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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 **taxtechnical.ird.govt.nz** (search keywords: public consultation).

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

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

You can also subscribe at **taxtechnical.ird.govt.nz/subscribe** to receive regular email updates when we publish new draft items for comment.

Your opportunity to comment

Ref	Draft type	Title	Comment deadline
PUB00357	Interpretation statement	GST and finance leases	17 December 2021
PUB00372	Question we've been asked	What is required to establish and maintain a "public fund" under s LD 3(2)(d) of the Income Tax Act 2007?	24 December 2021
PUB00330	Question we've been asked	GST – goods purchased on deferred payment terms	24 December 2021

IN SUMMARY

New legislation

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NEW LEGISLATION

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

The COVID-19 Resurgence Support Payments Scheme (August 2021) Amendment Order (No 4) 2021

The COVID-19 Resurgence Support Payments Scheme (August 2021) Amendment Order (No 4) 2021 (the amending Order) came into force on 1 November 2021. This Order amended *the COVID-19 Resurgence Support Payments Scheme (August 2021) Order 2021* (the principal Order) to end the affected revenue periods for the first three grants under the August activation.

Background

The principal Order (2021/222) came into force on 24 August 2021 and activated the COVID-19 Resurgence Support Payments (RSP) scheme to provide grants to support businesses affected by the 17 August 2021 escalation in COVID-19 Alert Levels.

Refer to *Tax Information Bulletin Vol 33 No 9 October 2021* and *Tax Information Bulletin Vol 33 No 10 November 2021* for further information on the principal Order and subsequent amending Orders.

Amendment

The 'affected revenue period' for a grant under the RSP scheme is the period from which an applicant can nominate a consecutive seven-day period to measure their revenue decline. The nominated seven-day period for each grant may overlap.

Since the RSP was activated on 24 August 2021, the affected revenue period for each grant has been set to end immediately before all areas of New Zealand return to COVID-19 return to COVID-19 Alert Level 1.

This amending Order sets the end of the affected revenue periods for the first three grants under the August activation to the close of 1 November 2021. The fourth grant under the scheme, activated on 29 October 2021, is unaffected by this change.

Applications

Applications for the first three grants under the August activation remain open until 1 December 2021 and may be submitted via myIR.

The full eligibility requirements have been set out by the Commissioner under section 7AAB(3) of the TAA and are published on the Inland Revenue website **ird.govt.nz/covid-19/business-and-organisations/resurgence-support-payment/eligibility**.

The COVID-19 Resurgence Support Payments Scheme (August 2021) Amendment Order (No 5) 2021

The COVID-19 Resurgence Support Payments Scheme (August 2021) Amendment Order (No 5) 2021 (the amending Order) came into force on 12 October 2021. This Order amended *the COVID-19 Resurgence Support Payments Scheme (August 2021) Order 2021* (the principal Order) to provide for a fifth grant payment.

Background

The principal Order (2021/222) came into force on 24 August 2021 and activated the COVID-19 Resurgence Support Payments (RSP) scheme to provide grants to support businesses affected by the 17 August 2021 escalation in COVID-19 Alert Levels.

Refer to *Tax Information Bulletin Vol 33 No 9 October 2021*, *Tax Information Bulletin Vol 33 No 10 November 2021*, and the above item for further information on the principal Order and subsequent amending Orders.

Additional payments

This amending Order provides for a fifth grant to be made under the COVID-19 Resurgence Support Payment (RSP) scheme.

Affected revenue periods

A person is eligible for a grant under the RSP scheme if the person experienced a minimum 30% decline in revenue in relation to a business or organisation during a nominated 7-day period. A person must nominate a 7-day period within the affected revenue period for each payment. The nominated 7-day period for each payment may overlap with the nominated periods for other payments.

The affected revenue period for the fifth grant starts on 5 November 2021 and ends immediately before all areas of New Zealand either:

- return to COVID-19 Alert Level 1; or
- are at Orange or Green under the COVID-19 Protection Framework.

Amount of grant

The amount of the fifth grant is double the amount of the previous grants under the August scheme. The amount is calculated as the lesser of:

- $3,000 plus an additional amount of $800 for each full-time equivalent worker employed by the person (up to a maximum 50 FTE); or
- 8 times the actual revenue decline measured by the applicant's nominated seven-day period.

Amending the affected revenue period for fourth grant

This amending Order also changes the criteria to determine the end of the affected revenue period for the fourth grant to align it with the fifth grant. This ensures that the settings for the fourth grant are clear in the event that part of New Zealand moves to the COVID-19 Protection Framework.

Applications

Applications for the fifth grant opened on 12 November 2021 and can be submitted via myIR.

The full eligibility requirements have been set out by the Commissioner under section 7AAB(3) of the TAA and are published on the Inland Revenue website **ird.govt.nz/covid-19/business-and-organisations/resurgence-support-payment/eligibility**.

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 Prd 21/06: Kiwibank Limited

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

Name of person who applied for the Ruling

This Ruling has been applied for by Kiwibank Limited (Kiwibank) - IRD No. 79-167-495 and the Kiwibank Consolidated Tax Group – IRD No. 121-260-735.

Taxation Laws

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

This Ruling applies in respect of ss BG 1 and GB 35(2).

The Arrangement to which this Ruling applies

The Arrangement is the issue by Kiwibank of certain redeemable perpetual preference shares (PPS) of up to $300 million to third party investors by way of a public offer.

Kiwibank intends to recognise the PPS as Additional Tier 1 capital for the purposes of the Reserve Bank of New Zealand (RBNZ) capital adequacy rules.

Kiwibank will use the proceeds of the issue of the PPS for its general banking business.

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

Documents

1. The following documents describe the Arrangement:
   a) Kiwibank's constitution provided to Inland Revenue on 10 September 2021
   b) Kiwibank 2021 perpetual preference share terms (Terms) provided to Inland Revenue on 23 September 2021
   c) RBNZ document: BPR110 Capital Definitions (1 July 2021)

Terms of PPS

Issue of PPS

2. Each of the PPS will have an issue price of $1 (cl 1.3 of the Terms).
3. Clause 2.1 of Kiwibank's constitution permits the issue of redeemable shares.

Voting rights

4. PPS holders will have no right to attend or vote at meetings of holders of Kiwibank ordinary shares, nor will they have the right to participate in or vote on decisions of ordinary shareholders made outside of shareholder meetings (cl 1.8(a) of the Terms).
5. PPS holders will have the protective voting rights conferred by section 117 of the Companies Act 1993 and certain changes to the Terms require the approval (by way of special resolution) of PPS holders (cl 6.2(c) of the Terms).

Distributions

6. The PPS will carry a right to quarterly distributions.

7. The distribution payable on each scheduled distribution date is calculated in accordance with the following formula (cl 2.3 of the Terms):

$$\text{Distribution payable} = \frac{\text{Distribution Rate} \times (1\text{-Tax Rate}) \times \text{Issue Price}}{4}$$

8. The "Distribution Rate" is calculated according to the following formula (cl 2.2 of the Terms):

$$\text{Distribution Rate} = (\text{Swap Rate} + \text{Margin})$$

9. Where:

   "Swap Rate" means:

   a) in respect of the first Fixed Rate Period:

      i) the mid-market swap rate for an interest rate swap with a term of 5 years commencing on the Rate Set Date, as calculated by Kiwibank on the Rate Set Date in accordance with market convention with reference to Bloomberg page 'ICNZ4' (or its successor page); or

      ii) if a rate is unable to be determined in accordance with i) above, or if Kiwibank forms a view, on reasonable grounds, that the rate so determined is not an accurate reflection of market rates, the average of the mean bid and offered swap rates quoted by each of the Reference Banks on the Rate Set Datefor an interest rate swap with a term of 5 years commencing on the Rate Set Date,

   b) in respect of any other Fixed Rate Period:

      i) the mid-market swap rate for an interest rate swap with a term of 5 years commencing on the applicable rate reset date, as calculated by Kiwibank at or about 11am on the Rate Reset Date in accordance with market convention with reference to Bloomberg page 'ICNZ4' (or its successor page); or

      ii) if a rate is unable to be determined in accordance with i) above, or if Kiwibank forms a view, on reasonable grounds, that the rate so determined is not an accurate reflection of market rates, the average of the mean bid and offered swap rates quoted by each of the reference banks at or about 11am on the Rate Reset Date for an interest rate swap with a term of 5 years commencing on the Rate Reset Date,

   in each case expressed on a percentage basis, adjusted for quarterly payments and rounded, if necessary, to the nearest two decimal places with five being rounded up.

   "Margin" means the margin (expressed as a percentage per annum) determined by Kiwibank in consultation with the Joint Lead Managers following the Bookbuild and announced by Kiwibank via NZX on the Rate Set Date.

10. If the Distribution Rate determined in accordance with clause 2.2 of the Terms is less than 0% per annum, the Distribution Rate will be deemed to be 0% per annum.

11. The "Tax Rate" means the New Zealand corporate tax rate on the relevant Distribution Payment Date (expressed as a decimal).

12. Kiwibank is obliged to fully impute the distributions on the PPS (cl 2.4 of the Terms). If any distribution is not fully imputed, then Kiwibank must increase the cash component of the distribution to equal the shortfall in imputation credits (cl 2.5 of the Terms).

13. Distributions are payable at Kiwibank's absolute discretion (cl 2.6 of the Terms) although PPS holders will expect regular dividends to be paid where possible. In addition, the payment of any distribution on any distribution payment date is subject to:

    a) the payment of the distribution not resulting in a breach of Kiwibank's Conditions of Registration as at the time of the payment; and

    b) Kiwibank being solvent on the distribution payment date and remaining solvent immediately after such payment is made.

14. If a distribution is not paid on a scheduled distribution date for any reason it does not accrue and is not payable at any time (cl 2.7 of the Terms).

15. If a distribution on the PPS is not paid, then a "dividend-stopper" applies to Kiwibank, meaning that no dividends or other distributions may be paid on Kiwibank ordinary shares, or any payments with respect to any other capital instruments that rank equally with or junior to the PPS may be made, until Kiwibank pays PPS distributions in full on two subsequent scheduled distribution dates or there are no PPS outstanding (cl 2.10 of the Terms).

Redemption

16. The PPS are perpetual and have no fixed maturity date. PPS holders do not have a right to require redemption of their PPS (cl 3.5 of the Terms).
17. Under cl 3.1 of the Terms, all (but not some) of the PPS may be redeemed for:
    a) their issue price at the option of Kiwibank on an Optional Redemption Date, the first of which is the fifth anniversary of the Issue Date and then every five years after that date; or
    b) the greater of the issue price and the market value of the PPS on the occurrence of a Tax Event or Regulatory Event (as defined in the Terms).
18. Kiwibank's constitution at cl 4.1 provides that Kiwibank may repurchase any of its securities.
19. Kiwibank can only redeem the PPS if (cl 3.3 of the Terms):
    a) Either:
        i) prior to or concurrent with the redemption, Kiwibank replaces the PPS with a paid-up capital instrument of the same or better quality for RBNZ capital adequacy purposes, and with terms and conditions that are sustainable for the income capacity of the Kiwibank Group; or
        ii) Kiwibank does not intend to replace the PPS and it has demonstrated to the RBNZ's satisfaction that after the redemption the Kiwibank Group's capital is adequate; and
    b) Kiwibank has provided to the RBNZ any information and supporting documentation required;
    c) the RBNZ has given its prior written approval to the redemption; and
    d) Kiwibank will remain solvent immediately after the redemption, and otherwise comply with any applicable law, directive or requirement.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

a) Section GB 35(2) will not apply to the Arrangement.

b) Section BG 1 will not apply to the Arrangement.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 3 November 2021 and ending on 30 November 2026.

This Ruling is signed by me on the 4th day of October 2021.

Howard Davis
Group Leader, Tax Counsel Office

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.

COV 21/05: Variation to section 68CC(3) of the Tax Administration Act 1994

Variation

The Commissioner of Inland Revenue has, under the discretion provided under section 6I of the Tax Administration Act 1994, made the following statutory variation:

> For a criteria and methodologies notice in relation to the R&D tax credit for the 2020-2021 income tax year under section 68CC(3) of the Tax Administration Act 1994, the date by which that notice must be filed with the Commissioner is extended to the 7th day of December 2021 for a person with a balance date of 30 April 2021 or later.
>
> For a criteria and methodologies notice in relation to the R&D tax credit for the 2021-2022 income tax year under section 68CC(3) of the Tax Administration Act 1994, the date by which that notice must be filed with the Commissioner is extended to the last day of the third month before the end of the first income year for a person with a balance date between 28 February 2022 and 30 June 2022.
>
> This variation applies in circumstances where the planning or conduct of eligible research and development or the ability to appropriately obtain necessary information, seek advice and formulate an application under section 68CC of the Tax Administration Act 1994 on time has been materially delayed or disrupted by the COVID-19 outbreak and its effects.

Application date

This variation applies from 9 November 2021 to 30 June 2022.

Dated at Wellington on 9 November 2021.

Jonathan Rodgers
Group Leader – Tax Counsel Office
Inland Revenue

Background (material under this heading does not form part of the variation)

Summary of effect

1. This variation extends:
   - to 7 December 2021 the time by which a person with a late balance date, to be entitled to research and development tax credits under s LY 1 of the Income Tax Act 2007, must apply for criteria and methodology approval for the 2020-2021 income year;
   - by three months (to 30 November 2021 for customers with a February balance date and to 31 March 2022 for customers with a June balance date) the times by which a person with balance dates between 28 February 2022 and June 2022, to be entitled to research and development tax credits under s LY 1 of the Income Tax Act 2007, must apply for criteria and methodology approvals for the 2021-2022 income year.

Provisions affected

2. Section 68CC(3) of the Tax Administration 1994.

Application of variation

3. This variation applies to a person who is seeking the Commissioner's approval of their research and development activities by filing a criteria and methodologies application for the 2020-2021 or the 2021-2022 income years under s 68CC of the Tax Administration Act 1994. The variation recognises that the impact of COVID-19 may have delayed or disrupted the planning or conduct of research and development or the ability to obtain information, seek advice and formulate an application.

Associated variations

4. See also COV 21/01 "Variation to sections 33E and 68CC(3) of the Tax Administration Act 1994" dated 21 April 2021.

References

Legislative references

Tax Administration Act 1994: ss 6H and 6I, s 68CC.

LEGAL DECISIONS – CASE SUMMARIES

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.

Case summary

TRA finds taxpayer undertook land developments himself, omitted to return substantial income and filed returns he knew to be false; "dishonestly, and systematically evaded tax, then attempted to avoid the consequences of his deception."

Decision date: 29-October-2021

CSUM 21/10

Case

TRA 009/20 [2021] NZTRA 4

Legislative References

Income Tax Act 2007, ss CB 1, CB 3, CB 6, DA 1.

Tax Administration Act 1994, ss 6, 6A, 141E, 141FB.

Legal terms

Onus of proof, unreported income, shortfall penalty for evasion

Summary

The Taxation Review Authority (the "**TRA**") upheld the Commissioner's assessments for tax on unreported income and shortfall penalties for evasion.

The TRA concluded that the income from land sales in the disputed transactions was income under s CB 3 of the Income Tax Act 2007 ("**ITA**") or alternatively income under s CB 1 of the ITA.

The TRA also concluded that the disputant was liable for a shortfall penalty for evasion, finding he dishonestly and systematically evaded tax and attempted to avoid the consequences of his deception.

Impact

This case turned on the facts rather than the law. Is an example of a finding of dishonest and systematic evasion of tax.

Facts

The disputant entered into the purchase and sale of five properties. With one exception (bought and sold as bare land), he arranged the purchase of bare land, construction of a house on the land and sale of the completed house. The disputant claimed he was acting under power of attorney for Chinese nationals, managing the properties and receiving payments for his services arranging the land development and transactions.

However, the disputant personally controlled the property development, sales and acquisitions. The profit was not transferred to China and remained in a New Zealand bank account, with the disputant as the sole signatory. This profit was over and above the management fee the disputant declared in his tax returns over three tax years ending 21 March 2014 to 31 March 2016. The proceeds of the sale of properties were used by the disputant for personal expenses.

Issues

The central factual issue was:

- Whether the disputant was undertaking a property management role and the profit of sales belonged to someone else?

The broad issues for determination were:

- Whether the disputant derived income from carrying out an undertaking or scheme under s CB 3 of the ITA 2007?
- Alternatively, whether the disputant derived income from carrying on a business under s CB 1 of the ITA 2007?
- Whether the disputant deducted costs and expenses from the derived income under s DA 1 ITA 2007?
- Whether the disputant is liable for the evasion shortfall penalty

Decision

Disputant's role in the property transactions

The TRA found that this case was factual in nature, and turned almost entirely on the truth of the disputant's claim he had only a management role and the profits belonged to someone else.

The Commissioner disagreed with the disputant's assertion that he solely acted under power of attorney for others. The Commissioner's investigation included obtaining information from the People's Republic of China under the Double Tax Convection. The registered proprietors stated they had no knowledge or involvement in the properties and did not receive any benefits from them.

The TRA held the disputant's evidence was inconsistence, inconsistent with the written material, inconsistent with the statements of third parties, and implausible. It found that the disputant's use of powers of attorney had no substance behind it.

The TRA concluded that the evidence established the disputant was the true principle for the disputed transaction.

In reaching this conclusion, the TRA considered the following:

- The disputant has a New Zealand education and experience organising construction projects demonstrating his knowledge to follow business process.
- The disputant's claims of naivety and acting on the directions of others against his interests is implausible.
- The Commissioner provided evidence that the disputant had wealth inconstant with reported income.
- The denial of the people the disputant claimed were the principals, and that there was no evidence provided to show they were treated as such.

Derived Income from the disputant's role in property transactions

The Commissioner quantified the disputant's income derived from the five property transactions, based on the sale prices. This income was presented as assessable under s CB 3 of the ITA or, alternatively, CB 1 of the ITA.

The TRA held that due to the factual findings there can be no sensible argument that the derived income provisions do not apply. In agreeance with the Commissioner's assessment, the TRA found that either section could apply. There was no contention on this matter from the Disputant.

Deducted costs and expenses from the derived income

The TRA held that given the conclusion that the disputant derived income, the amount of taxable profit requires deduction of costs and expenses of deriving income.

The TRA concluded, that despite some contention when quantifying the deductions there was no basis to reject the Commissioners quantification in whole or in part.

Liability for the shortfall penalty

The TRA held that the findings make it inevitable that the disputant was liable for a shortfall penalty for evasion pursuant to s 141E of the Tax Administration Act 1994. The disputant understood his obligations but created a fictitious set of records where he pretended to be an agent acting under powers of attorney. The disputant was aware that the people he selected were not in New Zealand and were not liable for tax.

The TRA concluded that the disputant dishonestly, and systematically evaded tax then attempted to avoid the consequences of his deception.

About this document

These are brief case summaries, prepared by Inland Revenue, of decisions made by the Taxation Review Authority, the District Court, the High Court, the Court of Appeal or the Supreme Court in matters involving the Revenue Acts. For Taxation Review Authority matters, names have been anonymized. The findings of the court described in a case summary will no longer represent current law where the matter has been successfully appealed or subsequent amended legislation has been enacted.

TECHNICAL DECISION SUMMARIES

Technical decision summaries (TDS) are summaries of technical decisions made by the Tax Counsel Office. As this is a summary of the original technical decision, it may not contain all the facts or assumptions relevant to that decision. A TDS is made available for information only and is not advice, guidance or a "Commissioner's official opinion" (as defined in s 3(1) of the Tax Administration Act 1994). **You cannot rely on this document as setting out the Commissioner's position more generally or in relation to your own circumstances or tax affairs**. It is not binding and provides you with no protection (including from underpaid tax, penalty or interest.

TDS 21/01: GST: Non-profit body claiming input tax deductions

Technical decision summary - Adjudication

Decision date: 12 July 2021

Issue date: 18 October 2021

Subjects | Ngā kaupapa

GST: Cancellation of GST registration, input tax deductions, supplies of donated goods and services.

Abbreviations | Whakapotonga kupu

The abbreviations used in this document include:

Commissioner	Commissioner of Inland Revenue
GST	Goods and services tax
TAA	Tax Administration Act 1994

Taxation laws | Ngā ture take

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

Facts | Ngā meka

1. The non-profit body is registered under the Charities Act 2005 as a charitable entity. It received income from donations and from making supplies of donated goods and services.
2. The non-profit body was registered for GST. Its GST returns included sales of donated goods and services and input tax deductions claimed for expenses for its leased premises, e . rent, water, rates, power and insurance.

Issues | Ngā take

3. The issues considered in this dispute were:
   - whether the non-profit body was entitled to the input tax deductions it claimed; and
   - whether the non-profit body's GST registration should be cancelled.
4. A preliminary issue on the onus and standard of proof was also considered.

Decisions | Ngā whakatau

5. The Tax Counsel Office decided that:
   - the non-profit body was not entitled to the input tax deductions it claimed; and
   - the non-profit body's GST registration should be cancelled from the date it was GST registered.

Reasons for decisions | Ngā take mō ngā whakatau

Preliminary Issue | Take tōmua: Onus and standard of proof

6. The onus of proof in civil proceedings[1] is on the taxpayer, except for shortfall penalties for evasion or similar act, or obstruction.[2] The taxpayer must prove that an assessment is wrong, why it is wrong, and by how much it is wrong.[3]
7. The standard of proof in civil proceedings is the balance of probabilities.[4]This standard is met if it is proved that a matter is more probable than not. Whether the non-profit body has discharged the onus of proof is considered in the other issues.

Issue 1 | Take tuatahi: Input tax deductions

8. Input tax is charged under s 8(1) on the supply of goods or services acquired by a person (s 3A). In calculating the amount of GST payable, a GST registered person may deduct input tax to the extent to which the goods or services are used for, or are available for use in, making taxable supplies (s 20(3C)(a)).
9. A "taxable supply" is a supply of goods and services in New Zealand that is charged with GST under s 8.[5] However, s 8 does not impose GST on exempt supplies.
10. Goods and services acquired by a non-profit body are treated as being used in the course or furtherance of their taxable activity to the extent the goods and services are not used for making exempt supplies (s 20(3K)).
11. The supply by a non-profit body of donated goods and services is an exempt supply (s 14(1)(b)). Donated goods and services are defined as goods and services gifted to a non-profit body that are intended for use in the carrying on or carrying out of the purposes of the non-profit body.[6]Even if made for consideration, a supply by a non-profit body of donated goods and services will be exempt.[7]

12 The non-profit body may have provided goods and services for consideration but these were exempt supplies. This is because the goods and services it supplied were donated. The non-profit body had not shown that it was making any taxable supplies. Therefore, it was not entitled to the input tax deductions it claimed.

Issue 2 | Take tuarua: Cancellation of GST registration

13. The Commissioner may cancel a person's GST registration if the Commissioner is satisfied that the person is not carrying on a taxable activity (s 52(5)). The cancellation may be retrospective to the date the person was GST registered if the Commissioner is satisfied that the person did not carry on any taxable activity from that date (s 52(5A)).
14. A taxable activity is an activity carried on continuously or regularly by a person that involves, or is intended to involve, the supply of goods and services to another person for a consideration (s 6(1)(a)). However, a taxable activity does not include any activity to the extent to which the activity involves the making of exempt supplies (s 6(3)(d)).
15. The non-profit body only made exempt supplies and so the non-profit body's activity was not a taxable activity. Therefore, the non-profit body's GST registration should be cancelled from the date it was GST registered.

[1] Challenge proceedings (ie, the proceedings that would follow if this dispute proceeds to the Taxation Review Authority or a court) are civil proceedings.

[2] Section 149A(2) of the Tax Administration Act 1994 (TAA).

[3] *Buckley & Young Ltd v CIR* (1978) 3 NZTC 61,271 (CA); *Beckham v CIR* (2008) 23 NZTC 22,066 (CA).

[4] Section 149A(1) of the TAA; *Yew v CIR* (1984) 6 NZTC 61,710 (CA); *Birkdale Service Station Ltd v CIR* (1999) 19 NZTC 15,493 (HC); *Case X16* (2005) 22 NZTC 12,216; *Case Y3* (2007) 23 NZTC 13,028.

[5] See definition of "taxable supply" in s 2.

[6] Definition of "non-profit body" in s 2.

[7] *Case M40* (1990)12 NZTC 2,247 at 2,252-2,254.

TECHNICAL DECISION SUMMARIES

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TDS 21/02: GST – Eligibility to input tax deductions

Technical decision summary - Adjudication

Decision date: 23 June 2021

Issue date: 19 October 2021

Subjects | Ngā kaupapa

GST: agency, cancellation of registration, input tax deductions, non-resident supplier; TAA: claimed procedural defects of assessment; onus and standard of proof.

Abbreviations | Whakapotonga kupu

The abbreviations used in this document include:

CCS	Customer and Compliance Services, Inland Revenue
Commissioner	Commissioner of Inland Revenue or CIR
GST	Goods and services tax
GST Act	Goods and Services Tax Act 1985
TAA	Tax Administration Act 1994
TRA	Taxation Review Authority

Taxation laws | Ngā ture take

All legislative references are to the Goods and Services Tax Act 1985 (**GST Act**) unless otherwise specified.

Facts | Ngā meka

1. Company A is an overseas incorporated company and is registered as an overseas company under the New Zealand Companies Act 1993.
2. It is registered for GST in New Zealand with its taxable activity described as ticket selling for non-resident airlines.
3. Company A maintains it buys and sells airline flights in its own right and not as an agent of the airlines.
4. Company A's GST returns show zero-rated supplies of flights sold and input tax deductions for GST charged by the airlines on supply of flights and the supply of virtual office supplies.

Issues | Ngā take

5. The main issues considered in this dispute were:
   - concerns about Customer and Compliance Services (**CCS**), Inland Revenue's handling of this dispute;
   - whether Company A bought and sold airline flights in its own right;
   - if Company A bought and sold the flights in its own right, whether its supply of the flights was zero-rated international carriage;
   - whether Company A is entitled to the input tax deductions it claimed;
   - whether Company A's GST registration should be cancelled;
   - if Company A's GST registration should be cancelled, whether it could register for GST as a non-resident supplier.
6. There was also a preliminary issue on the onus and standard of proof.

Decisions | Ngā whakatau

7. The Tax Counsel Office decided that:
   - the concerns that Company A raised about the handling of this dispute by CCS is not supported by the evidence. In any event, as stated by the High Court in *Dandelion Investments v CIR*, the proper course for challenging the assessments is not to attack the method by which the Commissioner made them but to provide the Taxation Review Authority (**TRA**) or court with the evidence and arguments necessary for it to deal with the matter in the manner the taxpayer contends;[1]
   - company A did not buy and sell the flights in its own right. It sold the flights on behalf of the airlines as an agent;
   - the conclusion that Company A did not buy and sell the flights in its own right makes it unnecessary to consider whether the supply of the flights was zero-rated international carriage;
   - company A is not entitled to the input tax deductions it claimed;
   - company A's GST registration should be cancelled from the date it was GST registered;
   - company A has not shown that it is entitled to be GST registered as a non-resident supplier.

Reasons for decisions | Ngā take mō ngā whakatau

Preliminary Issue | Take tōmua: Onus and standard of proof

8. The onus of proof in civil proceedings[2] is on the taxpayer, except for shortfall penalties for evasion or similar act, or obstruction.[3]The taxpayer must prove that an assessment is wrong, why it is wrong, and by how much it is wrong.[4]
9. The standard of proof in civil proceedings is the balance of probabilities.[5]This standard is met if it is proved that a matter is more probable than not. Whether Company A has discharged the onus of proof is considered in the other issues.

Issue 1 | Take tuatahi: Concerns raised by Company A about CCS's handling of this dispute

10. Company A expressed concerns about delays and changes and apparent inconsistencies in views taken by CCS during the course of this dispute. Company A contended that CCS deliberately took action to prevent it from receiving GST refunds.
11. Changes in the Commissioner's view are understandably frustrating for taxpayers. However, the Commissioner:
    - must determine a taxpayer's tax liability according to law, and
    - is obliged to change her view if an earlier view is considered incorrect.[6]

[1] *Dandelion Investments Ltd v CIR* (1996) 17 NZTC 12,689 (HC). This approach was expressly approved by the Court of Appeal in *Dandelion Investments Ltd v CIR* (2003) 21 NZTC 18,010 (CA) at [62].

[2] Challenge proceedings (ie, the proceedings that would follow if this dispute proceeds to the Taxation Review Authority or a court) are civil proceedings.

[3] Section 149A(2) of the TAA.

[4] *Buckley & Young Ltd v CIR* (1978) 3 NZTC 61,271 (CA); *Beckham v CIR* (2008) 23 NZTC 22,066 (CA).

[5] Section 149A(1) of the TAA; *Yew v CIR* (1984) 6 NZTC 61,710 (CA); *Birkdale Service Station Ltd v CIR* (1999) 19 NZTC 15,493 (HC); *Case X16* (2005) 22 NZTC 12,216; *Case Y3* (2007) 23 NZTC 13,028.

[6] *CIR v Michael Hill Finance (NZ) Ltd* [2016] NZCA 276, (2016) 27 NZTC 22-056 at [29] and [43]; *Westpac v CIR* (2008) 23 NZTC 21,694 (CA) at [77]; *Case N19* (1991) 13 NZTC 3,158 at [49].

12. Any procedural defects in an assessment can be addressed by the TRA or a court if a dispute proceeds to challenge stage.[7] They will consider the assessment again and can make any assessment the Commissioner can make. In reaching their own decision, the TRA or court can cure any defects in the Commissioner's assessment.
13. Therefore, as stated by the High Court in *Dandelion*, the proper course for challenging the assessment is not to attack the method by which the Commissioner made it but to provide the TRA or court with the evidence and arguments necessary for it to deal with the matter in the manner the taxpayer contends.
14. The evidence in this dispute does not show CCS was motivated by any improper purpose or otherwise acted deliberately to delay or prevent Company A from receiving GST refunds.
15. In addition, it seems reasonable for CCS to require Company A to provide evidence to show it was making zero-rated supplies. This is given that the Commissioner has a statutory duty to assess the correct amount of tax and that the onus is on Company A to show it was making zero-rated supplies.
16. It is also apparent from the evidence that deciding the correct application of the law has been made more difficult by the lack of documentation provided by Company A to show all relevant contractual arrangements it entered into and how the GST Act should apply. The lack of information may have contributed to the changes in view and delays.
17. In any event, the proper course for challenging CCS's proposed adjustments is for Company A to provide the evidence and arguments necessary for the issues to be resolved in the manner it contends.

Issue 2 | Take tuarua: Whether Company A bought and sold airline flights in its own right

18. The nature of a supply is determined from the contractual arrangements entered into and not by what is in broad substance being supplied:
    - Parties to a supply are determined by reference to the general principles of contract law.[8]
    - GST Act provisions are directed to the contractual arrangements between the supplier and the recipient of the supply.[9]
    - The true nature of a transaction is ascertained by a careful consideration of the legal arrangements actually entered into.[10]
19. Under provisions of the GST Act relating to agents, generally, and unless the agent and principal agree otherwise:
    - supplies made by an agent for and on behalf of any other person who is their principal are deemed to be made by the principal and not the agent (s 60(1));
    - supplies made to an agent acting on behalf of another person who is their principal is deemed to be made to the principal and not the agent (s 60(2)).
20. With effect from 1 October 2016 a principal and agent can agree that the agent and not the principal is treated as making the taxable supply (s 60(1AB)). A principal and agent can also agree that:
    - a supply is treated as two supplies, one from the principal to the agent and one from the agent to the recipient (s 60(1B));
    - with effect from 30 March 2017, a supply by a person is treated as being two supplies, one from the person to the agent and one from the agent to the principal (s 60(2B)).
21. The evidence for this dispute does not include any agreement with any airline other than Airline X to show the nature of the contractual relationship and transactions between Company A and the airlines. The agreement with Airline X shows that Company A sold flights on behalf of Airline X as an agent.
22. Further, the evidence does not include any document recording Company A and Airline X having agreed that:
    - Company A and not Airline X would be treated as supplying flights;
    - any supply of flights would be treated as two supplies, one from Airline X to Company A and one from Company A to the recipient.
23. Other evidence including invoices, e-Tickets and International Air Transport Association documentation is also consistent with Company A selling the flights on behalf of the airlines as agent.

[7] *Tannadyce Investments Ltd v CIR* [2011] NZSC 158, (2011) 25 NZTC 20-103.

[8] *CIR v Capital Enterprises Ltd* (2002) 20 NZTC 17,511 (HC) at [50]. See also *CIR v Databank Systems Ltd* (1990) 12 NZTC 7,227 (PC).

[9] *Wilson & Horton Ltd v CIR* (1995) 17 NZTC 12,325 (CA) at 12,328.

[10] *CIR v Gulf Harbour Development Ltd* (2004) 21 NZTC 18,915 (CA).

24. The evidence does not include any agreements showing any contractual arrangements between Company A and overseas tour operators. Nor does the evidence include any invoices showing the on-sale of the flights by Company A to overseas tour operators or any other persons or any other documentation supporting any such sales.
25. In summary, the evidence does not show that Company A purchased the flights outright from the airlines and on-sold them to overseas tour operators. Rather, the evidence suggests that Company A sold the flights on behalf of the airlines as an agent. In that case the airlines rather than Company A were supplying the flights.

Issue 3 | Take tuatoru: Whether Company A's supply of the flights was zero-rated international carriage

26. CCS argues that, if Company A bought and sold the flights in its own right, it has not shown that the flights were zero-rated as international carriage (s 11A(1)(b)). Company A argues that the flights were zero-rated as international carriage.
27. It has been decided that Company A did not buy and sell the flights in its own right. This decision makes it unnecessary to consider whether the supply of the flights was zero-rated as international carriage. Company A was not supplying any flights that could be zero-rated international carriage.

Issue 4 | Take tuawhā: Whether Company A is entitled to the input tax deductions it claimed

28. "Input tax" is tax charged under s 8(1) on a supply of goods or services acquired by a registered person (s 3A). Section 8 imposes GST on a supply in New Zealand of goods and services by a registered person in the course or furtherance of a taxable activity.
29. Input tax may be deducted under s 20 to the extent to which the goods or services to which it relates are used for, or are available for use in, making taxable supplies. A "taxable supply" is defined in s 2 to mean a supply of goods and services in New Zealand that is charged with GST under s 8.
30. The parties had proceeded on the basis that the relevant supplies were supplies of services. Relevantly, services are supplied in New Zealand if the supplier is:
    - resident in New Zealand (s 8(2)). A company is resident in New Zealand:
        - if it is incorporated,[11] it has its head office,[12] its centre of management,[13] or its directors exercise control of it,[14] in New Zealand; or[15]
        - to the extent it carries on in New Zealand a taxable activity or any other activity while having a fixed or permanent place in New Zealand relating to that taxable activity or other activity.[16]To be carrying on a taxable activity in New Zealand, a person must be making supplies in New Zealand for a consideration;[17] or
    - non-resident and the services are physically performed in New Zealand by a person who is in New Zealand at the time the services are performed (s 8(3)).
31. Also, generally, to claim an input tax deduction the recipient of a supply must hold and retain a "tax invoice" relating to the supply (s 20(2)) (except in certain circumstances, such as a supply for a consideration of $50 or less (s 24(5)).[18]
32. Company A claimed input tax deductions relating to supplies of flights. It seems likely that Company A also claimed input tax deductions for "virtual office" services it purchased.
33. For Company A to be entitled to the input tax deductions claimed:
    - it must have acquired the services to which the input tax relates;
    - the services must have been used for, or available for use in, making taxable supplies; and
    - it must have generally held tax invoices relating to the supplies.

[11] Section 13 of the Companies Act 1993.

[12] Based on definitions of "office" and "home" in the *Concise Oxford English Dictionary* (12th ed, Oxford University Press, New York, 2011), a company would be resident in New Zealand if it uses a room, rooms, or building in New Zealand as its chief or principal place of business for clerical, administrative, or similar work.

[13] *De Beers Consolidated Mines Ltd v Howe* [1906] AC 455 (HL) and *New Zealand Forest Products Finance NV v CIR* (1995) 17 NZTC 12,073 (HC).

[14] *Case 11/2011* (2011) 25 NZTC ¶1-011; *Vinelight Nominees Ltd v CIR* (2012) 25 NZTC ¶20-155 (HC).

[15] The s 2(1) definition of "resident" refers to s YD 2 (residence of companies) of the Income Tax Act 2007.

[16] Proviso (a) of the s 2(1) definition of "resident".

[17] Section 6.

[18] *Case 1/2012* (2012) 25 NZTC 1-013; *Case 3/2016* (2016) 27 NZTC 3-025.

34. Company A has not shown that it purchased the flights outright from the airlines. This means that Company A has not shown that it acquired the services to which the input tax relates. Therefore, Company A was not entitled to the input tax deductions it claimed for the flights.
35. It seems more probable than not that Company A acquired virtual office services (including telephone answering, fax handling, mail services, and an address) for which it claimed input tax deductions. However, Company A has not shown that it supplied flights in its own right. This means that Company A cannot have used the virtual office services in making taxable supplies of the flights.
36. Company A may have made supplies of services when it arranged the sale of flights (**Arranging Services**). However, to be taxable supplies, any supplies of Arranging Services must have been made in New Zealand. Any such supplies of Arranging Services may have been made in New Zealand if they were performed in New Zealand by a person in New Zealand at the time the services were performed (s 8(3)), or Company A was resident in New Zealand (s 8(2)).
37. Company A had no staff or other persons in New Zealand performing Arranging Services such that s 8(3) would apply to treat the services as supplied in New Zealand.
38. Also, Company A was not resident in New Zealand such that s 8(2) would apply to treat the services as supplied in New Zealand. Firstly, although Company A was registered under the Companies Act 1993 as an overseas company, it was not incorporated in New Zealand. In addition, neither its director nor any of its staff were in New Zealand. This makes it unlikely that it had its head office or centre of management in New Zealand, or that its director exercised control of it in New Zealand.
39. Company A argued that its use of the internet meant that its director controlled it in New Zealand without being physically present in New Zealand. However, it remains the law that control of a company by a sole director is exercised in the country in which the director is physically located when they make their decisions.
40. Second, Company A has not shown that it was making supplies of the flights in New Zealand in its own right. Even if the Arranging Services comprised a taxable activity, Company A has not shown the taxable activity was carried on in New Zealand. Nor has Company A shown that it was carrying on any other activity in New Zealand. Therefore, Company A was not entitled to the input tax deductions it claimed for the Arranging Services.
41. This makes it unnecessary to decide whether Company A had a fixed or permanent place in New Zealand. Nevertheless, the virtual office services would not ordinarily be regarded as a space that could be occupied. And, even if they were a fixed or permanent place in New Zealand, the place must have related to a taxable activity or other activity carried on by Company A in New Zealand.
42. This also makes it unnecessary to decide whether Company A held tax invoices for the Arranging Services. However, Company A has not shown that it held tax invoices for all of the Arranging Services for which it claimed input tax deductions.

Issue 5 | Take tuarima: Whether Company A's GST registration should be cancelled

43. The Commissioner may cancel a person's GST registration if satisfied that the person is not carrying on a taxable activity. If the person is non-resident, the Commissioner must be satisfied that the person is not carrying on a taxable activity in New Zealand. The cancellation date may be retrospective to the date the person was GST registered if the Commissioner is satisfied the person was not carrying on a taxable activity or a taxable activity in New Zealand, as the case may be, from that date (ss 52(5), 52(5A), and 52(7)).
44. It has been concluded that Company A was not resident in New Zealand. Accordingly, to cancel Company A's GST registration, the Commissioner must be satisfied that Company A is not carrying on a taxable activity in New Zealand.
45. It has also been concluded that Company A was not carrying on a taxable activity in New Zealand. Therefore, the Commissioner may cancel Company A's GST registration and the cancellation date may be retrospective to the date Company A was GST registered.

Issue 6 | Take tuaono: Whether Company A could register for GST as a non-resident supplier

46. Section 54B allows non-residents to register for GST and claim input tax deductions subject to certain requirements. However, Company A does not argue, and has not provided any evidence to show, that it meets all of the s 54B requirements.
47. Even if Company A was GST registered under s 54B, registration would not entitle it to claim any input tax deductions on flights it sold on behalf of the airlines as an agent. This is because Company A does not acquire the flights outright. Based on the evidence, at most, Company A could only claim the modest amounts of input tax charged on virtual office services acquired by it.

TECHNICAL DECISION SUMMARIES

Technical decision summaries (TDS) are summaries of technical decisions made by the Tax Counsel Office. As this is a summary of the original technical decision, it may not contain all the facts or assumptions relevant to that decision. A TDS is made available for information only and is not advice, guidance or a "Commissioner's official opinion" (as defined in s 3(1) of the Tax Administration Act 1994). **You cannot rely on this document as setting out the Commissioner's position more generally or in relation to your own circumstances or tax affairs**. It is not binding and provides you with no protection (including from underpaid tax, penalty or interest.

TDS 21/03: Liability for shortfall penalties

Technical decision summary - Adjudication

Decision date: 29 June 2021

Issue date: 4 November 2021

Subjects | Ngā kaupapa

TAA: Shortfall penalties, onus and standard of proof

Abbreviations | Whakapotonga kupu

The abbreviations used in this document include:

Commissioner	Commissioner of Inland Revenue or CIR
GST	Goods and services tax
CCS	Customer and Compliance Services, Inland Revenue
TAA	Tax Administration Act 1994

Taxation laws | Ngā ture take

All legislative references are to the Tax Administration Act 1994 (**TAA**) unless otherwise specified.

Facts | Ngā meka

1. The taxpayers were shareholders of Company X. One was the sole director of Company X (the subject of TDS 21/04) and the other managed the businesses of Company X.
2. The GST returns of Company X were reassessed by Customer and Compliance Services (**CCS**), Inland Revenue on the basis that unexplained deposits made into bank accounts of the taxpayers and a family trust are undisclosed cash sales of Company X for GST purposes. These assessments have been confirmed by the Tax Counsel Office of Inland Revenue.
3. CCS reassessed the income tax returns of the taxpayers to include additional shareholder salary amounts. The amount of additional shareholder salary was calculated based on an equal share of the undisclosed cash sales of Company X.
4. CCS also imposed on each of the shareholders a shortfall penalty for evasion. The taxpayers have accepted the assessment of the additional shareholder salary but dispute the imposition of the shortfall penalty.

Issues | Ngā take

5. The issue considered in this dispute is:
    - Whether the taxpayers are liable for a shortfall penalty for evasion or, in the alternative, for gross carelessness or not taking reasonable care.

6. There was also a preliminary issue on the onus and standard of proof.

Decisions | Ngā whakatau

7. The Tax Counsel Office decided that:
    - The taxpayers of the company are liable for a shortfall penalty for evasion. Alternatively, the shareholders are liable for shortfall penalties for gross carelessness or not taking reasonable care. Any shortfall penalties for which the shareholders are liable are reduced by 50% for previous behaviour.

Reasons for decisions | Ngā take mō ngā whakatau

Preliminary Issue | Take tōmua: Onus and standard of proof

8. The onus of proof in civil proceedings[1] is on the taxpayer, except for shortfall penalties for evasion or similar act, or obstruction.[2] The taxpayer must prove that an assessment is wrong, why it is wrong, and by how much it is wrong.[3]
9. The standard of proof in civil proceedings is the balance of probabilities.[4] This standard is met if it is proved that a matter is more probable than not. Whether the shareholders have discharged the onus of proof is considered in the relevant issues.

Issue 1 | Take tuatahi: Shortfall penalties

Shortfall penalty for evasion

10. Section 141E(1)(a) imposes a shortfall penalty for evasion on a taxpayer if the following requirements are satisfied:[5]
    - The taxpayer has taken a tax position.
    - Taking the tax position has resulted in a tax shortfall.
    - The taxpayer has evaded the assessment or payment of tax . Evasion requires an intention to avoid the assessment or payment of tax known to be chargeable.
11. The penalty payable for evasion or similar act is 150% of the resulting tax shortfall.
12. The onus of proof rests with the Commissioner to show that a taxpayer is liable for a shortfall penalty for evasion under s 141E.[6] This is different from the other shortfall penalties where the onus of proof is on the taxpayer. The standard of proof is the balance of probabilities.[7]

Shortfall penalty for gross carelessness

13. Section 141C of the TAA imposes a shortfall penalty for gross carelessness on a taxpayer if the following requirements are satisfied:[8]
    - The taxpayer has taken a tax position.
    - Taking the tax position has resulted in a tax shortfall.
    - The taxpayer has been grossly careless in taking the taxpayer's tax position.
14. The penalty payable for gross carelessness is 40% of the resulting tax shortfall.

[1] Challenge proceedings (ie, the proceedings that would follow if this dispute proceeds to the TRA or a court) are civil proceedings.

[2] Section 149A(2).

[3] *Buckley & Young Ltd v CIR* (1978) 3 NZTC 61,271 (CA); *Beckham v CIR* (2008) 23 NZTC 22,066 (CA).

[4] Section 149A(1); *Yew v CIR* (1984) 6 NZTC 61,710 (CA); *Birkdale Service Station Ltd v CIR* (1999) 19 NZTC 15,493 (HC); *Case X16* (2005) 22 NZTC 12,216; *Case Y3* (2007) 23 NZTC 13,028.

[5] The shortfall penalty for evasion or a similar act is considered in the Interpretation Statement: Shortfall Penalty—Evasion as published in *Tax Information Bulletin* Vol 18, No 11 (December 2006). Further detail is included in the related TDS 21/04 for Company X.

[6] Section 149A(2) of the TAA.

[7] Section 149A(1) of the TAA.

[8] The shortfall penalty for gross carelessness is considered in the Interpretation Statement: Shortfall Penalty for Gross Carelessness as published in *Tax Information Bulletin* Vol 16, No 8 (September 2004). Further detail is included in the related TDS 21/04 for Company X.

Shortfall penalty for not taking reasonable care

15. Section 141A imposes a shortfall penalty for not taking reasonable care on a taxpayer if the following requirements are satisfied:[9]
    - The taxpayer has taken a tax position.
    - Taking the tax position has resulted in a tax shortfall.
    - The taxpayer has not taken reasonable care in taking the taxpayer's tax position.
16. The penalty payable for not taking reasonable care is 20% of the resulting tax shortfall.

Application of the penalties

17. The taxpayers took tax positions that resulted in tax shortfalls. The taxpayers are liable for evasion shortfall penalties because:
    - In the income years in dispute the taxpayers received shareholder salaries from Company X which they both included in their tax returns. Accordingly, they knew that they were required to include amounts received from Company X for their personal benefit in their income tax returns.
    - The taxpayers filed their income tax returns without including any of the undisclosed cash sales of Company X paid into their joint private bank account and into the bank account of a family trust knowing that the returns were incorrect and misleading and in breach of their tax obligations. Even if the taxpayers did not know the amounts were income, at the very least, they were inadvertent to that probability and recklessly filed their returns without including the amounts, not caring whether the returns were correct or not. There is no evidence that they made enquiries to determine whether the amounts were income or not.
18. If it is concluded that the requirements of the evasion shortfall penalty are not satisfied the shareholders are liable for shortfall penalties for gross carelessness. Filing their income tax returns without including any of the undisclosed cash sales of Company X paid into their joint private bank account and into the bank account of a family trust shows a complete disregard by the taxpayers for the consequences of their actions. This factor created a high risk of the tax shortfalls occurring. That risk and its consequences would have been foreseen by a reasonable person in the circumstances.
19. Further, if it is concluded that the requirements of the gross carelessness shortfall penalty are not satisfied the shareholders are liable to shortfall penalties for not taking reasonable care. A reasonable person would have foreseen as a reasonable probability of not including amounts received from Company X for their personal benefit in their income tax returns, that a tax shortfall would arise.
20. Any shortfall penalties for which the shareholders are liable are reduced by 50% under s 141FB for previous behaviour.

[9] The shortfall penalty for not taking reasonable care is considered in the Interpretation Statement: Shortfall penalty for not taking reasonable care as published in *Tax Information Bulletin* Vol 17, No 9 (November 2005). Further detail is included in the related TDS 21/XX for Company X.

TECHNICAL DECISION SUMMARIES

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TDS 21/04: GST – Undisclosed cash sales and liability for shortfall penalties

Technical decision summary - Adjudication

Decision date: 29 June 2021

Issue date: 4 November 2021

Subjects | Ngā kaupapa

GST: Cash sales; TAA: Shortfall penalties, onus and standard of proof

Abbreviations | Whakapotonga kupu

The abbreviations used in this document include:

Commissioner	Commissioner of Inland Revenue or CIR
GST	Goods and services tax
GST Act	Goods and Services Tax Act 1985
TAA	Tax Administration Act 1994

Taxation laws | Ngā ture take

All legislative references are to the Tax Administration Act 1994 (**TAA**) unless otherwise specified.

Facts | Ngā meka

1. Company X owned and operated several retail establishments. Company X is registered for GST.
2. During the GST periods in dispute bank statement and vouching data showed unexplained cash deposits made into the joint private bank account of two shareholders of Company X and into the bank account of a family trust.

Issues | Ngā take

3. The issues considered in this dispute were:
   - Whether the unexplained deposits made into the bank accounts of the shareholders and the family trust are undisclosed cash sales of Company X for GST purposes.
   - Whether Company X is liable for shortfall penalties for evasion under s 141E or, in the alternative, gross carelessness under s 141C or not taking reasonable care under s 141A.
4. There was also a preliminary issue on the onus and standard of proof.

Decisions | Ngā whakatau

5. The Tax Counsel Office decided that:
   - The unexplained deposits made into the bank accounts of the shareholders and the family trust are undisclosed cash sales of Company X for GST purposes.
   - Company X is liable for evasion shortfall penalties for evasion. Alternatively, Company X is liable for shortfall penalties for gross carelessness or not taking reasonable care. Any shortfall penalties for which Company X is liable are reduced by 50% for previous behaviour.

Reasons for decisions | Ngā take mō ngā whakatau

Preliminary Issue | Take tōmua: Onus and standard of proof

6. The onus of proof in civil proceedings[1] is on the taxpayer, except for shortfall penalties for evasion or similar act, or obstruction.[2] The taxpayer must prove that an assessment is wrong, why it is wrong, and by how much it is wrong.[3]
7. The standard of proof in civil proceedings is the balance of probabilities.[4] This standard is met if it is proved that a matter is more probable than not. Whether Company X has discharged the onus of proof is considered in the relevant issues.
8. An assessment made by the Commissioner cannot be arbitrary. She must make the best judgement she can on the information in her possession as to the amount of taxable income and the amount of tax payable. In some cases, a taxpayer may be able to discharge the onus of proof by showing that the assessment is arbitrary or demonstrably unfair.[5]

Issue 1 | Take tuatahi: Whether the unexplained deposits are undisclosed cash sales of Company X for GST purposes

9. In relation to unexplained amounts received by a taxpayer it is for the taxpayer to prove that the Commissioner's assessment is incorrect. The taxpayer must do more than simply provide a credible possible alternative explanation for the amounts.[6] It will depend on the facts of the particular case as to what evidence will be required to discharge a taxpayer's onus of proof.[7]
10. The taxpayer can meet the onus of proof if they provide specific details of other sources of funds that are capital or non-taxable in nature.[8] In *Case 8/2017*, Judge Sinclair stated that it would "be necessary for there to be corroborative evidence, in particular contemporaneous evidence and records, in support of a disputant's ex post facto explanations".[9]
11. Company X did not discharge the onus of showing on the balance of probabilities that the unexplained cash deposits made into the bank accounts of the shareholders and the family trust were not undisclosed cash sales from its business for these reasons:
    - The GST assessments were not arbitrary. The GST assessments were based on bank deposit information and vouching data. Cash sales analysis supports the view that the assessments were reasonable (being less than half of the industry average).
    - Company X did not provide sufficient evidence to support its explanations regarding the source of any of the unexplained deposits or the additional business expenditure it said was incurred in generating additional cash sales from its business.

[1] Challenge proceedings (ie, the proceedings that would follow if this dispute proceeds to the Taxation Review Authority or a court) are civil proceedings.

[2] Section 149A(2) of the TAA.

[3] *Buckley & Young Ltd v CIR* (1978) 3 NZTC 61,271 (CA); *Beckham v CIR* (2008) 23 NZTC 22,066 (CA).

[4] Section 149A(1) of the TAA; *Yew v CIR* (1984) 6 NZTC 61,710 (CA); *Birkdale Service Station Ltd v CIR* (1999) 19 NZTC 15,493 (HC); *Case X16* (2005) 22 NZTC 12,216; *Case Y3* (2007) 23 NZTC 13,028.

[5] *Lowe v CIR* (1981) 5 NZTC 61,006 (CA); *CIR v Canterbury Frozen Meat Co Ltd* (1994) 16 NZTC 11,150 (CA); *CIR v New Zealand Wool Board* (1999) 19 NZTC 15,476 (CA).

[6] *Case S30* (1995) 17 NZTC 7,207 and *Case E69* (1982) 5 NZTC 59,378.

[7] See *Case 2/2017* [2017] NZTRA 02, (2017) 28 NZTC 4-001 at [7] and [9];

[8] *Case L40* (1989) 11 NZTC 1,249

[9] *Case 8/2017* [2017] NZTRA 08, (2017) 28 NZTC 4-007 at [46].

Issue 2 | Take tuarua: Shortfall penalties

Shortfall penalty for evasion

12. Section 141E(1)(a) imposes a shortfall penalty for evasion on a taxpayer if the following requirements are satisfied:[10]
    - The taxpayer has taken a tax position. A tax position is a position or approach to tax under a tax law as taken in or in respect of a tax return, income statement, or due date.[11]
    - Taking the tax position has resulted in a tax shortfall. A tax shortfall is the difference between the tax effects of the correct tax position and the tax effects of the taxpayer's tax position.[12]
    - The taxpayer has evaded the assessment or payment of tax. Evasion requires an intention to avoid the assessment or payment of tax known to be chargeable:
      - The element of intention will be satisfied if the taxpayer knows that their action or omission will breach a tax obligation. There must be some blameworthy act or omission on the part of the taxpayer. The required intent for evasion can be inferred from surrounding circumstances and conduct.[13]
      - Recklessness can amount to evasion and involves the conscious taking of risk. Recklessness will be proven where:[14]
        - Facts actually known to the taxpayer were such that they must have put the taxpayer on inquiry that a tax obligation may not be met.
        - The taxpayer made a conscious decision to ignore the facts without making further inquiry.
13. The penalty payable for evasion or similar act is 150% of the resulting tax shortfall.
14. The onus of proof rests with the Commissioner to show that a taxpayer is liable for a shortfall penalty for evasion under s 141E.[15] This is different from the other shortfall penalties where the onus of proof is on the taxpayer. The standard of proof is the balance of probabilities.[16]

Shortfall penalty for gross carelessness

15. Section 141C of the TAA imposes a shortfall penalty for gross carelessness on a taxpayer if the following requirements are satisfied:[17]
    - The taxpayer has taken a tax position.
    - Taking the tax position has resulted in a tax shortfall.
    - The taxpayer has been grossly careless in taking the taxpayer's tax position. Gross carelessness means doing or not doing something in a way that, in all of the circumstances, suggests or implies a complete or high level of disregard for the consequences (s 141C(3)):
      - Gross carelessness is characterised by conduct which creates a high risk of a tax shortfall occurring where that risk and its consequences would have been foreseen by a reasonable person in the circumstances.[18]
      - The test for gross carelessness is not whether the taxpayer actually foresaw the probability that their act or omission would cause a tax shortfall but whether a reasonable person would have foreseen that probability. Whether the taxpayer has acted intentionally is not a consideration.[19]
      - A person who takes reasonable care is not grossly careless.[20]

[10] The shortfall penalty for evasion or a similar act is considered in the Interpretation Statement: Shortfall Penalty—Evasion as published in *Tax Information Bulletin* Vol 18, No 11 (December 2006).

[11] Definitions of "tax position" and "taxpayer's tax position" in s 3 of the TAA.

[12] Definition of "tax shortfall" in s 3 of the TAA.

[13] *Taylor v Attorney-General* [1963] NZLR 261 (SC); *Lloyds Bank Ltd v Marcan* [1973] 2 All ER 359; *Case H90* (1986) 8 NZTC 619; *Case N47* (1991) 13 NZTC 3,388; *R v G* [2013] NZCA 146.

[14] *Case H90* (1986) 8 NZTC 619; *R v Harney* [1987] 2 NZLR 576 (CA); *Case P29* (1992) 14 NZTC 4,213; *Case S100* (1996) 17 NZTC 7,626; *R v G* [2013] NZCA 146.

[15] Section 149A(2) of the TAA.

[16] Section 149A(1) of the TAA.

[17] The shortfall penalty for gross carelessness is considered in the Interpretation Statement: Shortfall Penalty for Gross Carelessness as published in *Tax Information Bulletin* Vol 16, No 8 (September 2004).

[18] *Case W4* (2003) 21 NZTC 11,034 at [44].

[19] *Case W4* at [60]; *Case 9/2014* (2014) 26 NZTC 2-019 at [88].

[20] *Case W4*; *Re Carlaw and FCT* 95 ATC 2166 (AAT); *Re Sparks and FCT* [2000] AATA 28 and see also *Pech v Tilgals* [1994] ATC 4206.

16. The penalty payable for gross carelessness is 40% of the resulting tax shortfall.

Shortfall penalty for not taking reasonable care

17. Section 141A imposes a shortfall penalty for not taking reasonable care on a taxpayer if the following requirements are satisfied:[21]
    - The taxpayer has taken a tax position.
    - Taking the tax position has resulted in a tax shortfall.
    - The taxpayer has not taken reasonable care in taking the taxpayer's tax position:[22]
        - The test of "reasonable care" is whether a reasonable person in the taxpayer's circumstances would have foreseen a tax shortfall as a reasonable probability. It is not a question of whether the taxpayer actually foresaw the probability.
        - Taking reasonable care includes exercising reasonable diligence to determine the correctness of a return. It also includes keeping adequate books and records to properly substantiate a return and generally making a reasonable attempt to comply with the tax law.
        - The "reasonable care" test does not require the commitment of unlimited time and money or other resources. The effort required of the taxpayer is commensurate with the reasonable person in the taxpayer's circumstances.[23]
18. The penalty payable for not taking reasonable care is 20% of the resulting tax shortfall.

Application of the penalties

19. Company X took a tax position that resulted in a tax shortfall. Company X is liable for evasion shortfall penalties because:
    - Company X had included some cash sales in most of its GST returns and accordingly knew that it was required to include cash sales in its GST returns.
    - Company X took deliberate steps to divert significant amounts of cash from the business by depositing cash into various bank accounts and ultimately into the bank accounts of the shareholders and the family trust.
    - Company X filed its GST returns without including an amount of cash sales knowing that the returns were incorrect, misleading and in breach of its tax obligations.
20. If it is concluded that the requirements of the evasion shortfall penalty are not satisfied, Company X is liable to shortfall penalties for gross carelessness. Depositing cash into bank accounts of persons other than Company X and not including these cash sales in its GST returns shows a complete disregard by Company X for the consequences of its actions. This factor created a high risk of the tax shortfalls occurring. That risk and its consequences would have been foreseen by a reasonable person in the circumstances.
21. Further, if it is concluded that the requirements of the gross carelessness shortfall penalty are not satisfied Company X is liable to shortfall penalties for not taking reasonable care. A reasonable person would have foreseen as a reasonable probability of not recording all income from its taxable activity, that a tax shortfall would arise.
22. Any shortfall penalties for which Company X is liable are reduced by 50% under s 141FB for previous behaviour.

[21] The shortfall penalty for not taking reasonable care is considered in the Interpretation Statement: Shortfall penalty for not taking reasonable care as published in *Tax Information Bulletin* Vol 17, No 9 (November 2005).

[22] *Case W4* (2003) 21 NZTC 11,034.

[23] See also *Case W3* (2003) 21 NZTC 11,014 and *TRA 007/12* [2014] NZTRA 08, (2014) 26 NZTC 2018.

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