided in subclause (3) must be made for the period.

(3) For the AIM instalment period, the person must make a tax adjustment to accounting income and expenditure on the basis of the closing value for their livestock determined by a physical stocktake done for the period.

(4) A person using national standard costs to value livestock must—

(a) use the Commissioner's most recent determination issued under section EC 23 of the Income Tax Act 2007 to calculate the value of homebred livestock and the value of livestock listed in schedule 18, column 2 of the Income Tax Act 2007; and

(b) value purchases at cost in terms of section EC 24 of the Income Tax Act 2007.

(5) A person using the herd scheme and national average market values to value livestock must use the Commissioner's most recent determination issued under section EC 15 of the Income Tax Act 2007 to calculate the value of livestock.

(6) Where the Commissioner has received a valid election from a taxpayer under section EC 17 of the Income Tax Act 2007, the value of livestock under subclause (5) may reflect the adoption of a herd value ratio for a type of specified livestock subject to the herd scheme.

Example:

Liam operates a dairy farm and uses an AIM-capable accounting system to calculate his provisional tax liability.

To value his livestock Liam uses the national standard cost scheme.

For the current income year Liam acquired a perpetual inventory system which provides a continuous record of each stock movement.

In the above circumstances applying clause 3(1) of this determination, Liam may rely on the output of his perpetual inventory system, and on the relevant values under subpart EC of the Income Tax Act 2007.

Liam may also rely on the Commissioner's determination under section EC 23 of that Act setting national standard costs which was issued for the income year prior to the current income year.

4. Tax adjustments: manual and automatic

A tax adjustment under this determination must be made by—

(a) the user of the accounting software, manually:

(b) the accounting software, automatically:

(c) any other means, as appropriate.

5. Tax adjustments: errors and oversights in previous instalment period

An error or oversight affecting accounting income or expenditure (including income or expenditure adjusted by a determination) for an instalment period in an income year must be corrected by making a tax adjustment in the next instalment period after the one in which the error or oversight is identified.

6. Interpretation

(1) In this determination, unless the context otherwise requires,—

instalment period, for a person, means the 2-monthly or monthly period given by schedule 3, part AB of the Income Tax Act 2007 for the applicable instalment date:

livestock means livestock, as defined in section YA 1 of the Income Tax Act 2007, excluded from being trading stock due to the application of section EB 2(3)(f) of the Income Tax Act 2007:

perpetual inventory system means a system which tracks each individual stock movement as it occurs and does not solely rely on periodic stocktakes to determine the closing value of trading stock and calculate accounting income and expenditure in relation to it:

trading stock has the same meaning as in section EB 2 of the Income Tax Act 2007.

(2) Any word or term that is defined in a Revenue Act and used, but not defined, in this determination has the same meaning as in that Act.

(3) Examples used in this determination are included in this determination only as interpretational aids. If there is conflict between an interpretational aid and a provision of this determination, the provision prevails.

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

This determination is signed on the 10th day of October 2017.

Keith Taylor
Manager, PAS

LEGAL DECISIONS – CASE NOTES

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

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

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

Filing of amended statement of claim an abuse of process when proceeding was previously struck out

Case	Muir & Anor v Commissioner of Inland Revenue [2017] NZHC 2082
Decision date	29 August 2017
Act(s)	Rules 2.11 and 15.1 High Court Rules 2016
Keywords	Strike-out, "dismissing or staying part of proceeding", "review of registrar's decision", inherent jurisdiction and abuse of process

Summary

The taxpayers Dr Muir ("Dr Muir") and Hillvale Holdings Limited ("Hillvale") are parties to the Trinity litigation. This proceeding concerns amended statements of claim being filed or sought to be filed in proceedings (CIV-2011-404-1132) which were struck out by the High Court (Faire J) on 22 April 2015. The Court held that the proceedings were at an end when Faire J struck them out and the amended statements of claim were an abuse of the Court's process.

Impact

1. A proceeding which is struck out is struck out in its entirety and it is an abuse of the Court's processes to attempt to file an amended statement of claim.
2. A summary judgment or strike out application is not required where the filing of a document is a nullity and it is appropriate for a party to file a memorandum drawing the Court's attention to the registry's error in accepting the document for filing.
3. The Court has an inherent jurisdiction to prevent abuses of its processes and to direct removal of the document which should not have been accepted for filing.

Facts

On 22 April 2015 the High Court (Faire J) struck out the tax challenges and dismissed the appeals brought by Dr Muir, Hillvale and other taxpayers. Dr Muir appealed Faire J's decision but Hillvale did not. The Court of Appeal subsequently dismissed the appeal. Leave was granted by the Supreme Court and, after Dr Muir attempted to argue new grounds, the leave granted was revoked.

The High Court Registrar accepted Dr Muir's amended statement of claim dated 29 August 2016 (three days after the Supreme Court revoked leave) for filing and the Commissioner of Inland Revenue ("the Commissioner"), at the request of the registry, filed a memo setting out the procedural history.

On 13 September 2016 Faire J issued a minute noting that no application under rule 2.11 of the High Court Rules 2016 ("HCR") had been filed seeking to review the registry's acceptance of the document for filing. Faire J directed that any challenge would presumably have to be made as either an application for summary judgment under Part 12 of the HCR or strike out under Part 15. The Commissioner filed an application under r 2.11 of the HCR for review of the Registrar's decision to accept Dr Muir's amended statement of claim for filing.

Hillvale did not appeal the 22 April 2015 strike out decision, was not a party of Faire J's minute of 13 September 2016 and took no further action until it attempted to file an amended statement of claim on 22 March 2017. This was initially accepted by the registry but then later rejected and the filing fee returned. Hillvale filed an application under r 2.11 of the HCR to review the decision to reject its amended statement of claim for filing.

Decision

The Court canvassed the general principles relating to rr 2.11 and 15.1 of the HCR and the Court's inherent jurisdiction to review the acceptance of a document for filing.

Toogood J concluded that Dr Muir's amended statement of claim was an abuse of process and the filing was a nullity considering the proceeding had been struck out. For the same reasons, Hillvale's tendering of its amended statement of claim was an abuse of the Court's process.

The status of the proceeding

Toogood J was satisfied that the tax challenge proceedings were brought to an end when Faire J struck them out on 22 April 2015. His Honour reiterated that Dr Muir was initially granted leave to the Supreme Court but after he attempted to argue new grounds, leave was revoked with the Supreme Court stating that the "appellant's proceedings will remain struck out in their entirety" (*Muir v Commissioner of Inland Revenue* [2016] NZSC 113, (2016) 27 NZTC 22-067 at [11]).

Associate Judge Bell considered the same issue in relation to the same struck out proceedings in a decision granting the Commissioner summary judgment against Dr Muir where his Honour stated (*Commissioner of Inland Revenue v Muir* [2017] NZHC 1413 [44]):

> "…once a proceeding is at an end it is not possible to file fresh pleadings in the same proceeding to resume the litigation. That applies to both a judgment on the merits and to a decision to terminate on other grounds."

Is a decision to accept a document for filing reviewable under HCR 2.11?

Toogood J agreed that a decision to accept a document for filing was not reviewable under r 2.11 of the HCR. A decision to accept a document for filing does not amount to a Registrar's exercise of jurisdiction in terms of r 2.11(1)(a). The term "exercise of jurisdiction" takes its meaning from rr 2.5 – 2.10 immediately preceding it and refers to the jurisdiction of the Registrar to make certain decisions that would otherwise be made by a Judge or Associate Judge.

Toogood J noted that accepting a document for filing is routinely the task for front-line staff members under the supervision and guidance of Deputy Registrars and does not fall within the jurisdiction referred to in r 2.11(1)(a) of the HCR.

Is the Court's inherent jurisdiction available to review the acceptance of a document for filing?

The Commissioner's primary submission was that there was no longer any proceeding in existence in which an amended statement of claim could have been filed and therefore the Registrar should have rejected the document. No particular application (such as strike out or judicial review) is required because an error by registry staff is not capable of creating jurisdiction to accept a document for filing. The Court can rectify such an error by invoking its inherent jurisdiction to prevent abuses of its process.

Toogood J noticed that it was not clear that Faire J turned his mind to the Court's inherent jurisdiction and he respectfully disagreed with Faire J's view that it was necessary for the Commissioner to apply for summary judgment or a strike out order.

Citing *Re Rafiq* ([2014] NZHC 2291 at [11]), Toogood J confirmed that the Court retains an inherent jurisdiction pursuant to which it has a duty to strike out pleadings that are an abuse of process. If a registry officer accepts a document for filing after the proceeding has been concluded, the acceptance is a nullity. It is also clear that filing a document which purported, misleadingly, to amend a pleading in a proceeding which had been brought to an end constitutes a collateral attack on the decisions of the High Court, Court of Appeal and Supreme Court and was an abuse of the Court process. The Court has an independent duty to prevent abuse of process and a broad inherent procedural power to strike out proceedings where litigation amounts to an abuse of process.

Toogood J considered the Commissioner adopted the appropriate course of filing a memorandum drawing the Court's attention to the registry officer's error and that it was not in the interests of justice to require a formal summary judgment or strike-out application.

Hillvale's arguments

The Court accepted that Dr Muir and Hillvale were separate parties and that not every decision or judgment against Dr Muir would bind Hillvale. However Hillvale was a party to the Trinity litigation which was struck out by Faire J on 22 April 2015 and Hillvale chose not to appeal that strike out decision. The Registrar was right to reject the document, notwithstanding the earlier decision by a registry officer that it should be accepted, because the filing was a nullity and an abuse of the Court's procedure.

The High Court directed that Dr Muir's statement of claim be removed from the Court file and any filing fee returned and dismissed Hillvale's application to review the Registrar's refusal to file its document.

Commissioner granted unless order for security for costs

Case	Peter William Mawhinney as Trustee of the Forest Trust v The Commissioner of Inland Revenue [2017] NZHC 2195
Decision date	8 September 2017
Act(s)	High Court Rules 2016, r 7.48(2)
Keywords	"Application for unless order", High Court Rule 7.48(2), security for costs

Summary

This proceeding concerns the non-payment of a security for costs order. The Commissioner of Inland Revenue ("the Commissioner") sought orders that unless the plaintiff pays the $40,000 security for costs within 14 days, his claim will be struck out. The Court granted the Commissioner's application but gave the plaintiff 30 days to pay the security for costs.

Impact

The Court will grant an unless order where there has been a reasonable time within which to comply with an order to provide security for costs. The failure to comply with the security for costs order has caused delays and is at odds with the clear public interest in ensuring the just, speedy and inexpensive determination of a proceeding.

Facts

In July 2012, Mr Mawhinney as trustee of the Forest Trust ("the Trust") sought damages of over $5m from the Commissioner after she disallowed a goods and services tax ("GST") refund of approximately $67,000. Mr Mawhinney also filed an application for summary judgment seeking approximately $600,000 for GST refunds withheld by the Commissioner.

The Commissioner applied for security for costs of $40,000 and sought that the proceedings be stayed until the sum was paid or security was given. On 4 July 2014, Associate Judge Christiansen granted that order and held that the amount sought was reasonable and could not be said to stop Mr Mawhinney from pursuing the claim. On 3 December 2014 Brewer J upheld the decision on review.

The proceeding has been stayed since the order made by the Associate Judge in 2014. The current application for an unless order was filed and served on 16 May 2017.

Mr Mawhinney's Affidavits

The Commissioner objected to three of Mr Mawhinney's affidavits being read. Those affidavits were originally served as unsworn affidavits, outside the Court ordered deadline, and shortly before the initial hearing of the application. The initial hearing, however, was adjourned due to a power cut.

The Court considered that the Commissioner has now had the opportunity to read and consider the affidavits which were subsequently served in sworn form. Her Honour noted that the application was for an order which, if granted, would likely result in the proceeding being struck out. She concluded that there is no prejudice to the Commissioner and the interests of justice weigh in favour of permitting the affidavits to be read.

Decision

The Court set out the principles in *SM v LFDB* ([2014] NZCA 326, [2014] 3 NZLR 494 at [31]) which apply to unless orders:

- An unless order is an order of last resort and will be granted where there is a history of failure to comply with earlier orders.
- An unless order should clearly set out when and what is the sanction for non-compliance.
- The sanction will apply without further order if the party in default does not comply with the order by the time specified. The party in default may seek relief by application to the Court.
- The party should not assume that belated compliance of the order will suffice. Justice may require that the party in default be relieved if the Court is satisfied that the breach resulted from something for which the party should not be held responsible.
- Where the unless order has deliberately been breached, it will be difficult in the interests of justice to grant that person relief from the order.
- When deciding whether to excuse a breach of an unless order a Judge must ask what does justice demand in the circumstances of this case? Matters to consider when deciding this include public interest in the administration of justice without unnecessary delays and costs, the interests of the injured party to minimise delay and wasted costs, and injustice to the defaulting party but this carries less weight than other considerations.

A plaintiff must be given a reasonable opportunity to comply with an order for security for costs before a proceeding is struck out.

Analysis

The proceeding has been stayed for over three years and the Court stated this is a reasonable time within which to comply with an order to provide security for costs.

The Court considered that the delay in the proceeding is prejudicing the Commissioner as the events took place in 2009 and it is difficult for staff to recall key events in the proceeding. The Commissioner also needs to maintain staff or employ additional staff should the proceeding move forward.

The Court stated that Mr Mawhinney's failure to comply with the security for costs order has caused delays and is at odds with the clear public interest in ensuring the just, speedy and inexpensive determination of a proceeding.

The Court was not convinced that Mr Mawhinney will have funds available to him through the sale of logs in April 2018 in order to vary the order in the future. There was no evidence produced to substantiate his claim. There is current litigation about whether the logs may be harvested without a resource consent and the Court was unconvinced that the harvesting of smaller areas as of right would return the amounts submitted by Mr Mawhinney.

The Court stated that it seems unlikely that there are other avenues of funds available to Mr Mawhinney. The Court was not persuaded that litigation between another trust associated with Mr Mawhinney and the Commissioner will result in any source of funds being available in the short term, and noted that there is no undertaking or legally enforceable agreement by which this other trust agreed to advance sums to Mr Mawhinney.

The Court also took into account that Mr Mawhinney's claim had been assessed as weak by the judges involved in earlier decisions relating to security for costs.

The order to provide security for costs strikes a balance between the rights of plaintiffs to bring and progress their proceeding, and the rights of defendants to be protected from unmeritorious claims brought by impecunious plaintiffs. On balance, the Court held the interests of justice require Mr Mawhinney to be afforded one final opportunity to pay the security for costs order or have his claims struck out.

Result

The unless order is granted; unless the plaintiff pays the security for costs in the sum of $40,000 into Court within 30 days from the date of this judgment, the plaintiff's proceedings will be struck out.

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