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TAX INFORMATION Bulletin

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YOUR OPPORTUNITY TO COMMENT

Inland Revenue regularly produces a number of statements and rulings aimed at explaining how taxation law affects taxpayers and their agents. Because we are keen to produce items that accurately and fairly reflect taxation legislation and are useful in practical situations, your input into the process, as a user of that legislation, is highly valued.

You can find a list of the items we are currently inviting submissions on as well as a list of expired items at **www.ird.govt.nz/public-consultation**

Email your submissions to us at **public.consultation@ird.govt.nz** or post them to:

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

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IN SUMMARY

Binding rulings

Public ruling BR Pub 17/01: Income tax – treatment of unclaimed amounts of $100 or less and Public ruling BR Pub 17/02: Income tax – treatment of unclaimed amounts of $100 or less – amounts held on trust 2

These public rulings and commentary are a reissue of BR Pub 13/03 and BR Pub 13/04 which provided guidance on when amounts of unclaimed money of less than $100, received in the course of business, are derived as income. The rulings are due to expire at the end of the 2016/2017 income year. The only significant change is that they will be reissued on an indefinite basis. There have been some relatively minor updates to the rulings and commentary but the effect of the rulings remains the same.

Product ruling BR Prd 16/11: Reach Media New Zealand Limited 19

This product ruling applies to the engagement of distributors by Reach Media to physically deliver unaddressed mail (newspapers, circulars, leaflets, brochures, catalogues, advertising material, samples and other similar items) from drop-off locations to households and other premises throughout New Zealand.

Product ruling BR Prd 16/12: Reach Media New Zealand Limited 23

This product ruling applies to the engagement of drivers by Reach Media to transport unaddressed mail (newspapers, circulars, leaflets, brochures, catalogues, advertising material, samples and other similar items) from Reach Media's premises to a number of pre-determined drop-off locations.

Product ruling BR Prd 16/13: Reach Media New Zealand Limited 27

This product ruling applies to the engagement of supervisors by Reach Media to oversee the delivery of unaddressed mail (newspapers, circulars, leaflets, brochures, catalogues, advertising material, samples and other similar items) by distributors in a defined area and complete related tasks.

Legislation and determinations

National standard costs for specified livestock determination 2017 31

This determination is made in terms of section EC 23 of the Income Tax Act 2007. It shall apply to any specified livestock on hand at the end of the 2016-2017 income year where the taxpayer has elected to value that livestock under the national standard cost scheme for that income year.

Legal decisions - case notes

Taxation Review Authority finds sale of business took place at value stated by taxpayer and sets aside Commissioner's reassessments 33

The Taxation Review Authority has found that the sale of a business by the sole trader disputant to his company was in 2002 for the amount stated by the taxpayer. The taxpayer was reassessed by the Commissioner of Inland Revenue on the basis the credits to his current account were deemed dividends and shortfall penalties were also imposed. The reassessments and shortfall penalties were set aside.

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**

BR Pub 17/01: Income tax - treatment of unclaimed amounts of $100 or less

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

Taxation Laws

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

This Ruling applies in respect of s CB 1.

The Arrangement to which this Ruling applies

The Arrangement is the receipt by a holder of an amount of $100 or less:

- to which the proviso to s 4(1) of the Unclaimed Money Act 1971 applies; and
- that is received by the holder in the ordinary course of carrying on its business (and, therefore, is not capital in nature).

The Arrangement does not include amounts while they are held on trust for the owner.

For the purposes of this Ruling, the terms "owner" and "holder" have the same meanings as under ss 2 and 5 of the Unclaimed Money Act 1971.

For the purposes of this Ruling, the term "business" has the same meaning as under s YA 1.

How the Taxation Law applies to the Arrangement

The Taxation Law applies to the Arrangement as follows:

- The amount will be income derived under s CB 1 when it:
  - has been applied by the holder for its own benefit (or for the benefit of any other person or for any purpose or object); and
  - is probable that the amount will not have to be repaid to the owner.

The period or tax year for which this Ruling applies

This Ruling will apply for an indefinite period from the first day of the 2017/18 income year.

This Ruling is signed by me on 30 January 2017.

Susan Price
Director, Public Rulings

BR Pub 17/02: Income tax - treatment of unclaimed amounts of $100 or less - amounts held on trust

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

Taxation Laws

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

This Ruling applies in respect of s CB 1.

The Arrangement to which this Ruling applies

The Arrangement is the receipt by a holder of an amount of $100 or less to which the Unclaimed Money Act 1971 applies that is:

- received by the holder in the ordinary course of carrying on its business (and, therefore, is not capital in nature); and
- held on trust for the owner and has not been derived beneficially by the holder.

For the purposes of this Ruling, the terms "owner" and "holder" have the same meanings as under ss 2 and 5 of the Unclaimed Money Act 1971.

For the purposes of this Ruling, the term "business" has the same meaning as under s YA 1.

How the Taxation Law applies to the Arrangement

The Taxation Law applies to the Arrangement as follows:

- The amount will not be income derived under s CB 1 for the holder while it is held on trust for the owner.

The period or tax year for which this Ruling applies

This Ruling will apply for an indefinite period from the first day of the 2017/18 income year.

This Ruling is signed by me on 30 January 2017.

Susan Price
Director, Public Rulings

Commentary on Public rulings BR Pub 17/01 and BR Pub 17/02

This commentary is not a legally binding statement. The commentary is intended to help readers understand and apply the conclusions reached in Public Rulings BR Pub 17/01 and BR Pub 17/02 (the Rulings).

Legislative references are to the Income Tax Act 2007 unless otherwise stated. Relevant legislative provisions are reproduced in the appendix to this commentary.

Summary

1. BR Pub 17/01 and BR Pub 17/02 are reissues of BR Pub 13/03 and BR Pub 13/04, which expire at the end of the 2016/17 income year. The effect of these Rulings is the same as the effect of BR Pub 13/03 and BR Pub 13/04.
2. Many businesses hold money that is owing to another person. In New Zealand, the Unclaimed Money Act 1971 (UMA 1971) sets out rules that apply to holders of unclaimed money. Generally, after a certain period, unclaimed money becomes payable to the Commissioner of Inland Revenue. However, the amount ceases to be unclaimed money (although the owner of the money may still be entitled to repayment) where the amount of unclaimed money:
   - does not exceed $100 per owner (the person entitled to the money); and
   - is applied by the holder for their own benefit (or for the benefit of any other person or for any purpose or object) within prescribed timeframes (6 years or 25 years).

   If the holder does not apply the amount for its own benefit, that amount will continue to be unclaimed money and will be payable to the Commissioner of Inland Revenue after 6 years or 25 years.
3. At issue is the tax treatment of these amounts; in particular, whether and when they can be business income of a taxpayer.
4. For amounts of unclaimed money of $100 or less, it is concluded that while money is held on trust and cannot be (and has not been) applied by the holder for their own benefit (or for the benefit of any other person or for any purpose or object) it cannot be income of the holder. These amounts remain subject to the UMA 1971 and must be paid to the Commissioner within the specified timeframes.
5. An unclaimed amount (of $100 or less) not held on trust will be derived when it:
   - has been applied by the holder for its own benefit (or for the benefit of any other person or for any purpose or object); and
   - is probable that the amount will not have to be repaid (this would include situations that mean the amount is not legally recoverable – for example, a contractual term or limitation period).
6. Whether it is probable that an amount will not be repaid will depend on the particular business. Business records and accounting treatment are likely to be relevant to determining this.
7. If a holder has recognised a previously unclaimed amount as income and subsequently returns that amount to the owner, the holder will be entitled to a deduction under s DA 1(b).

Background

8. Some doubt exists about the correct tax treatment of unclaimed amounts. BR Pub 13/03 and BR Pub 13/04 were issued to set out the Commissioner's view on the correct tax treatment of amounts under $100.
9. These current Rulings (BR Pub 17/01 and BR Pub 17/02) are reissues of BR Pub 13/03 and BR Pub 13/04. They are intended to provide on-going certainty, so have been issued for an indefinite period.

Application of the legislation

10. The following analysis starts with a summary of the provisions of the UMA 1971. It then considers relevant case law on the timing of derivation of income and a line of United Kingdom (UK) cases that look at when unclaimed money will be trading profits of the holder.

Summary of Unclaimed Money Act 1971

11. Section 4(1)(a)–(d) of the UMA 1971 defines amounts that are "unclaimed money". This section includes specific types of amounts that are unclaimed money and the period (6 years or 25 years) after which the amounts become unclaimed money.

12. Section 4(1)(e) of the UMA 1971 sets out a general catch–all provision. Broadly, any money that has been owing by any holder for 6 years immediately following the date on which the money has become payable by the holder will be "unclaimed money".

13. The proviso to s 4(1) of the UMA 1971 states:

    Provided that money of any of the kinds referred to in this subsection shall cease to be unclaimed money where—

    (i) in respect of any one owner it does not exceed $100 in total; and

    (ii) before the 1st day of June next succeeding the end of the period of 6 years or, as the case may be, 25 years specified in this subsection, that unclaimed money is, without limiting any claim any owner may have thereto, applied by the holder for his own benefit or for the benefit of any other person or for any purpose or object.

14. Consequently, an amount will cease to be unclaimed money where it does not exceed $100 and it is applied for the benefit of the holder (or for the benefit of any other person or for any purpose or object) within the prescribed timeframes. However, this does not affect any claim that the owner of the money may have against the holder for repayment.

15. Section 4(2) of the UMA 1971 also excludes certain amounts from being unclaimed money. These amounts include certain dividends, rebates payable by a mutual society, and benefits payable from any pension or superannuation fund.

16. "Holder" is widely defined in s 5 of the UMA 1971. The term includes any company incorporated in New Zealand and any company or bank carrying on business in New Zealand. It also includes certain holders (who are not companies) who are obliged to account for only particular kinds of unclaimed money (for example, auctioneers for the balance of any proceeds of goods sold at auction and real estate agents for money held in the real estate agent's trust account).

17. Other persons may elect to be holders and comply with the UMA 1971.

18. The UMA 1971 imposes certain obligations on holders of unclaimed money. These obligations include:

    - keeping a register of unclaimed money in accordance with s 6 of the UMA 1971;
    - notifying owners and the Commissioner of entries in the unclaimed money register in accordance with s 7 of the UMA 1971;
    - paying the unclaimed money to the Commissioner in accordance with the period specified in s 8 of the UMA 1971 (at this time the holder is relieved of all further liability to any claimant for the money).

    Failure to comply with these obligations is an offence (s 13 UMA 1971).

19. At issue is the tax treatment of amounts that come within the proviso to s 4(1) of the UMA 1971; in particular, whether these amounts can be business income of a taxpayer. These are amounts that would, in the absence of the proviso, be unclaimed money (and the holder subject to the obligations outlined above). Instead, where an amount does not exceed $100 and it is applied for the benefit of the holder (or for the benefit of any other person or for any purpose or object) within the prescribed timeframes, it will cease to be unclaimed money. Therefore, the UMA 1971 will no longer apply to it.

When an amount will be business income

20. Section CB 1 provides:

    CB 1 Amounts derived from business

    Income

    (1) An amount that a person derives from a business is income of the person.

    Exclusion

    (2) Subsection (1) does not apply to an amount that is of a capital nature.

21. An amount will be income where it is "derived" from a business. The following discussion applies where:

    - a taxpayer is carrying on a business;
    - the amounts in question are received in the ordinary course of that business;
    - the amounts are not capital in nature; and
    - no specific timing regime applies to deem derivation to be at a particular time.

22. Case law has established two main methods of recognising income for tax purposes: the cash or receipts method and the accruals or earnings method. The accruals method is generally the most appropriate one for calculating business income. This usually requires the realisation of income on the basis of ordinary commercial principles (unless a more specific provision of the Act applies).

23. It is possible that derivation could occur on receipt or at some point following receipt or that derivation might never occur. Determining the correct point in time requires consideration of the case law on the meaning of derivation.

24. The leading case in this area is *Arthur Murray (NSW) Pty Ltd v FCT* (1965) 114 CLR 314. In *Arthur Murray*, the taxpayer carried on a business of giving dancing lessons. Courses of tuition were available for 5, 15 or 30 hours of private tuition to be taken within a year. Some students contracted for 1,200 hours of tuition to be taken at any time during the student's lifetime. Payment for a course of lessons was often made in advance. The students were given no contractual right to a refund (the terms of the contract prohibited it). However, refunds were sometimes given. The taxpayer argued that fees received in advance of tuition were not taxable income at the time of receipt. The court agreed, finding (at 318) as follows:

> [Income] refers to amounts which have not only been received but have "come home" to the taxpayer; and that must surely involve, if the word "income" is to convey the notion it expresses in the practical affairs of business life, **not only that the amounts received are unaffected by legal restrictions, as by reason of a trust or charge in favour of the payer-not only that they have been received beneficially**-but that the situation has been reached in which they may properly be counted as gains completely made, so that there is neither legal nor business unsoundness in regarding them without qualification as income derived.
>
> **The ultimate inquiry in either kind of case, of course, must be whether that which has taken place, be it the earning or the receipt, is enough by itself to satisfy the general understanding among practical business people of what constitutes a derivation of income.** A conclusion as to what that understanding is may be assisted by considering standard accountancy methods, for they have been evolved in the business community for the very purpose of reflecting received opinions as to the sound view to take of particular kinds of items.
>
> …
>
> Likewise, as it seems to us, in determining whether actual earning has to be added to receipt in order to find income, **the answer must be given in the light of the necessity for earning which is inherent in the circumstances of the receipt. It is true that in a case like the present the circumstances of the receipt do not prevent the amount received from becoming immediately the beneficial property of the company; for the fact that it has been paid in advance is not enough to affect it with any trust or charge, or to place any legal impediment in the way of the recipient's dealing with it as he will.** But those circumstances nevertheless make it surely necessary, as a matter of business good sense, that the recipient should treat each amount of fees received but not yet earned as subject to the contingency that the whole or some part of it may have in effect to be paid back, even if only as damages, should the agreed quid pro quo not be rendered in due course. **The possibility of having to make such a payment back** (we speak, of course, in practical terms) **is an inherent characteristic of the receipt itself**. In our opinion it would be out of accord with the realities of the situation to hold, while the possibility remains, that the amount received has the quality of income derived by the company. **For that reason it is not surprising to find, as the parties in the present case agree is the fact**, that according to established accountancy and commercial principles in the community the books of a business either selling goods or providing services are so kept with respect to amounts received in advance of the goods being sold or of the services being provided that the amounts are not entered to the credit of any revenue account until the sale takes place or the services are rendered: in the meantime they are credited to what is in effect a suspense account, and their transfer to an income account takes place only when the discharge of the obligations for which they are the prepayment justifies their being treated as having finally acquired the character of income. [Emphasis added]

25. Several New Zealand cases have followed *Arthur Murray*. *Arthur Murray* was cited with approval in *A Taxpayer v CIR* (1997) 18 NZTC 13,350 (CA) in relation to the principle that an amount needs to be received beneficially by the taxpayer before it will be derived.

26. Recently the Court of Appeal in *Sovereign Assurance Co Ltd v Commissioner of Inland Revenue* [2013] NZCA 652 relied on the principles in *Arthur Murray* as to when an amount is derived. The Court of Appeal focused narrowly on the aspect of *Arthur Murray* addressing when income was derived through being "earned" rather than any issues as to beneficial entitlement.

27. *Sovereign Assurance* is complex and involved insurance and re-insurance. The taxpayer was an insurance company that entered into agreements with well-resourced reinsurers where it ceded or passed on most of its insured risks. The parties also employed a financing mechanism where the reinsurers agreed to make advances to the taxpayer by paying commissions on policies ceded under the treaties, and the taxpayer agreed to pay the reinsurers commission repayments in amounts equal to the commission payments plus an interest component. The Court of Appeal considered the real focus of the taxpayer's appeal was whether the commission payments the reinsurer made were income in the taxpayer's hands.

28. The Court of Appeal considered that the contractual obligations between the taxpayer and the reinsurer meant the taxpayer was not entitled to retain the commission as its own without repaying the reinsurer an equivalent amount (together with interest). Accordingly, the court considered the commissions were not "earned" because they were received conditionally and were subject to an obligation to be repaid. Therefore, the commission payments were not derived as income.

29. In *CIR v Molloy* (1990) 12 NZTC 7,146 (HC) the taxpayer was a life insurance agent. He received commissions in advance subject to terms requiring repayment if the policy was terminated within a certain timeframe. The court found that the commissions were not income at the time of receipt. Thomas J stated at 7,152:

> In my view the advances made to the agent by the company in this case on account of commission do not have the quality of income derived by the agent at the time of receipt. **The possibility or inherent risk that such advances may have to be repaid (only about 5% in the case of the respondent but up to 30% on average for the company's agents as a whole) is significant, and it is an integral part of the advance, or the receipt of the advance, itself.** For the very good reason that the company wishes to provide an incentive for the agent to solicit soundly based business and then, if necessary, work to ensure that the policies entered into are sustained for a sufficient period to ensure that they are viable, the arrangement contemplates that he will not have earned his commission unless the policy remains in force for two years.
>
> In my opinion, it is these factors which deprive the advances made from having the quality of income earned and derived by the agent at the time they are received. [Emphasis added]

30. *Bowcock v CIR* (1981) 5 NZTC 61,062 concerned an employee who took study leave. Under the terms of the arrangement, the taxpayer received his normal salary. If he left his employment within a certain time after finishing his course, some of the money had to be repaid. The taxpayer did leave his employment and had to repay certain amounts. He claimed that these amounts were never part of his income. The court distinguished *Arthur Murray*, finding that the amounts became the absolute property of the taxpayer when they were paid. Whether any liability arose in the future to repay any part of the money depended entirely on the course the objector chose to take.

31. The principles from *Arthur Murray* were also applied in *Case N30* (1991) 13 NZTC 3,266 (TRA). The taxpayer in *Case N30* carried on a courier business. As part of its business, the taxpayer sold pre-paid books of tickets of varying denominations. The tickets had no expiry date. There was no contractual right to a refund, although the taxpayer would usually give a refund for unused tickets if asked. Some of the tickets were never redeemed. Amounts received were not returned as income when they were received, but were returned as income when they were redeemed. It was agreed that this was generally the appropriate tax treatment. At issue was the treatment of amounts that were never redeemed and whether these should be returned as income. It was accepted that the amount could not be accurately calculated. Judge Bathgate held that when the taxpayer could say as a matter of probability that a ticket would not be redeemed, the amount should be included as income.

32. The taxpayer in *A Elson (Inspector of Taxes) v Prices Tailors Ltd* [1963] 1 All ER 231 (ChD) carried on business as a tailor. When a customer placed an order they were required to pay a deposit. If, subsequently, the customer declined to take the garment, the taxpayer would refund the deposit (although contractually it did not have to do so). However, often neither the garment nor the deposit was claimed. At issue was whether the unclaimed deposits were trading receipts in the year in which they were paid.

33. The court found that the payments were true deposits, rather than part-payments (as the taxpayer had argued). Consequently, the amounts belonged to the taxpayer at the time they were paid (as there was no legal requirement to refund them). The court went on to find that the deposit amounts were trading receipts in the year in which they were received. That the taxpayer would always refund the amounts if asked did not change this.

34. It might be suggested that the decision in *Prices Tailors* is inconsistent with the decision in *Arthur Murray*. *Prices Tailors* concerned a deposit towards a supply of goods, and the court held that the deposit was derived when it was received. On the other hand, *Arthur Murray* concerned a full payment for the provision of services in the future, and the court held that the amount was not derived until the services had been performed. The cases are consistent in that they both look at the legal obligations (the amounts paid were non-refundable) rather than what happened in practice. However, *Prices Tailors* did not appear to consider the fact that, at the time the deposit was paid, the taxpayer had not fulfilled the requirements of the contract (that is, making the suit available to the taxpayer).

Summary of principles from the cases

35. The following principles can be taken from the above cases:

- The word "income" conveys the notion it expresses in the practical affairs of business life. It is necessary to ask whether what has taken place is enough by itself to satisfy the general understanding among practical business people of what is derivation of income.
- An amount will be income when the earning process is complete. In the case of prepaid services, this will usually be when the services have been performed.
- Where it is probable that the services will not have to be performed and the amount will not have to be repaid, then the amount should be income.

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- It is necessary to consider the circumstances of receipt. For example, whether the amount is subject to a contingency of repayment is a relevant factor. Similarly, for an amount to be derived it must have been beneficially received by the taxpayer (that is, not be subject to a legal restriction such as a trust or charge that prevents the taxpayer dealing with the amount in their own interests).

United Kingdom cases

36. Several UK cases consider whether (and when) amounts received by taxpayers that may be subject to repayment are trading receipts that should be taken into account in calculating the taxpayer's profits.

37. *Lincolnshire Sugar Co Ltd (in liquidation) v Smart (HMIT)* [1937] 1 All ER 413 (HL) considered "advances" payable by the Government to sugar manufacturers. The advances became repayable in the event of imported sugar rising to a certain price or in certain other events such as a winding-up of the company. The advances were included as a liability in the company's balance sheet. No part of the advances ever became repayable. The issue was whether the advances were trading receipts of the company in the year they were received. The company contended that the advances were not trading receipts or, if the advances were trading receipts, they could not be brought into account as such, so long as they remained subject to repayment.

38. Lord MacMillan concluded that the amounts were trading receipts. The fact the payments were called advances and were repayable if certain contingencies occurred was not decisive; rather, Lord MacMillan was influenced by the fact the payments were made to the company so the money could be used in its business.

39. *Morley (Inspector of Taxes) v Tattersall* [1938] 3 All ER 296 (CA) involved a firm of auctioneers. Its conditions of sale provided that vendors should receive the purchase money following the sale and that no money would be paid without a written order. As a result of the operation of these conditions, large sums of money sometimes remained unclaimed in the hands of the firm. When a new partner was admitted in 1922, an amount for unclaimed balances for years before 1908 was transferred to the capital account of the old partner. In 1935, when another partner was admitted, an amount for unclaimed balances between 1922 and 1928 was transferred in part to the current accounts and in part to the capital accounts of the former partners. A partnership deed in 1936 provided that such liability as subsisted in respect of those sums should be assumed by the partnership and that such unclaimed balances as first arose six years before the taking of each annual account should be transferred at such account to the credit of the partners in accordance with their shares in the partnership. The partnership deed further provided that all liability in respect of the unpaid amounts should be borne by the partnership.

40. Sir Wilfrid Greene MR noted that the Statute of Limitation had not started to run for the balances. Therefore, the taxpayer was still obliged to make payment to a customer at any time if requested (at 298):

> Many of those balances have remained unclaimed for a considerable number of years, but the Solicitor-General quite properly admitted that the vendors in question were entitled to claim payment of their money at any time, unaffected by the Statute of Limitation, which has not yet begun to run, owing to the absence of any written order as required by the conditions. We are dealing, therefore, with obligations which, as a matter of law, are existing obligations, which the firm can be called on to perform at any moment. That is a matter not without importance in the examination of this case.

41. Sir Wilfrid Greene MR went on to further explain the effect of the agreements between the partners. In particular, he noted that the agreements did not affect the legal position between the clients and the partnership; rather, the agreements related to the accounting treatment of the unclaimed amounts as well as what was, in effect, an indemnity between the partners and the partnership in relation to the amounts (at 300):

> Pausing there for a moment, and eliminating, for the purpose of simplicity, the changes in the partnership agreement, it is of the utmost importance in this case to appreciate the real nature of what was being done. I say that because, in the arguments addressed to us on behalf of the Crown, various metaphorical expressions were used, such as "holding a sum," "changing the capacity in which a sum is held," "turning a sum into an asset," and so forth—expressions which, to my mind, are both inaccurate and misleading. What happened was that the partnership, being indebted to outside persons; in respect of sums which it had received, and which had passed into the general mass of its assets, and having carried in its balance-sheet a proper liability item to express that liability, decided at a certain point, and on certain principles laid down, that that liability item should be written down and diminished. That is what happened in 1921, in 1934, and year by year after the provisions of the new partnership agreement came into operation—merely the alteration of a debit item in the balance-sheet by eliminating from it certain liabilities which had previously gone to make it up. If that matter had stayed there, the only result on the balance-sheet would have been to increase the credit balance. It would have shown a greater surplus of assets over liabilities than it had shown prior to that writing down. It so happened that, for domestic reasons of their own, the partners, instead of leaving the matter in that way, with an increased credit balance, decided that that increase in the credit balance should be carried in the balance sheet to the partners' accounts. That does not alter the reality of the position one jot. **The true position is—and I repeat it, because it is only when that is appreciated that what I, with respect,**

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> **conceive to be the fallacies underlying the Crown's argument are perceived—that the only thing which was done on these occasions was the elimination from the liabilities side of the balance-sheet of something which had previously appeared as a liability therein.** [Emphasis added]

42. It was generally agreed between the parties that the money was not a trading receipt at the time it was received. However, it was argued that the amounts became trading receipts at the time the partners treated the amounts as their own. Sir Wilfrid Greene MR rejected this argument, finding that the writing down of the amount in the balance sheet did not convert that amount to income (at 301):

> It might be more convenient to deal with Mr Hills's argument first, because that is the one which starts off with the perfectly clear admission that the money, when received from the purchasers, was not a trading receipt. That proposition, I should have thought, was, in any case, quite incontestable. **The money received was money which had not got any profit-making quality about it. It was money which, in a business sense, was the clients' money, and nobody else's.** It was money for which Messrs Tattersall were liable to account to the clients, and the fact that Messrs Tattersall paid it into their own account, as they clearly did, and the fact that it remained among their assets until paid out, do not alter that circumstance. It would have been, for income tax purposes, in my judgment, entirely improper to have brought those receipts into the account at all for the purpose of ascertaining the balance of profits and gains. Indeed, as I have said, the Crown did not suggest that that would have been proper. What was said, however, was this. Mr Hills's argument was to the effect that, although they were not trading receipts at the moment of receipt, they had at that moment the potentiality of becoming trading receipts. That proposition involves a view of income tax law in which I can discover no merit except that of novelty. **I invited Mr Hills to point to any authority which in any way supported the proposition that a receipt which at the time of its receipt was not a trading receipt could by some subsequent operation ex post facto be turned into a trading receipt—not, be it observed, as at the date of receipt, but as at the date of the subsequent operation. It seems to me, with all respect to that argument, that it is based on a complete misapprehension of what is meant by a trading receipt in income tax law. No case has been cited to us in which anything like that proposition appears. It seems to me that the quality and nature of a receipt for income tax purposes is fixed once and for all when it is received.** What the partners did in this case, as I have said, was to decide among themselves that what they had previously regarded as a liability of the firm they would not, for practical reasons, regard as a liability. That does not mean, however, that at that moment they received something, nor does it mean that at that moment they imprinted on some existing asset a quality different from that which it had possessed before. There was no existing asset at all at that time. All that they did, as I have already pointed out, was to write down a liability item in their balance-sheet, and how by effecting that operation it can be said that a sum received years ago has been converted into something which it never was is a thing which, with all respect, passes my comprehension. [Emphasis added]

43. *Jay's the Jewellers Ltd v IRC* [1947] 2 All ER 762 (KB) involved the tax treatment of proceeds from the sale of pledged property. The Pawnbrokers Act 1872 required a pawnbroker to hold a pledge for 12 months and 7 days. If the pledged article had not been redeemed by then and the loan was no more than 10s, the pledge became the property of the pawnbroker, who could sell it and keep the proceeds. If the loan exceeded 10s, the pawnbroker was entitled to sell the pledged article by auction and to take the amount of the loan, the interest due and the cost of the sale out of the amount realised. Subject to the terms of any special contract, which were permitted if the loan exceeded 40s, at any time within three years of the sale the pledgor had the right to inspect the pawnbroker's books and demand payment of the surplus. After three years, the pledgor lost that right and the surplus became the property of the pawnbroker. Special contracts entered into by pawnbrokers with pledgors sometimes incorporated the three-year period, but in others a pledgor's rights to redeem were barred only by the ordinary period of limitation, six years.

44. The issue was whether the proceeds from the sales were subject to excess profits tax. The court held that, as a matter of law, the surpluses when received were not the taxpayers' monies at all; they belonged to their clients. Based on *Tattersall*, the court found that the surpluses were not trading receipts in the year that they were received. The court then went on to consider whether a surplus could be treated as a trade receipt in a later year when the taxpayer became entitled to retain it.

45. The court held that a new asset was created automatically by operation of law at the end of the three years (in the case of most of the loans) and common sense would seem to demand that that should be entered in the profit and loss account for the year and be treated as taxable. The court distinguished the decision in *Tattersall* as follows (at 766):

> It is, however, argued that I cannot give effect to that view because of *Tattersall*'s case. Is there anything in *Tattersall*'s case to indicate that that view is wrong? In that case there had been no change whatever in the character and nature of the money held. The Statute of Limitations had not commenced to run, and the court was dealing merely with the effect of a change in the method in which these sums were dealt with in the company's books.
>
> …
>
> Here the position is different. Here, at the end of three years, the money in question, the three-year-old surplus, did attain a totally different quality. I think there was then a definite trade receipt. At the end of the three years a new asset came into existence, an asset which had arisen out of a trade transaction.

46. The court then considered whether the position should be different for pledges that were subject only to the application of a limitation period. The same conclusion was held to apply (at 767):

> The position is somewhat different as to pledges for over £10, because the only change which takes place at the end of six years is that the customer's remedy is barred, but, from the business point of view, I think, it ought to be treated as the same. In practice those amounts would be properly dealt with by the taxpayers as their own. They could not get into difficulties by so doing. They cannot be called on to pay. I do not think any distinction ought to be drawn between the three-yearly surpluses and the six-yearly surpluses, and I am not prepared to differ from the view held by the Special Commissioners. Therefore, both appeals will fail.

47. In holding that the unclaimed deposits were income of the taxpayer in the year received, *Prices Tailors* (see [32]) distinguished *Tattersall* and *Jay's the Jewellers* on the basis that, in those cases, the amounts in question did not belong to the taxpayers (at the time they were received) (at 235):

> In *Morley v Tattersall*, the vendors' unclaimed balances, in the hands of a firm of auctioneers, of proceeds of sale of horses were held not to be trading receipts; and in Jay's, The Jewellers Ltd v Inland Revenue Comrs; Inland Revenue Comrs v Jay's, The Jewellers Ltd, a pawner's unclaimed balance in the hands of a pawnbroker of the proceeds of sale of an unredeemed pledge, after satisfying the amounts due under the pledge, was held not to be a trading receipt until the pawner's claim was statute-barred. **In these cases, the balances in the traders' hands were not theirs at all but were held for others, and this fact is fundamental to the decisions. The traders had no beneficial interest in them at the relevant time, and, although it was because they were traders that they received them, they were not receipts of their trade at all.** [Emphasis added]

48. The taxpayer in *Pertemps Recruitment Partnership Ltd v HMRC* [2010] UKFTT 218 carried on business as a recruitment agent. Sometimes it would receive overpayments from customers (that is, payments of amounts that were not owing). Where these amounts could not be refunded or applied against a later liability, the taxpayer kept the payments. The court found that receipt of mistaken payments was an inevitable incident of the taxpayer's business. The court further found that:

- when the overpayments were deposited in the taxpayer's bank account, the taxpayer did not know that they represented an overpayment;
- the taxpayer treated the overpayments as its own money (that is, the overpayments were not kept in a separate account);
- the taxpayer did not hold the mistaken payments on trust for the customer (*Tattersall* and *Jay's the Jewellers* were distinguished on this basis);
- no limitation period would likely apply to the overpayments; and
- the amounts paid belonged to the taxpayer unless the customer made a successful claim in restitution or the claim was settled by agreement.

49. The court held that the payments were profits from the taxpayer's trade in the year that they were received. The fact the customers had an entitlement to claim the money back did not change this. The tribunal judge stated (at [43]–[44]):

> HMRC's submission, with which we agree, is that an [sic] mistaken payment for services has the same characteristic in the hands of the recipient trader as a payment made not in error – **if the payment is made because the customer makes a mistake about owing something for services or for a trading transaction, the mistaken payment accrues from the trade of the recipient.** This is entirely consistent with the manner in which Pertemps operates its business. At the time payments are deposited into the Pertemps' bank account, it does not distinguish between overpayments and other receipts. Indeed it could not – as Pertemps banks payments before they are allocated to invoices on ledgers. Even if a receipt is eventually determined to be an overpayment, it will often be applied against other invoices rendered to the customer.
>
> … HMRC submit, and we agree, that **the overpayments are a natural consequence of the efficient and lawful way in which Pertemps conducts its business**, and that these processes will mean that **sometimes it makes more money from the supply of its services than it had anticipated**. In doing so, it has supplemented its trading profits, and the receipt is a trading receipt. [Emphasis added]

50. In *Gower Chemicals v HMRC* [2008] UKSPC 713, the taxpayer carried on business selling chemicals. Chemicals were sold in reusable containers. Customers paid a refundable deposit for a container that remained the property of the taxpayer. When a container was returned in good condition and in a reasonable time, the appellant would issue a credit note or refund the deposit. Sometimes containers were returned but the customer never took the credit or refund.

51. At issue was whether the unclaimed deposits were trading income. The Special Commissioners found that the deposits belonged to the taxpayer as soon as they were received and should be brought into income at that point. This was because the taxpayer knew that in the course of its business, 20 percent of the deposits would not have to be repaid. Special Commissioner Dr John Avery Jones stated (at [7]):

> The issue for me turns primarily on the nature of the receipt of the deposit by the Appellant. The Appellant knows that about 20 per cent of deposits will not have to be repaid. In my view this makes it impossible to say that the Appellant is merely holding the deposit for the customer. The straightforward analysis is that the deposit is a trading receipt just as the payment for the goods is a trading receipt but with the difference that about 80 per cent of the deposits will have to be repaid, for which it is right to make a provision. While I agree that factually this distinguishes this case from *Prices Tailors*, I do not consider that this changes anything. In that case the deposit was security for the completion of the garment that the customer had ordered. Deposits were in fact repaid to customers who did not accept the garment even though there was not contractual obligation to do so. The decision relied on *Smart v Lincolnshire Sugar Co* 20 TC 643 in which there was a contractual right to repayment of the deposit if a contingency occurred. The need for a provision for this was discussed in the case and it is recorded in *Prices Tailors* that the same point was raised. In my view the Appellant's past accounting treatment was correct. The deposit belongs to the Appellant as soon as it is received and should be brought into income at that point.

Summary of principles from the United Kingdom cases

52. It may appear that the reasoning in the UK cases is not always consistent. For example, as noted above, in *Tattersall*, the court found that the nature of a receipt for income tax purposes is fixed at the time it is received. However, the court in *Jay's the Jewellers* took the view that a receipt could become income at a later date where its nature was changed by the operation of law.

53. Despite the apparent inconsistencies, it is considered that the above cases can all be reconciled. Where a later case has reached a different view than an earlier case, the later case has refined or expanded the principles set out in the earlier case and adapted them to the facts at issue. Consequently, the following principles can be taken from the above cases:

- Where an amount is no longer liable to be repaid (whether by virtue of contractual terms, limitation or other statute), then it will become income (if it was not previously) (*Jay's the Jewellers*).
- Just because an amount may be subject to repayment does not mean that the amount cannot be income (*Lincolnshire Sugar, Pertemps*).
- When an amount is held on trust for a third party, it will not be income (*Tattersall*).
- Changing the accounting treatment of an amount will not, by itself, make that amount income (*Tattersall*).
- Unsolicited overpayments that a taxpayer treats as their own money belong to the taxpayer unless the customer makes a successful claim (*Pertemps*).
- Unsolicited overpayments and unclaimed refundable deposits are income in the year they are received (*Pertemps, Gower Chemicals*).

Application to unclaimed amounts of $100 or less in New Zealand

54. As noted above, for an amount to be derived it must be received beneficially by the taxpayer (that is, received free from legal impediments to the taxpayer dealing with the money in its own interests). In the context of unclaimed money, this is most likely to give rise to a question of whether an amount is held on trust or not. Therefore, the treatment of money held on trust is considered next.

Money held on trust

55. Most unclaimed money will not be held on trust. For example, where a customer has overpaid an account, the overpayment will not normally be held on trust by the holder. The relationship between a customer and a business will normally be a contractual one. Similarly, the relationship between a bank and depositor will normally be one of debtor–creditor and not trust (see *DFC New Zealand Ltd v Goddard* [1992] 2 NZLR 445). However, in certain circumstances, unclaimed money may be held on trust by the holder. Examples include funds held in a real estate agent's trust account or a solicitor's trust account.

56. A trust will often (but not always) be evidenced by the existence of a trust deed. A trust will be present where the holder holds the unclaimed money for the benefit of a third party (the "owner" for unclaimed money purposes) and cannot deal with the money in their own interests. Therefore, to determine whether an amount is held on trust, it is necessary to look at the terms on which the money was originally paid and on which it is currently held.

57. As noted above, money held on trust is unlikely to be able to be applied by the holder for their own benefit without breaching the terms of the trust. Consequently, the proviso to s 4(1) of the UMA 1971 will not be satisfied and the amounts will be unclaimed money. If s 4(1) is not satisfied, then the amounts cannot be income as they will be subject to the UMA 1971 and must be paid to Inland Revenue within the prescribed timeframes. If, on the other hand, the money is **in fact** applied by the holder for its own benefit, it is unlikely that the holder will be able to show that the money is held on trust (or otherwise not received beneficially).

58. The conclusion that money held on trust cannot be income of the holder is consistent with the case law considered above. None of the cases found that money held on trust could be income of the holder.

59. However, if money ceases to be held on trust (for example, by virtue of the terms of the trust or the application of a statutory provision) and the holder applies it for their own benefit, then s 4(1) of the UMA 1971 could apply and the amount could become income of the holder. In this case, the amount should be treated the same as amounts not held on trust.

Money not held on trust

60. At issue is when (if at all) amounts of unclaimed money applied by the holder for their own benefit will be derived by the holder. As noted above, it is assumed that the amounts are received by the holder in the ordinary course of their business.

61. New Zealand case law on derivation has followed the Australian decision of *Arthur Murray*. Therefore, in New Zealand, income will be derived when what has taken place is enough to satisfy the general understanding among practical business people of what is derivation of income. The UK case law may be of assistance in determining this. However, that case law was not considering the meaning of derivation, so care must be taken when applying the decisions in a New Zealand context.

62. In the case of unclaimed money, it could be argued that derivation occurs on receipt or at some point following receipt or that derivation never occurs. As no New Zealand case law is directly on point, it is necessary to consider the principles taken from the case law to determine how a court might apply them to resolve this issue.

63. Where a contractual or statutory provision (such as the Limitation Act 1950 or Limitation Act 2010) applies so that the holder of money will no longer be required to repay it if requested by the owner, then the amount will be income. This is consistent with the UK case law. It is also consistent with *Arthur Murray* and the New Zealand derivation cases, because the holder has to do nothing further to earn the amount and there is no possibility that the amount will be repayable. However, in many cases of unclaimed money, it is unlikely that the relevant Limitation Act will apply and there will be no contractual terms limiting the holder's liability to repay. Therefore, it is necessary to consider whether these amounts could be income even though they are still subject to the possibility of repayment.

64. As noted above, that an amount may be subject to repayment will not necessarily prevent it being income (see, for example, *Lincolnshire Sugar*, *Pertemps*, *Gower Chemicals*, *Case N30*, *Bowcock*).

65. *Pertemps* is the decision that is closest to the facts being considered. It could be argued that *Pertemps* should be applied in New Zealand, which would lead to the conclusion that (at least in the case of overpayments) the relevant amounts are income when they are received. However, this is not considered the correct approach for two reasons. First, in New Zealand the UMA 1971 potentially imposes some statutory obligations for the amounts until the proviso to s 4(1) applies to exclude the amount from being unclaimed money. Secondly, *Pertemps* is arguably inconsistent with the approach taken in *Arthur Murray* and the subsequent New Zealand cases. This is discussed in more detail from [66] onwards. In summary, it is considered that *Pertemps* provides support for the proposition that the amounts of unclaimed money are in the nature of income. However, it is not considered good authority in New Zealand for **when** that income is derived.

66. It could be argued that the fact (in many cases) the holder will always be liable to repay the relevant amounts to the owner (if asked) means applying *Arthur Murray* would lead to the conclusion that the amounts would never be derived. However, it is considered that the principles from *Arthur Murray* need to be interpreted in the context of the facts in that decision. *Arthur Murray* was considering prepaid services. This meant its analysis was focused on establishing when an amount would be "earned" where there was a future requirement to perform services on request. No consideration was given to what the position would be where there was no (or no longer an) obligation to perform any services.

67. The same point can be made about the decision in *Sovereign Assurance*. The Court of Appeal's reliance on *Arthur Murray* in that case must also be placed in its proper context. The Court of Appeal was solely concerned with whether income was derived through being "earned". However, in the case of unclaimed money the holder will not be providing services (or goods) to the customer. The very nature of an unclaimed amount means it cannot be earned. In this instance, derivation is not triggered when the amount is "earned". On that basis, *Sovereign Assurance* is of limited assistance in considering when derivation occurs for unclaimed amounts.

68. *Case N30* expanded the scope of the principles from *Arthur Murray*.
In *Case N30* income was held to be derived even though the services paid for had not been performed. The earning process was found to be complete once it was probable that the service would not be required to be performed.

69. In the context of an amount of unclaimed money, that amount will not be "earned" in the sense of goods or services being provided for it. However, it is an amount that is received in the ordinary course of the taxpayer's business, and it is being treated by the taxpayer as its own money (in the sense of having been applied for the holder's use). As nothing further needs to be done by the taxpayer to earn the money, the only thing stopping it being derived is the fact it is subject to the contingency of repayment. As time passes, that contingency will become more remote.

70. Once it is probable that the unclaimed amount will not need to be repaid, it should be treated as income. The "probable" threshold is based on the test used in *Case N30*. A different standard may be more appropriate. For example, it could be argued that it is sufficient for an amount to be treated as income where it is "unlikely" that it will need to be repaid. However, on balance, it is considered that the case law better supports the slightly higher "probable" threshold. Practically, there may not be much difference in any event.

71. When it is probable that an amount will not be repaid will depend on the particular business. Business records and accounting treatment are likely to be relevant to determining this. For example, if business records show that once an amount is applied for the benefit of the holder under the proviso to s 4(1) of the UMA 1971, it is probable that it will not be paid back, then this suggests the amount should be returned as income at that time. If, on the other hand, the business records show that even after 10 years, customers still successfully request the return of unclaimed amounts (on more than just isolated occasions), then this may suggest that the amounts should not yet be treated as income. This will be a question of fact to be determined in each case. It is not possible to provide more prescriptive factors.

72. In summary, an unclaimed amount will be derived when it:
    - has been applied by the holder for its own benefit (that is, the proviso to s 4(1) of the UMA 1971 applies); and
    - is probable that the amount will not have to be repaid (which would include situations (described in [71]) when the amount is not legally recoverable; for example, under a contractual term or a Limitation Act).

Amounts subsequently repaid to owners

73. Section DA 1 sets out the general permission for deductibility. In particular, s DA 1(b) allows a deduction for an amount of expenditure to the extent to which it is incurred in the course of carrying on a business for the purpose of deriving assessable or excluded income.

74. The Rulings apply to amounts of unclaimed money that holders receive in the ordinary course of their business. The Commissioner's view is that repayment of these amounts to their owners is also undertaken in the course of the holder's business. Consequently, if a holder subsequently returns an amount that has previously been recognised as income, the holder would be entitled to a deduction under s DA 1(b).

Conclusions

75. For amounts of unclaimed money of $100 or less, while money is held on trust and cannot be (and has not been) applied by the holder for their own benefit (or for the benefit of any other person or for any purpose or object), it cannot be income of the holder. These amounts remain subject to the UMA 1971 and must be paid to the Commissioner within the specified timeframes.

76. An unclaimed amount (of $100 or less) not held on trust will be derived when it:
    - has been applied by the holder for its own benefit (that is, the proviso to s 4(1) of the UMA 1971 applies); and
    - is probable that the amount will not have to be repaid (which would include situations when the amount is not legally recoverable; for example, under a contractual term or a Limitation Act).

77. When it is probable that an amount will not be repaid will depend on the particular business. Business records and accounting treatment are likely to be relevant to determining this.

78. If a holder has recognised a previously unclaimed amount as income and subsequently returns that amount to the owner, the holder will be entitled to a deduction under s DA 1(b).

Example: Unclaimed money not held on trust

79. This example is included to assist in explaining the application of the law.

80. Supaphone Ltd is carrying on business as a telecommunications company. Many of Supaphone's clients pay their accounts by monthly automatic payment. Sometimes when clients close their accounts with Supaphone, they forget to cancel their automatic payments straight away. This results in overpayments to Supaphone. Supaphone attempts to contact customers to return these overpayments, but these customers are often impossible to locate. Supaphone also receives payment by cheque. Sometimes, despite its best attempts, Supaphone cannot match the cheque received with a particular customer's account. In both situations, the amounts received are subject to the UMA 1971.

81. Where unclaimed amounts are $100 or less, Supaphone applies them to its business (within the applicable timeframes) under the proviso to s 4(1) of the UMA 1971. At this time, the amounts are no longer subject to the UMA 1971.

82. Supaphone's business records show that over the past 10 years, repayment requests are made for 50 percent of unclaimed amounts within four years of receipt. However, in the past 10 years only two people have requested the return of unclaimed money more than four years after it was received. Therefore, after four years it is probable that the amount will not have to be repaid.

83. Supaphone asks whether (and when) the unclaimed amounts of $100 or less are business income under s CB 1.

84. The unclaimed amounts are not held by Supaphone on trust. Therefore, the amounts will be income under s CB 1 when they are derived (assuming that no other timing regime applies). The amounts will be derived when:

    - Supaphone applies the amounts to its business under the proviso to s 4(1) of the UMA 1971 (which occurs around six years after receipt); and
    - it is probable that Supaphone will not have to repay the amounts (in this case four years after receipt).

85. As the later of these events is the application of the amounts under the proviso to s 4(1), the amounts are derived and should be returned as business income when Supaphone applies these amounts to its business.

References

Subject references

business income
derivation
unclaimed money

Legislative references

Income Tax Act 2007, s CB 1
Limitation Act 1950
Limitation Act 2010
Unclaimed Money Act 1971, ss 4–8, 13

Case references

A Taxpayer v CIR (1997) 18 NZTC 13,350 (CA)
A Elson (Inspector of Taxes) v Prices Tailors Ltd [1963] 1 All ER 231 (ChD)
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DFC New Zealand Ltd v Goddard [1992] 2 NZLR 445
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Jay's the Jewellers Ltd v IRC [1947] 2 All ER 762 (KB)
Lincolnshire Sugar Co Ltd (in liquidation) v Smart (HMIT) [1937] 1 All ER 413 (HL)
Morley (Inspector of Taxes) v Tattersall [1938] 3 All ER 296 (CA)
Pertemps Recruitment Partnership Ltd v HMRC [2010] UKFTT 218
Sovereign Assurance Co Ltd v Commissioner of Inland Revenue [2013] NZCA 652

Appendix: Legislation

Income Tax Act 2007

1. Section CB 1 provides:

CB 1 Amounts derived from business

Income

(1) An amount that a person derives from a business is income of the person.

Exclusion

(2) Subsection (1) does not apply to an amount that is of a capital nature.

Unclaimed Money Act 1971

2. Section 2 of the Unclaimed Money Act 1971 relevantly provides:

2 Interpretation

In this Act, unless the context otherwise requires,—

…

owner, in relation to any unclaimed money, means the person entitled to the unclaimed money; and includes any other person claiming under or on behalf of that person

…

3. Section 4 of the Unclaimed Money Act 1971 provides:

4 Unclaimed money

(1) Subject to this section, unclaimed money shall consist of—

(a) money, including the interest or any amount in the nature of interest thereon, deposited with any holder so as to bear interest for a fixed term, which has been in the possession of the holder for the period of 6 years immediately following the date of expiry of the term:

(b) money, including the interest or any amount in the nature of interest thereon, deposited with any holder so as to bear interest—

(i) without limitation of time; or

(ii) for a fixed term where, on the expiry of the fixed term, the money, if it is not withdrawn by the customer, is to be treated as reinvested,—

where in either case the customer has not operated on the account for a period of 25 years, whether by deposit, or withdrawal, or instruction in writing:

(c) money deposited upon current account or otherwise with any holder and not bearing interest, where—

(i) in any case where the holder is a savings bank, the customer has not operated on the account for a period of 25 years, whether by deposit, or withdrawal, or instruction in writing; and

(ii) in any other case, the customer has not operated on the account for a period of 6 years, whether by deposit, or withdrawal, or instruction in writing:

(d) money payable or distributable on or in consequence of the maturity of a policy of life assurance, being money which has been in the possession of any holder for the period of 6 years immediately succeeding the date on which—

(i) the policy matured otherwise than by death; or

(ii) the holder first had reason to suppose that the policy has matured by death, whether such death has been legally proved or not,—

whichever date is the earlier, and notwithstanding that by the terms of the policy the money is not payable or distributable except on proof of death, or on proof of age or any other collateral matter:

(e) any other money, of any kind whatsoever, which has been owing by any holder for the period of 6 years immediately following the date on which the money has become payable by the holder:

provided that money of any of the kinds referred to in this subsection shall cease to be unclaimed money where—

(i) in respect of any one owner it does not exceed $100 in total; and

(ii) before the 1 June next succeeding the end of the period of 6 years or, as the case may be, 25 years specified in this subsection, that unclaimed money is, without limiting any claim any owner may have thereto, applied by the holder for his own benefit or for the benefit of any other person or for any purpose or object.

(2) Unclaimed money shall not include—

(a) any dividends, not being dividends payable by a mutual association in relation to money deposited with the association, payable by a company to any of its shareholders:

(b) any rebate payable by a mutual association (other than a holder of the kind referred to in paragraph (f) of subsection (1) of section 5) to any of its members in relation to the trading transactions of the member with the association, not being a rebate payable in relation to money deposited with the association:

(c) any benefits payable from any pension or superannuation fund.

(3) Where a holder has ceased to carry on business or has died, and the holder, or, as the case may be, his personal representative, has for a period of 6 months or more immediately succeeding the date of that cessation or death been in possession of or owed money which has remained unclaimed and—

(a) which would become unclaimed money when the period referred to in the appropriate paragraph of subsection (1) had expired if the money had remained unclaimed; or

(b) which would have so become unclaimed money if it were not money of any of the kinds referred to in subsection (2),—

the holder or that personal representative may, if he thinks fit, pay the money to the Commissioner and furnish to the Commissioner particulars of the payment and of the person on whose behalf the money was held or to whom it was owed; and thereupon that money shall be deemed to be unclaimed money, and the provisions of this Act, as far as they are applicable, shall apply accordingly.

(4) In subsection (2) the expression **mutual association** means any body or association of persons, whether incorporated or not, which enters into transactions of a mutual character with its members, whether or not it also enters into transactions with other persons.

4. Section 5 of the Unclaimed Money Act 1971 provides:

5 Holder

(1) This Act shall apply to unclaimed money held or owing by the following holders:

(a) any company incorporated in New Zealand and any liquidator or receiver of any such company:

(b) any company incorporated out of New Zealand and carrying on business in New Zealand, and any liquidator or receiver of any such company:

(c) any bank, including a savings bank, carrying on business in New Zealand:

(d) any building society within the meaning of the Building Societies Act 1965:

(e) any person, firm, body, or institution carrying on the business of borrowing and lending money in New Zealand, in respect of money borrowed:

(f) any insurance office or company carrying on business in New Zealand, including the Government Life Insurance Corporation:

(g) any person registered as an auctioneer under the Auctioneers Act 2013:

(h) any agent within the meaning of the Real Estate Agents Act 2008, whether or not a company, in respect of money held in a trust account:

(ha) any conveyancing practitioner within the meaning of the Lawyers and Conveyancers Act 2006, in respect of money held in a trust account:

(i) any sharebroker within the meaning of the Sharebrokers Act 1908, whether or not a company, in respect of money held on behalf of clients:

(j) any qualified statutory accountant (within the meaning of section 5(1) of the Financial Reporting Act

2013) in respect of money held on behalf of clients:

(k) any motor vehicle trader within the meaning of the Motor Vehicle Sales Act 2003, whether or not a company, for money held on behalf of any person for whom the trader has acted as agent in the course of carrying on the business of motor vehicle trading.

(2) Any person, firm, body, or institution may elect to be the holder in respect of such money held or owing by him or it as he or it thinks fit, not being—

(a) unclaimed money in respect of which he or it is the holder under subsection (1) of this section; or

(b) except where subsection (3) of section 4 of this Act applies, money to which subsection (2) of that section applies;—

and in that case he or it shall be deemed to be the holder in respect of that money.

5. Section 6 of the Unclaimed Money Act 1971 provides:

6 Register to be kept

(1) Every holder shall, on 1 June in each year, enter in an alphabetical register, to be kept at the head or principal office in New Zealand of the holder, in the form prescribed in the Schedule to this Act, particulars of unclaimed money arising on or after 1 June in the preceding year; and from and after 8 June in each year that register shall be open to the inspection of all persons at that head or principal office during the hours within which the ordinary business of the holder is transacted, on payment of such fee as may be determined by the holder, but not exceeding 50 cents:

provided that—

(a) on ceasing to carry on business in New Zealand a holder shall deposit the register in the custody of the Registrar of the District Court nearest to the place where that register was theretofore kept:

(b) any holder may at any time so deposit any book or part of the register in which no entry has been made for a period of not less than 6 years immediately preceding the date of that deposit.

(2) Nothing in this section shall apply to any unclaimed money in respect of which special provisions are made by or under any other Act, or to any unclaimed money which, pursuant to the proviso to subsection (1) of section 4 of this Act, ceases to be unclaimed money.

6. Section 7 of the Unclaimed Money Act 1971 provides:

7 Holder to notify Commissioner and owners of entries in register of unclaimed money

(1) Not later than 30 June in each year, every holder shall, by letter addressed to the last known place of business or abode of the owner, post to every owner in respect of whom an entry as the owner of unclaimed money was required to be made on the first day of that month in the register kept by the holder pursuant to section 6, a notice specifying the amount of that money and the fact that it is entered in the register as unclaimed money, and the holder shall thereupon enter in that register the date of posting of the notice.

(2) Not later than 30 September in each year, every holder shall furnish to the Commissioner a copy of every entry made, on or after 1 June in that year, in the register kept by the holder pursuant to section 6, and shall indicate to the Commissioner which, if any, of the unclaimed money in respect of which the entry was so made, has, on or after that 1 June, been paid to the owner thereof.

(3) Nothing in this section shall apply to any unclaimed money in respect of which special provisions are made by or under any other Act.

7. Section 8 of the Unclaimed Money Act 1971 provides:

8 Payment of unclaimed money to Commissioner

(1) All unclaimed money arising in any year ending with 31 May which has not, before the next succeeding 30 September, been paid by a holder to the owner thereof, and in respect of which no person has before that 30 September established a valid claim, shall be paid, on or before the next succeeding 31 October, by the holder to the Commissioner: provided that this subsection shall not apply to any unclaimed money in respect of which special provisions in relation to payment to the Commissioner are made by this Act or in respect of which special provisions are made by or under any other Act.

(2) All money payable to the Commissioner in accordance with this section shall be recoverable by the Commissioner on behalf of the Crown by action in his official name in any court of competent jurisdiction against the holder as a debt due to the Crown.

(3) All unclaimed money received by the Commissioner under this or any other Act shall be paid into a Crown Bank Account.

(4) Where unclaimed money is paid by a holder to the Commissioner in accordance with this Act, the holder shall thereafter be relieved of all further liability to any claimant in respect of the money so paid.

8. Section 13 of the Unclaimed Money Act 1971 provides:

13 Offences

Every person commits an offence, and is liable on conviction to a fine not exceeding $500, who wilfully or negligently—

(a) being a holder, fails to comply with any provision of section 6, section 7, subsection (1) of section 8, or section 10 of this Act, or with any condition on which the Commissioner has granted exemption under section 9 of this Act; or

(b) being a director, manager, secretary, or other officer of the holder, authorises or permits that failure to comply.

Product ruling BR Prd 16/11: Reach Media New Zealand Limited

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

Name of the Person who applied for the Ruling

This Ruling has been applied for by Reach Media New Zealand Limited (Reach Media).

Taxation Laws

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

This Ruling applies in respect of ss DA 2(4), RD 5, RD 7 and RD 8 of the Act and s 6(3)(b) of the Goods and Services Tax Act 1985.

The Arrangement to which this Ruling applies

The Arrangement is the engagement of people (Distributors) by Reach Media under a standard form contract, "Contract for Services – Distribution Contractor" (Distribution Contract or Contract), to physically deliver unaddressed mail (including newspapers, circulars, leaflets, brochures, catalogues, advertising material, samples and other similar items) (Unaddressed Mail), from drop-off locations to households and other premises throughout New Zealand.

Further details of the Arrangement are set out below.

Parties to the Arrangement

1. The Parties to the Arrangement are as follows:
   - Reach Media – a company incorporated in New Zealand under the Companies Act 1993 that is currently owned equally by New Zealand Post Limited and Salmat International Pty Limited. Reach Media carries on the business of distributing and delivering Unaddressed Mail to households and other premises throughout New Zealand.
   - Distributors – people who physically deliver Unaddressed Mail from the drop-off locations to households and other premises throughout New Zealand.
2. Although not technically parties to the Arrangement, Reach Media also contracts with:
   - Supervisors – people who oversee the delivery of Unaddressed Mail by Distributors in a defined area and complete related tasks; and
   - Drivers – people who use their own vehicles to transport Unaddressed Mail from Reach Media's premises to a series of predetermined drop-off locations.
3. Reach Media distributes and delivers only Unaddressed Mail. Reach Media is not involved in the carriage of "letters" (as defined in s 2 of the Postal Services Act 1998) or addressed mail. The Distributors will not be delivering any item that requires Reach Media to be registered as a "postal operator" under the Postal Services Act 1998 (Postal Operator). Reach Media was registered as a Postal Operator, but has subsequently been deregistered.
4. Reach Media is currently run by a management team based in Auckland with processing branches throughout the country. Unaddressed Mail is delivered by a network of Distributors, Drivers and Supervisors.
5. Reach Media's processes and systems align with industry practice. The industry uses a delivery model of supervisors who co-ordinate the activities of a team of distributors. Drivers, Distributors and Supervisors are paid on a "piece-rate basis" under contracts for services (ie, as independent contractors).

Distribution Contract

6. Distributors are engaged under a standard form contract (Distribution Contract) to physically deliver Unaddressed Mail from drop-off locations to households and other premises throughout New Zealand.
7. Distributors agree that in providing the services under the Distribution Contract, (Services) they must also read and comply with the procedures set out in Reach Media's online operational manual (Operational Manual). The Operational Manual does not replace or override any of the material terms of the Distribution Contract, and it does not affect the nature of the contractual relationship between Reach Media and the Distributors.
8. Specific procedural details referred to in the Distribution Contract and the Operational Manual are also provided in specific delivery instructions given to Distributors before each job (Delivery Instructions). These Delivery Instructions contain information on the particular product being delivered. The Delivery Instructions also provide information to Distributors about any changes that Reach Media has made to the Operational Manual.
9. The Distribution Contract will remain materially the same as the version provided to Inland Revenue on 24 June 2016.
10. The main terms of the Distribution Contract are summarised below.

Deliveries

11. The Distribution Contract states that the Distributor agrees to:
    - deliver all the Unaddressed Mail received by the Distributor from Reach Media to the letter boxes in the Distributor's round within the timeframes (Delivery Window) communicated by Reach Media in the Delivery Instructions (exactly when each Distributor completes the deliveries within the Delivery Window is at the Distributor's discretion);
    - make all deliveries in accordance with the delivery guidelines in the Operational Manual (which may be amended by Reach Media from time to time);
    - ensure that any other commitments do not affect the Distributor's obligations to Reach Media; and
    - familiarise themselves with and fully comply with the Operational Manual (and any amendments) and applicable legislation, including that related to tax and health and safety.

Payment

12. The Distribution Contract states the following in relation to payment:
    - The Distributor will be paid for performing the Services at the rates set out in Schedule 2 of the Distribution Contract. (Rates are determined by the volume of the Unaddressed Mail deliveries.)
    - These fees are the only amounts payable to the Distributor in respect of the Services and are inclusive of all taxes (except GST) and other duties or levies.
    - Payment will be made by direct credit into the Distributor's bank account fortnightly on a Thursday.
    - Reach Media will provide a "buyer-created invoice" to Distributors within seven days of payment or before payment if an email address has been supplied by the Distributor. The Contract explains that this means Reach Media will create the invoice and send it to the Distributor. The Distributor must not send any invoice to Reach Media.
13. Schedule 1 of the Distribution Contract requires Distributors to provide their personal details, bank details and, if they are GST registered, their IRD number.

Delivery equipment

14. The Distribution Contract states that the Distributors are responsible for providing, at their own expense, their own delivery equipment (such as bags, vehicles, footwear, reflective or high-visibility clothing, and wet weather gear). The Distributors are also responsible for ensuring any such equipment is well maintained, safe and fit for its purpose.

Taxation

15. The Distribution Contract states the following in relation to taxation:

- Distributors are responsible for paying their own taxes, duties and levies (including income tax, GST and Accident Compensation levies, if applicable), and any other income-related payments or deductions that may be legislated from time to time.
- The Distributors will register for GST with Inland Revenue if required to do so and will advise Reach Media that they are GST registered. Reach Media will then provide them with a buyer-created tax invoice. Distributors must not send a GST tax invoice to Reach Media.

Termination of the Distribution Contract

16. The Distribution Contract states that Reach Media or the Distributors may terminate the Distribution Contract for any reason by giving two weeks' notice in writing. However, Reach Media may terminate the Distribution Contract immediately without notice, if the Distributor is in serious breach of the Distribution Contract or the Operational Manual (and any amendments).

Status of contractor

17. The Distribution Contract states the following in relation to the contractor status of Distributors:

- The Distributor is engaged by Reach Media under a contract for services, which means they are an independent contractor. The Distribution Contract does not create an employment relationship between the Distributor and Reach Media.
- The Distributor is free to accept other engagements or work while they are contracted by Reach Media.

Liability

18. The Distribution Contract states that the Distributor will undertake the Services at their own risk. This means Reach Media will not be liable to the Distributor (or any other person) for any loss resulting from the Distributor's deliberate actions or negligence or where they breach any terms of the Distribution Contract or the Operational Manual (and any amendments).

Delivery options

19. The Distribution Contract states the following in relation to delivery options:

- It is the Distributor's responsibility to carry out the Services as required under the Distribution Contract.
- If the Distributor is sick or unable to carry out the Services, then they need to arrange for someone else to do so. When they do this, the Distributor is responsible for any payment and all other obligations to others who assist them in this way.
- If the Distributor is unable to meet their contractual obligations to ensure the Unaddressed Mail is delivered within the Delivery Window, they must notify their Delivery Supervisor immediately.

Frequency of deliveries

20. The Distribution Contract states that Reach Media does not guarantee any minimum amount of deliveries because the volume of Unaddressed Mail available for distribution will vary, depending on the time of year and the requirements of Reach Media's clients.

Operational Manual

21. The Operational Manual provides guidance and helpful information for Reach Media's contractors on the completion of their duties under the Distribution Contract. Reach Media may amend the Operational Manual at any time, and amendments will be identified to Distributors when they receive their Delivery Instructions. The Operational Manual is divided into two sections, the first of which is applicable only to Distributors.
22. Section One of the Operational Manual covers:
    - the role of the Delivery Supervisor;
    - understanding the round map;
    - receiving the Unaddressed Mail for delivery;
    - understanding the Delivery Instructions;
    - preparing and delivering Unaddressed Mail;
    - confirming delivery;
    - health and safety matters;
    - understanding the fortnightly invoice; and
    - important things Distributors should do and not do when carrying out their obligations under the Distribution Contract.
23. Section Two of the Operational Manual is applicable to all of Reach Media's contractors and provides that Distributors and their families may be ineligible to enter competitions advertised in Unaddressed Mail delivered by Distributors.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

(a) For the purposes of the PAYE rules, any payment made to a Distributor by Reach Media under the Distribution Contract will not be "salary or wages" or "extra pay" or a "schedular payment" within the meaning of those terms as defined in ss RD 5, RD 7 and RD 8.

(b) For the purpose of s DA 2(4), any payment made to a Distributor by Reach Media under the Distribution Contract will not be "income from employment".

(c) For the purposes of the Goods and Services Tax Act 1985, the provision of services by any Distributor under the Distribution Contract will not be excluded from the definition of "taxable activity" (as defined in s 6 of the Goods and Services Tax Act 1985) by s 6(3)(b) of the Goods and Services Tax Act 1985.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 July 2016 and ending on 30 June 2021.

This Ruling is signed by me on the 1st day of December 2016.

Howard Davis
Director (Taxpayer Rulings)

Product ruling BR Prd 16/12: Reach Media New Zealand Limited

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

Name of the Person who applied for the Ruling

This Ruling has been applied for by Reach Media New Zealand Limited (Reach Media).

Taxation Laws

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

This Ruling applies in respect of ss DA 2(4), RD 5, RD 7 and RD 8 of the Act and s 6(3)(b) of the Goods and Services Tax Act 1985.

The Arrangement to which this Ruling applies

The Arrangement is the engagement of people (Drivers) by Reach Media under a standard form contract, "Contract for Services to Perform Driver Delivery Services of Unaddressed Mail" (Driver Delivery Contract or Contract), to transport unaddressed mail (including newspapers, circulars, leaflets, brochures, catalogues, advertising material, samples and other similar items) (Unaddressed Mail) from Reach Media's premises to predetermined drop-off locations.

Further details of the Arrangement are set out below.

Parties to the Arrangement

1. The Parties to the Arrangement are as follows:
   - Reach Media – a company incorporated in New Zealand under the Companies Act 1993 that is currently owned equally by New Zealand Post Limited and Salmat International Pty Limited. Reach Media carries on the business of distributing and delivering Unaddressed Mail to households and other premises throughout New Zealand.
   - Drivers – people who use their own vehicles to transport Unaddressed Mail from Reach Media's premises to a series of predetermined drop-off locations.
2. Although not technically parties to the Arrangement, Reach Media also contracts with:
   - Distributors – people who physically deliver Unaddressed Mail from the drop-off locations to households and other premises throughout New Zealand; and
   - Supervisors – people who oversee the delivery of Unaddressed Mail by Distributors in a defined area and complete related tasks.
3. Reach Media distributes and delivers only Unaddressed Mail. Reach Media is not involved in the carriage of "letters" (as defined in s 2 of the P ostal Services Act 1998) or addressed mail. Drivers will not carry any item that requires Reach Media to be registered as a "postal operator" under the Postal Services Act 1998 (Postal Operator). Reach Media was registered as a Postal Operator, but has subsequently been deregistered.
4. Reach Media is currently run by a management team based in Auckland with processing branches throughout the country. Unaddressed Mail is delivered by a network of Distributors, Drivers and Supervisors.
5. Reach Media's processes and systems align with industry practice. The industry uses a delivery model of supervisors who co-ordinate the activities of a team of distributors. The Drivers, Distributors and Supervisors are paid on a "piece-rate" basis under contracts for services (ie, as independent contractors).

Driver Delivery Contract

6. Drivers are engaged under a standard form contract (Driver Delivery Contract) to transport Unaddressed Mail from Reach Media's premises to several predetermined drop-off locations.
7. Drivers agree that in providing the services under the Driver Delivery Contract (Services) they must also read and comply with the procedures set out in Reach Media's online operational manual (Operational Manual). The Operational Manual does not replace or override any of the material terms of the Driver Delivery Contract, and it does not affect the nature of the contractual relationship between Reach Media and the Drivers.
8. Specific procedural details referred to in the Driver Delivery Contract are also provided in specific delivery instructions given to Drivers before each job (Delivery Instructions). These Delivery Instructions contain information on the particular product being delivered. The Delivery Instructions also provide information to Drivers about any changes Reach Media has made to the Operational Manual.
9. The Driver Delivery Contract will remain materially the same as the version provided to Inland Revenue on 24 June 2016.
10. The main terms of the Driver Delivery Contract are summarised below.

Services

11. The Driver Delivery Contract states that Drivers must complete the Services that are set out in Schedule 1 of the Driver Delivery Contract. In completing the Services, Drivers will:
    - ensure their other business commitments do not affect their obligations to Reach Media; and
    - familiarise themselves and fully comply with the Operational Manual (which may be amended by Reach Media from time to time) and any applicable legislation including that related to tax and health and safety.
12. Schedule 1 of the Driver Delivery Contract states that the Services to be performed are the:
    - collection of Unaddressed Mail plus Delivery Notifications for drop off to a defined set of Distributors from one of Reach Media's nominated premises on the day before the commencement of the Delivery Window;
    - physical delivery of Unaddressed Mail to be delivered by Distributors to nominated individual Distributor drop-off points in the quantities specified in the Delivery Notifications; and
    - physical return of any surplus stock to the nominated Reach Media processing site.

Equipment

13. The Driver Delivery Contract states that Drivers are responsible for providing, at their own expense, their own equipment (such as personal office supplies, telephone, vehicles and wet weather gear). Drivers are also responsible for ensuring such equipment is well maintained, safe and fit for its purpose.

Vehicle

14. The Driver Delivery Contract sets out the Drivers' obligations regarding the safe and legal operation of any vehicle used to provide the Services. The Driver Delivery Contract also states that Drivers must effect and maintain at their own cost and expense adequate public liability insurance (on terms agreed by Reach Media) and comprehensive motor vehicle insurance.

Payment

15. The Driver Delivery Contract states the following in relation to payment:
    - The Driver will be paid for performing the Services at the rates set out in Schedule 2 of the Contract. (Rates are determined by the volume of the Unaddressed Mail deliveries.)
    - These fees are the only amounts payable to the Driver in respect of the Services and are inclusive of all taxes (except GST) and other duties or levies.
    - Reach Media will email the Driver a "buyer-created tax invoice" twice a month. The Driver must not send an invoice to Reach Media. The Driver must check the invoice and advise Reach Media of any errors. Payment will be made by way of direct credit to the Driver's bank account fortnightly on a Thursday.
16. Schedule 3 of the Driver Delivery Contract requires Drivers to provide to Reach Media their personal details, bank details and, if they are GST registered, their IRD number.

Taxation

17. The Driver Delivery Contract states the following in relation to taxation:
    - Drivers will register for GST with Inland Revenue if they are required to do so. The Contract sets out the current registration threshold.
    - Drivers are responsible for paying their own taxes on payments made to them by Reach Media under the Driver Delivery Contract.
    - Reach Media may be required to withhold taxes from its payments to the Driver, in which case the payments made will be reduced to the extent that tax is withheld. If Reach Media wrongly fails to withhold tax from payments made to the Driver, it will be entitled to recover such amounts from the Driver.

Termination of the Driver Delivery Contract

18. The Driver Delivery Contract states that Reach Media or the Driver may terminate the Driver Delivery Contract for any reason by giving four weeks' notice in writing. However, if Reach Media believes the Driver is in serious breach of the Driver Delivery Contract or the Operational Manual (including any amendments), then Reach Media may terminate the Driver Delivery Contract immediately without notice.

Status of contractor

19. The Driver Delivery Contract states the following in relation to the contractor status of Drivers:
    - The Driver is engaged by Reach Media under a contract for services, which means they are an independent contractor. The terms of the Driver Delivery Contract or its operation do not create an employment relationship between the Driver and Reach Media.
    - The Driver is free to accept other engagements or work while they are engaged by Reach Media. However, the Driver agrees not to undertake other work that does or may conflict with the interests of Reach Media.

Liability

20. The Driver Delivery Contract states the following in relation to liability:
    - Drivers will undertake the Services at their own risk. This means Reach Media will not be liable to the Driver (or any other person) for any loss resulting from the Driver's deliberate actions or negligence or where they breach any terms of the Driver Delivery Contract or the Operational Manual (and any amendments).
    - The Driver agrees to indemnify Reach Media against any direct, indirect or consequential injury, loss or damage that Reach Media may suffer as a result of any breach by the Driver of the Driver Delivery Contract or arising out of an act, a default or an omission, or any representation made by the Driver. This indemnity will continue to apply after termination of the Driver Delivery Contract.

Delivery options

21. The Driver Delivery Contract states the following in relation to delivery options:
    - It is the Driver's responsibility to carry out the Services as required under the Driver Delivery Contract.
    - If the Driver is sick or not able to personally carry out the Services, then they must arrange for someone else to do so. When they do this, the Driver is solely responsible for payment and all other obligations to others who assist them in this way.

Frequency of deliveries

22. The Driver Delivery Contract states that Reach Media does not guarantee any minimum amount of Unaddressed Mail for which the Driver will carry out the Services. The volume of Unaddressed Mail available for distribution will vary depending on the time of year and the needs of Reach Media's clients.

Operational Manual

23. The Operational Manual provides guidance and helpful information for Reach Media's contractors on the completion of their duties under the Driver Delivery Contract. The Operational Manual may be amended by Reach Media at any time and amendments will be identified to Drivers when they receive their Delivery Instructions. The Operational Manual is divided into two sections, the first of which is applicable only to Distributors.
24. Section Two of the Operational Manual is applicable to all Reach Media contractors, including Drivers, and provides that Drivers and their families may be ineligible to enter competitions advertised in Unaddressed Mail delivered by Drivers.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

(a) For the purposes of the PAYE rules, any payment made to a Driver by Reach Media under the Driver Delivery Contract will not be "salary or wages" or "extra pay" or a "schedular payment" within the meaning of those terms as defined in ss RD 5, RD 7 and RD 8.

(b) For the purpose of s DA 2(4), any payment made to a Driver by Reach Media under the Driver Delivery Contract will not be "income from employment".

(c) For the purposes of the Goods and Services Tax Act 1985, the provision of services by any Driver under the Driver Delivery Contract will not be excluded from the definition of "taxable activity" (as defined in s 6 of the Goods and Services Tax Act 1985) by s 6(3)(b) of the Goods and Services Tax Act 1985.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 July 2016 and ending on 30 June 2021.

This Ruling is signed by me on the 1st day of December 2016.

Howard Davis
Director (Taxpayer Rulings)

Product ruling BR Prd 16/13: Reach Media New Zealand Limited

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

Name of the Person who applied for the Ruling

This Ruling has been applied for by Reach Media New Zealand Limited (Reach Media).

Taxation Laws

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

This Ruling applies in respect of ss DA 2(4), RD 5, RD 7 and RD 8 of the Act and s 6(3)(b) of the Goods and Services Tax Act 1985.

The Arrangement to which this Ruling applies

The Arrangement is the engagement of people (Supervisors) by Reach Media under a standard form contract, "Contract for Services to Supervise Delivery of Unaddressed Mail" (Supervision Contract or Contract), to oversee the delivery of unaddressed mail (including newspapers, circulars, leaflets, brochures, catalogues, advertising material, samples and other similar items) (Unaddressed Mail) by Distributors in a defined area and complete related tasks.

Further details of the Arrangement are set out below.

Parties to the Arrangement

1. The Parties to the Arrangement are as follows:
   - Reach Media – a company incorporated in New Zealand under the Companies Act 1993 that is currently owned equally by New Zealand Post Limited and Salmat International Pty Limited. Reach Media carries on the business of distributing and delivering Unaddressed Mail to households and other premises throughout New Zealand.
   - Supervisors – persons who oversee the delivery of Unaddressed Mail by Distributors in a defined area and complete related tasks.
2. Although not technically parties to the Arrangement, Reach Media also contracts with:
   - Distributors – people who physically deliver Unaddressed Mail from the drop-off locations to households and other premises throughout New Zealand; and
   - Drivers – people who use their own vehicles to transport Unaddressed Mail from Reach Media's premises to a series of predetermined drop-off locations.
3. Reach Media distributes and delivers only Unaddressed Mail. Reach Media is not involved in the carriage of "letters" (as defined in s 2 of the Postal Services Act 1998) or addressed mail. The item deliveries that are supervised by the Supervisors are not items the carriage of which requires Reach Media to be registered as a "postal operator" under the Postal Services Act 1998 (Postal Operator). Reach Media was registered as a Postal Operator, but has subsequently been deregistered.
4. Reach Media is currently run by a management team based in Auckland with processing branches throughout the country. Unaddressed Mail is delivered by a network of Distributors, Drivers and Supervisors.
5. Reach Media's processes and systems align with industry practice. The industry uses a delivery model of supervisors who co-ordinate the activities of a team of distributors. The Drivers, Distributors and Supervisors are paid on a "piece rate" basis under contracts for services (ie, as independent contractors).

Supervision Contract

6. Supervisors are engaged under a standard form contract (Supervision Contract) to oversee the delivery of Unaddressed Mail by Distributors in a defined area and complete related tasks.
7. Supervisors agree that in providing the services under the Supervision Contract (Services) they must also read and comply with the procedures set out in Reach Media's online operational manual (Operational Manual). The Operational Manual does not replace or override any of the material terms of the Supervision Contract, and it does not affect the nature of the contractual relationship between Reach Media and the Supervisors.

8. Specific procedural details referred to in the Supervision Contract are also provided in specific delivery instructions given to Supervisors before each job (Delivery Instructions). These Delivery Instructions contain information on the particular product being delivered. The Delivery Instructions also provide information to Supervisors about any changes that Reach Media has made to the Operational Manual.
9. The Supervision Contract will remain materially the same as the version provided to Inland Revenue on 24 June 2016.
10. The main terms of the Supervision Contract are summarised below.

Services

11. The Supervision Contract states that Supervisors are required to complete the Services that are set out in Schedule 1 of the Supervision Contract. In completing the Services, Supervisors will:
    - ensure that their other business commitments do not affect their obligations to Reach Media; and
    - familiarise themselves and fully comply with the Operational Manual (which may be amended by Reach Media from time to time) and any applicable legislation including that related to tax and health and safety.
12. Schedule 1 of the Supervision Contract states that the Services to be performed by all Supervisors are to:
    - oversee the physical delivery of the individual items of Unaddressed Mail by the Distributors to nominated individual delivery points;
    - maintain and supply to Reach Media details of current Distributors and provide information relating to any round changes and associated delivery quantities including "no circular" counts; and
    - ensure Distributors phone or text in confirmation of delivery before the close of the Delivery Window.
13. Certain Supervisors must also perform additional services. These are predominantly Supervisors who are not located in a metro area.

Equipment

14. The Supervision Contract states that Supervisors are responsible for providing, at their own expense, their own equipment (such as personal office supplies, telephone, vehicles and wet weather gear). Supervisors are also responsible for ensuring that such equipment is well maintained, safe and fit for its purpose.

Payment

15. The Supervision Contract states the following in relation to payment:
    - The Supervisor will be paid for performing the Services at the rates set out in Schedule 2 of the Supervision Contract. (Rates are determined by the volume of the Unaddressed Mail deliveries.)
    - These fees are the only amounts payable to the Supervisor in respect of the Services and are inclusive of all taxes (except GST) and other duties or levies.
    - Reach Media will email the Supervisor a "buyer-created tax invoice" before payment. The Supervisor must not send an invoice to Reach Media. The Supervisor must advise Reach Media immediately if they believe the invoice is incorrect. Payment will be made by way of direct credit to the Supervisor's bank account fortnightly on a Thursday.
16. Schedule 3 of the Supervision Contract requires Supervisors to provide their personal details, bank details and, if they are GST registered, their IRD number.

Taxation

17. The Supervision Contract states the following in relation to taxation:
    - Supervisors will register for GST with Inland Revenue if required to do so. The Contract sets out the current registration threshold.
    - Supervisors are responsible for the payment of their own taxes on payments made to them by Reach Media under the Supervision Contract.
    - Reach Media may be required to withhold taxes from its payments to Supervisors, in which case the payments made will be reduced to the extent that tax is withheld. If Reach Media wrongly fails to withhold tax from payments made to a Supervisor, it will be entitled to recover such amounts from the Supervisor.

Termination of the Supervision Contract

18. The Supervision Contract states that Reach Media or the Supervisors may terminate the Supervision Contract for any reason by giving four weeks' notice in writing. However, if Reach Media believes the Supervisor is in serious breach of the Supervision Contract or the Operational Manual (including any amendments) then Reach Media may terminate the Supervision Contract immediately without notice.

Status of contractor

19. The Supervision Contract states the following in relation to the contractor status of Supervisors:
    - The Supervisor is engaged by Reach Media under a contract for services, which means they are an independent contractor. The terms of the Supervision Contract or its operation do not create an employment relationship between the Supervisor and Reach Media.
    - The Supervisor is free to accept other engagements or work while they are engaged by Reach Media. However, the Supervisor agrees not to undertake other work that does or may conflict with the interests of Reach Media.

Indemnity

20. The Supervision Contract states that the Supervisor will undertake the Services at their own risk. This means Reach Media will not be liable to the Supervisor (or any other person) for any loss resulting from the Supervisor's deliberate actions or negligence or where they breach any terms of the Supervision Contract or the Operational Manual (including any amendments).

Delivery options

21. The Supervision Contract states the following in relation to delivery options:
    - It is the Supervisor's responsibility to carry out the Services as required under the Supervision Contract.
    - If the Supervisor is sick or not able to personally carry out the Services, then they must arrange for someone else to do so. When they do this, the Supervisor is solely responsible for payment and all other obligations to others who assist them in this way.

Frequency of deliveries

22. The Supervision Contract states that Reach Media does not guarantee any minimum amount of Unaddressed Mail for which the Supervisor will carry out the Services. The volume of Unaddressed Mail available for distribution will vary depending on the time of year and the needs of Reach Media's clients.

Operational Manual

23. The Operational Manual provides guidance and helpful information for Reach Media's contractors on the completion of their duties under the Supervision Contract. Reach Media may amend the Operational Manual at any time and amendments will be identified to Supervisors when they receive their Delivery Instructions. The Operational Manual is divided into two sections, the first of which is applicable only to Distributors.
24. Section Two of the Operational Manual is applicable to all Reach Media contractors, including Supervisors, and provides that Supervisors and their families may be ineligible to enter competitions advertised in Unaddressed Mail delivered by Supervisors.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

(a) For the purposes of the PAYE rules, any payment made to a Supervisor by Reach Media under the Supervision Contract will not be "salary or wages" or "extra pay" or a "schedular payment" within the meaning of those terms as defined in ss RD 5, RD 7 and RD 8.

(b) For the purpose of s DA 2(4), any payment made to a Supervisor by Reach Media under the Supervision Contract will not be "income from employment".

(c) For the purposes of the Goods and Services Tax Act 1985, the provision of services by any Supervisor under the Supervision Contract will not be excluded from the definition of "taxable activity" (as defined in s 6 of the Goods and Services Tax Act 1985) by s 6(3)(b) of the Goods and Services Tax Act 1985.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 July 2016 and ending on 30 June 2021.

This Ruling is signed by me on the 1st day of December 2016.

Howard Davis
Director (Taxpayer Rulings)

LEGISLATION AND DETERMINATIONS

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

Livestock values – 2017 national standard costs for specified livestock

The Commissioner of Inland Revenue has released a determination, reproduced below, setting the national standard costs for specified livestock for the 2016–2017 income year.

These costs are used by livestock owners as part of the calculation of the value of livestock on hand at the end of the income year, where they have adopted the national standard cost ("NSC") scheme to value any class of specified livestock.

Farmers using the scheme apply the rising one-year NSC to stock bred on the farm each year, and add the rising two-year NSC to the value of the opening young stock available to come through into the mature inventory group at year-end. Livestock purchases are also factored into the valuation of the immature and mature groupings at year-end, so as to arrive at a valuation reflecting the enterprise's own balance of farm bred and externally purchased animals.

NSCs are developed from the national average costs of production for each type of livestock farming based on independent survey data. Only direct costs of breeding and rearing rising one-year and two-year livestock are taken into account. These exclude all costs of owning (leasing) and operating the farm business, overheads, costs of operating non-livestock enterprises (such as cropping) and costs associated with producing and harvesting dual products (wool, fibre, milk and velvet).

For bobby calves, information from spring 2016 is used while other dairy NSCs are based on the 2015-2016 income and expenditure from a DairyBase sample of owner-operated dairy farms. For sheep, beef cattle, deer and goats, NSCs are based on survey data from the 2014-2015 sheep and beef farm survey conducted by the Beef & Lamb New Zealand Economic Service. This is the most recent information available for those livestock types at the time the NSCs are calculated in December 2016.

For the 2016–2017 income year there has been a decrease in the NSCs for dairy cattle, bobby calves, deer, dairy goats and pigs. To a large extent these decreases were due to decreases in feed (dairy cattle, bobby calves, dairy goats and pigs), fertilizer (dairy cattle, deer), freight and labour (bobby calves) and fuel (deer).

The NSCs calculated each year only apply to that year's immature and maturing livestock. Mature livestock valued under this scheme effectively retain their historic NSCs until they are sold or otherwise disposed of, albeit through a FIFO or inventory averaging system as opposed to individual livestock tracing. It should be noted that the NSCs reflect the average costs of breeding and raising immature livestock and will not necessarily bear any relationship to the market values (at balance date) of these livestock classes. In particular, some livestock types, such as dairy cattle, may not obtain a market value in excess of the NSC until they reach the mature age grouping.

One-off movements in expenditure items are effectively smoothed within the mature inventory grouping, by the averaging of that year's intake value with the carried forward values of the surviving livestock in that grouping. For the farm-bred component of the immature inventory group, the NSC values will appropriately reflect changes in the costs of those livestock in that particular year.

The NSC scheme is only one option under the current livestock valuation regime. The other options are market value, the herd scheme and the self-assessed cost scheme ("SAC") option. SAC is calculated on the same basis as NSC but uses a farmer's own costs rather than the national average costs. There are restrictions in changing from one scheme to another and before considering such a change livestock owners may wish to discuss the issue with their accountant or other adviser.

National Standard Costs for Specified Livestock Determination 2017

This determination may be cited as "The National Standard Costs for Specified Livestock Determination 2017".

This determination is made in terms of section EC 23 of the Income Tax Act 2007. It shall apply to any specified livestock on hand at the end of the 2016–2017 income year where the taxpayer has elected to value that livestock under the national standard cost scheme for that income year.

For the purposes of section EC 23 of the Income Tax Act 2007 the national standard costs for specified livestock for the 2016–2017 income year are as set out in the following table.

Kind of livestock	Category of livestock	National standard cost $
Sheep	Rising 1 year	32.20
	Rising 2 year	22.70
Dairy Cattle	Purchased bobby calves	143.00
	Rising 1 year	404.10
	Rising 2 year	322.50
Beef Cattle	Rising 1 year	343.80
	Rising 2 year	190.90
	Rising 3 year male non-breeding cattle (all breeds)	190.90
Deer	Rising 1 year	101.20
	Rising 2 year	49.90
Goats (Meat and Fibre)	Rising 1 year	26.60
	Rising 2 year	18.20
Goats (Dairy)	Rising 1 year	132.30
	Rising 2 year	26.20
Pigs	Weaners to 10 weeks of age	97.50
	Growing pigs 10 to 17 weeks of age	79.50

This determination is signed by me on the 26th day of January 2017.

Rob Wells

LTS Manager, Technical Standards

LEGISLATIONS AND DETERMINATIONS

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.

Taxation Review Authority finds sale of business took place at value stated by taxpayer and sets aside Commissioner's reassessments

Case	TRA 014/14 [2016] NZTRA 15
Decision date	15 December 2016
Act(s)	Income Tax Act 2004, s CD 3; Tax Administration Act 1994, ss 108 and 149A (2)(b)
Keywords	Onus of proof, deemed dividend, goodwill, valuation

Summary

The Taxation Review Authority ("the TRA") has found that the sale of a business by the sole trader disputant to his company was in 2002 for the amount stated by the taxpayer. The taxpayer was reassessed by the Commissioner of Inland Revenue ("the Commissioner") on the basis the credits to his current account were deemed dividends and shortfall penalties were also imposed. The reassessments and shortfall penalties were set aside.

Facts

In February 2002 the disputant sold the accountancy practice, which he operated as a sole trader, to his company ("the Company"). The Commissioner asserted that the amount paid for the practice was $425,000, as recorded in the Company's 2002 financial statements. The Commissioner reassessed the disputant's income tax liability for the 2007 and 2008 tax years on the basis that certain credits made to his shareholder account with the Company were deemed dividends. The Commissioner also imposed shortfall penalties for failing to take reasonable care.

In this proceeding the disputant challenged these reassessments and the imposition of the shortfall penalties. He said that the purchase price was $2,000,000, and that instead of bringing the full amount of the goodwill into the Company's accounts in the 2002 year, he brought in $425,000. He contended that the credits in dispute (being $565,214 in the 2007 year and $725,000 in the 2008 year) were part of that purchase price, not dividends, and that the reassessments are statute barred in any event.

The goodwill payment of $425,000 was written off in the 2003 year. No further amounts were brought in and written off in the 2004, 2005 and 2006 years. In the Company's financial statements for the 2007 year ("the First 2007 Statements") the disputant brought in $850,000 (taking the goodwill to $1,275,000) and wrote off another $425,000. The disputant subsequently produced two further sets of financial statements for the 2007 year (the Second and Third 2007 Statements) and amended the financial statements for the 2006 year ("the 2006 Amended Statements"). In the 2006 Amended Statements the goodwill figure was increased to $2,000,000. The Third 2007 Statements were consistent with the 2006 Amended Statements.

In or about September 2007 the disputant's family trust ("the Trust") purchased a beach property, funded by a $1,300,000 loan obtained by the Company from its bank. The loan was secured by a mortgage over properties owned by the Trust. Guarantees were provided by the disputant and the trustees of the Trust and another family trust. The funds were transferred to the disputant by way of repayment of the disputant's current account and then on-lent to the Trust.

The loan and repayment of the disputant's current account were recorded in the Company's financial statements for the 2008 year, filed with Inland Revenue on or about 5 September 2008.

Eventually all the mortgaged properties were sold by mortgagee sale. The loan was repaid but the equity in the properties was lost. The fee base of the accountancy practice was sold to another entity and the Company went into liquidation in 2013.

Decision

Counsel agreed that this case turned on whether the disputant could meet the onus of proof on him of showing on the balance of probabilities that in 2002 he sold his accountancy practice to his Company for $2,000,000.

Inconsistencies/Credibility

The TRA observed that there were a number of inconsistencies in the explanations and documents supplied during the course of the investigation.

The TRA noted that, in many instances, the explanations initially given had been corrected and/or expanded upon in later correspondence and in the statement of position filed on behalf of the disputant. The TRA also observed that during much of the later period that this dispute was on-going, the disputant was dealing with an acrimonious marriage breakup, mortgagee sales of his family's assets and restructuring of his accountancy practice.

The TRA did not agree with the Commissioner's submission that the disputant gave inconsistent and contradictory arguments in his evidence before the TRA. The TRA found that even though the disputant did not have a clear recollection of events and dates and was confused by questions in cross-examination, he was a credible and reliable witness.

Finally, the TRA did not accept the Commissioner's submission that it was not credible that a chartered accountant would have acted in the manner in which the disputant says he did. The TRA noted that the proceeding was not a negligence claim and the disputant's conduct and performance of his professional duties were not matters for determination, although noting the disputant readily accepted that aspects of his accountancy work involving his own affairs were "sloppy".

2002 Financial Statements and Journal Entries

The disputant explained that it was his intention to bring the goodwill into the financial statements progressively and to then write it off. The $425,000 goodwill sum was written off in the 2003 tax year.

A page taken from the Company's computer generated journal for the 2002 year was produced. On the page there were debit and credit entries for $425,000 and for $1,575,000. The disputant gave evidence that he did not bring the $1,575,000 into the 2002 financial statements and that there were entries on the next page of the journal reversing out this amount. He explained that he had made these entries as a record of the goodwill which had still to be brought into the Company's accounts in later years.

The disputant's previous lawyer had advised the Commissioner that entries reversing the entries relating to the $1,575,000 were made in 2008. The TRA found that this was not correct, finding that the accounting software used by the Company did not permit adjustments to the accounts years later and accepted the disputant's evidence that the journal entries were made in 2002.

Valuation

The disputant valued the goodwill of the company at $2,000,000, fixing the value of the fee base at $1,400,000 and the in-house software at $600,000, but he did not obtain an independent valuation. A valuation prepared for the disputant by an independent chartered accountant for the purposes of the dispute process valued the fee base at $1,040,000 and, at the hearing, the expert witness for the Commissioner, Mr H, considered a valuation of goodwill of $425,000 would be acceptable. The TRA noted that she was not required to determine the correct value in this case but it was quite evident that the disputant's valuation substantially overstated the goodwill value of the business.

2006-2008 Financial Statements and 2008 Review

The TRA accepted that the disputant chose to amend the financial statements for the 2007 year and to bring in all the goodwill in order to comply with the requirements of a practice review by the accountants' professional body in May 2008. The TRA did not agree with the Commissioner's contention that the disputant amended the opening balance for the 2007 year in order to gain a tax advantage by funding the purchase of the beach property through the Company.

In the TRA's view this contention overlooked that the disputant had already brought in further goodwill of $850,000 in the First 2007 Statements, taking the goodwill to $1,275,000. This action was consistent with an earlier sale at $2,000,000. The disputant then proceeded to write off the sum of $425,000 which, again, was consistent with the earlier write off in 2003 (and, in the TRA's view, was not consistent with wanting to achieve the tax advantage alleged by the Commissioner).

The TRA stated that there was no evidence that the disputant had any intention of purchasing a beach property in the period in which the TRA found that the First 2007 Statements were prepared. The TRA observed that if there was such an intention, it begs the question as to why the disputant did not bring the amount of $2,000,000 into the financial statements at that time.

Sale & Purchase Agreement

The disputant gave evidence that he had located a copy of the agreement for the sale and purchase. The disputant provided the agreement for sale and purchase to the Commissioner with his statement of position dated 4 October 2013 and explained the circumstances in which the document had been located. The Commissioner's Statement of Position identified a number of irregularities in the agreement. The Commissioner argued that the agreement was a fabrication which "the disputant had produced only recently".

The standard form sale and purchase agreement used was the second edition ADLS/REINZ form produced in July 1995. The TRA considered that it is unlikely that in 2012/2013 the disputant would have used the 1995 second edition of the ADLS/REINZ form, noting that the third edition came into force in or around March 2005. After carefully considering all of the evidence, the TRA accepted the disputant's evidence that the agreement for sale and purchase was prepared and signed in 2002.

Conclusion

Taking into account the factual findings and the evidence overall, the TRA was satisfied that the disputant entered into an agreement with the Company in 2002 to sell his accountancy practice to the Company for the sum of $2,000,000.00. The full amount of this goodwill payment was brought into the financial statements of the Company in the 2006 Amended Statements. Accordingly, the TRA found that the disputed credits were part of the purchase price and were not dividends.

Having reached this view, the Commissioner's reassessments for the 2007 and 2008 years were not correct and were set aside accordingly.

REGULAR CONTRIBUTORS TO THE TIB

Office of the Chief Tax Counsel

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

Legal and Technical Services

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

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

Policy and Strategy

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

Litigation Management

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

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